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PAPERS

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CHILEAN ECONOMIC MEASURES

THE CHILEAN MINISTER OF FINANCE, SR HERNAN BUCHI, ANNOUNCED ON 4 JANUARY TWO MAJOR MEASURES DESIGNED TO STIMULATE THE ECONOMY AND ENCOURAGE EXPORTS.

THE GENERAL LEVEL OF TARIFFS IS REDUCED FROM 20 PER CENT TO 15 PER CENT, HAND IN HAND WITH A 4 PER CENT DEVALUATION AGAINST THE US DOLLAR, BRINGING THE RATE OF EXCHANGE ON 5 JANUARY TO 243.97 PESOS =US1 DOLLAR AGAINST 234.48 THE PREVIOUS DAY.

2. BECAUSE MANY CHILEAN EXPORTS HAVE A HIGH IMPORT CONTENT, SOMETIMES AS MUCH AS 50 PER CENT OF THE TOTAL VALUE, A REDUCTION OF 5 PER CENT IN TARIFFS IS EXPECTED TO GIVE A SIGNIFICANT BOOST TO EXPORTS, WHILE THE SIMULTANEOUS DEVALUATION SHOULD HELP TO PROTECT IMPORT SUBSTITUTION BY LOCAL INDUSTRY. HOWEVER FOLLOWING ON THE ABOLITION OF THE 50 PER CENT SPECIAL TAX ON LUXURY GOODS SUCH AS VIDEOS AND TELEVISION SETS ANNOUNCED IN DECEMBER, THE MEASURE WILL RESULT IN SIGNIFICANTLY LOWER PRICES FOR A RANGE OF CONSUMER GOODS. THIS IS OF COURSE AN ELECTORAL YEAR IN CHILE.

DURING HIS EXPLANATION OF THE MEASURES SR BUCHI WAS ABLE TO POINT TO A WHOLE RANGE OF HEALTHY SIGNS FOR THE CHILEAN ECONOMY. THE ECONOMY IS RECKONED TO HAVE GROWN BY 5.4 PER CENT IN 1987 AND PRIVATE INVESTMENT WAS UP BY 30 PER CENT. THE BALANCE OF PAYMENTS DEFICIT WAS EXPECTED TO BE US DOLLARS 890 MILLION AGAINST A FORECAST 950 MILLION WHILE THE TRADE SURPLUS WAS ESTIMATED AT 1,080 MILLION AGAINST 955 MILLION FORECAST. UNEMPLOYMENT IS DOWN TO 8.5 PER CENT IN NOVEMBER AND ALTHOUGH THE INFLATION RATE FOR 1987 WOULD BE RATHER HIGHER THAN FORECAST AT OVER 21 PER CENT BUCHI PLAYED UP THE DECEMBER FIGURE OF 0.3 PER CENT AS EVIDENCE OF AN IMPROVING TREND.

HE ALSO STRESSED THE SUCCESS OF CHILEAN EFFORTS TO DEAL WITH THE FOREIGN DEBT BURDEN. DEBT CAPITALISATION SCHEMES HAD ACCOUNTED FOR A

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FURTHER REDUCTION OF US DOLLARS 1,600 MILLION UP TO NOVEMBER 1987, BRINGING THE TOTAL SINCE THE SCHEMES STARTED OPERATING IN 1985 TO US DOLLARS 2,900 MILLION. THE MAJOR RECENT BONUS, HOWEVER, HAS BEEN THE DOUBLING OF THE WORLD COPPER PRICE, IT IS THIS AND THE LIKELIHOOD OF IT CONTINUING WELL INTO 1988 WHICH HAVE GIVEN THE CHILEAN GOVERNMENT THE FLEXIBILITY IT NEEDS TO UNDERTAKE THESE MEASURES.

MOST REACTIONS TO THE MEASURES HAVE BEEN POSITIVE. PRICES SHOT UP ON THE SANTIAGO STOCK EXCHANGE WHILE INTEREST RATES STARTED TO FALL. IMPORTERS AND EXPORTERS HAVE EXPRESSED THEIR SUPPORT, AND SOME ECONOMISTS SEE THEM AS BENEFICIAL, AT LEAST IN THE SHORT TERM, HELPING TO OFFSET THE EFFECT OF RECENT US ANTI- CHILEAN ACTIONS. FOR OTHERS, HOWEVER, THESE ARE INFLATIONARY MEASURES INTRODUCED FOR ELECTORAL PURPOSES, AND THE TEXTILE MANUFACTURERS FEAR THE INCREASE IN FOREIGN COMPETITION FOR THEIR PRODUCTS, REFERRING TO THE BAD OLD DAYS OF 1979 AND 1982 WITH UNRESTRICTED FOREIGN COMPETITION.

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INFO ROUTINE: DTI, OTD 4/2A-ECGD, LONDON-FCO, M+CAD- BANK OF ENGLAND
STAFF PRINCIPAL O'SEAS OFFICE, PANAMA CITY

QUOTE

COSTA RICA QUARTERLY ECONOMIC REPORT

OCTOBER-DECEMBER 1987

RATE OF EXCHANGE-OFFICIAL COLONES: 20 TO THE USDOLLAR

INTER-BANK COLONES: 68.75 BUYING

69.75 SELLING

IN 1987, COSTA RICA'S ECONOMY CONTINUED TO DISPLAY RESILIENCY, ALTHOUGH GROWTH WAS SLIGHTLY DOWN FROM 1986. SOME OF THE YEAR-END ESTIMATED LEADING ECONOMIC INDICATORS (1986 FIGURES IN PARENTHESES) WERE:

GROWTH IN GDP:	4034 :3,5 (4.2)
INFLATION RATE:	15-16 PER CENT (15.4)
CURRENCY DEVALUATION:	17.7 PER CENT (10.8)
UNEMPLOYMENT=	5 1/2-6 PER CENT (6.10)
IMPORTS:	USDOLLARS 1,360M (1160)
EXPORTS:	USDOLLARS 1,250M. (1074)

OTHER IMPORTANT ITEMS IN 1987 WERE:

COSTA RICA'S COFFEE QUOTA IN OIC INCREASED BY 15 PER CENT TO 2.46 PER CENT

18 MONTH STAND-BY AGREEMENT SIGNED WITH IMF

NON-TRADITIONAL EXPORTS REPRESENTED THE FASTEST GROWING REVENUE EARNING SECTOR

CONSIDERABLE TAX INCREASES: UNPROPERTY AND PROPERTY TRANSFERS, LAND, VEHICLE LICENSE AND TRANSFERS

STRONG POINTS OF ECONOMY: HOUSING AND INDUSTRY, WEAK SPOT:

AGRICULTURE

U.K. EXPORTS TO COSTA RICA: UP 20 PER CENT AGAINST 1986 AT STERLING POUNDS 14M (ESTIMATE)

SOME EXPECTATIONS FOR 1988:

AUSTERITY GENERALLY

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REDUCTION IN COMPANY TAX FROM 50 PER CENT TO 30 PER CENT
RESTRICTIONS ON SELECTED IMPORTS, PRINCIPALLY LUXURIES
GREATER EMPHASIS ON THE EXPORT DRIVE
FURTHER PARIS CLUB TALKS
NO NEW TAXES
BANK CREDIT TO BE RELAXED
STRONGER DEVALUATION/HIGHER INFLATION
FURTHER SLOWDOWN IN ENOMIC GROWTH
POSSIBILITY OF RE-INSTATEMENT OF PART OF RE-INSTATEMENT OF PA
OF US SUGAR
QOUTA LOST IN 1987
AN IMPROVED AND EXTENDED CARIBBEAN BAN INITIATIVE-CBI 11
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PLEASE NOTE THAT THERE IS NO Q.ER. FOR NICARAGUA.

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URUGUAY QUARTERLY ECONOMIC REPORT

RATES OF EXCHANGE AT 31 DECEMBER 1987

BUYING URUGUAYAN NEW PESOS 515.00 EQUALS POUNDS STERLING ONE.
SELLING URUGUAYAN NEW PESOS 532.70 EQUALS POUNDS STERLING ONE.

RECENT ANNOUNCEMENTS MADE BY GOVERNMENT OFFICIALS INDICATE THAT EXPORTS IN 1987 WOULD AMOUNT TO US DOLLARS 1,200 MILLION WHICH IS A SUBSTANTIAL INCREASE OVER 1986 FIGURES, US DOLLARS 1,087 MILLION. THIS ESTIMATED AMOUNT SHOWS THE DYNAMISM OF THE EXPORT ORIENTATED SECTOR, PARTICULARLY IN THE AREA OF NON-TRADITIONAL ITEMS WHICH, ACCORDING TO PROJECTIONS MADE BY GENERAL INDUSTRY WOULD ACCOUNT FOR 67 PER CENT OF TOTAL EXPORTS. ALTHOUGH THE TONNAGE EXPORTED DID NOT SHOW AN INCREASE IN 1987, BEEF AND WOOL PROVED GOOD INCOME EARNERS AS A RESULT OF IMPROVEMENT IN WORLD PRICES.

ECONOMIC INDEXES HAVE NOT SHOWN SUBSTANTIAL CHANGES IN THE QUARTER UNDER REVIEW. INFLATION FOR 11 MONTHS OF 1987 AMOUNTED TO 55.1 PER CENT (59.9 PER CENT FOR YEAR ENDING IN NOVEMBER) AND THE TOTAL ESTIMATED FOR 1987 IS 58 PER CENT WHICH IS IN LINE WITH GOVERNMENT'S REVISED FORECAST OF 60 PER CENT.

CENTRAL GOVERNMENT DEFICIT AMOUNTED TO 7.3 PER CENT OF SPENDING IN PERIOD JANUARY/NOVEMBER 1987. ALTHOUGH THIS COMPARES UNFAVOURABLY WITH 6.4 PER CENT IN SIMILAR PERIOD IN 1986, IT IS SLIGHTLY BETTER THAN THE 10 PER CENT IN PERIOD ENDING JULY 1987.

AT A PRESS CONFERENCE AT END OF THE YEAR PRESIDENT SANGUINETTI EMPHASISED THAT ALTHOUGH URUGUAY'S ECONOMY IS ON THE RIGHT TRACK, ESPECIALLY WHEN TAKING INTO CONSIDERATION THE ECONOMIC POSITION OF ITS NEIGHBOURS AND MAIN TRADE PARTNERS, COMPLETE RECOVERY IS STILL A LONG WAY OFF. AS A PROOF OF THE CONFIDENCE SHOWN BY THE URUGUAYAN PRODUCTIVE SECTOR IN THE GOVERNMENT'S ECONOMIC POLICY HE MENTIONED THE SUBSTANTIAL INVESTMENTS MADE IN INCREASING LAND

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DEVOTED TO LIVESTOCK PRODUCTION, FROM 110,000 HAS IN 1986 TO 202,000 HAS IN 1987 AND THE LARGE INCREASE IN THE IMPORTS OF CAPITAL GOODS FOR THE INDUSTRIAL SECTOR WHICH WENT FROM US DOLLARS 93 MILLION IN 1986 TO US DOLLARS 180 MILLION IN THE FIRST 10 MONTHS OF 1987.

THIS LATTER STATEMENT IS ALSO SUPPORTED BY REPORTS RECENTLY PUBLISHED BY MINISTRY OF INDUSTRY AND ENERGY INDICATING THAT THE TOTAL OF INVESTMENT PROJECTS APPLYING FOR BENEFITS UNDER DECLARATION OF NATIONAL INTEREST INCREASED BY 20 PER CENT COMPARED TO 1986, AMOUNTING TO APPROXIMATELY US DOLLARS 70 MILLION.

ON HIS RETURN FROM TOKYO MINISTER OF ECONOMY AND FINANCE SAID THAT JAPAN'S EXIMBANK WOULD BE PREPARED TO FINANCE, IN CONJUNCTION WITH WORLD BANK A US DOLLAR 160 MILLION FOR IMPROVEMENT OF URUGUAY'S TRANSPORT SYSTEM. ANOTHER JAPANESE FINANCING AGENCY IS PREPARED TO GIVE A LOAN OF US DOLLARS 50 TO 60 MILLION FOR A DEVELOPMENT PROJECT FOR INFRASTRUCTURE AND URBAN AREAS IN SOME UP COUNTRY REGIONS. IADB APPROVED A US DOLLAR 19.3 MILLION LOAN FOR AGRICULTURAL TECHNOLOGY GENERATION AND TRANSFER PROJECT TO BE EXECUTED BY THE MINISTRY OF LIVESTOCK, AGRICULTURE AND FISHERIES. IADB LOANS FOR URUGUAY AMOUNTED TO US DOLLARS 150 MILLION IN 1987, OF WHICH SOME US DOLLARS 54 MILLION HAVE ALREADY BEEN DEPOSITED DURING THE YEAR.

PARLIAMENT PASSED A LAW ON FREE ZONES IN DECEMBER. THE PROVISIONS OF THE NEW LAW PROVIDE WIDE SCOPE FOR INDUSTRIAL OPERATIONS IN THE FREE ZONES WITH AN AIM TO PROMOTE INWARD INVESTMENT.

BRITISH EXPORTERS MAY FIND OPPORTUNITIES, PARTICULARLY IN THE MANUFACTURING SECTOR AND DEVELOPMENT PROJECTS FINANCED BY INTERNATIONAL AGENCIES.

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BOLIVIA: QUARTERLY ECONOMIC REPORT (ENDING 31 DECEMBER 1987)

RATE OF EXCHANGE: BOLIVIANOS 3.96 TO ONE POUND AT 31 DEC.

1. ALTHOUGH THE RESULTS OF THE ECONOMIC REACTIVATION DECREE (NO. 21660) PUBLISHED IN JULY HAVE BEEN RATHER SLOWER TO MANIFEST THEMSELVES THAN HAD BEEN EXPECTED, THERE IS AN AIR OF CONFIDENCE FOR THE PREDICTED OUT-TURN FOR THE ECONOMY FOR THE END OF THE YEAR. INFLATION IS EXPECTED TO HAVE BEEN REDUCED TO 10.7 PER CENT, AND ECONOMIC GROWTH IS EXPECTED, WITH AN INCREASE OF 2 PER CENT OF GNP (BOLIVIA'S FIRST POSITIVE GROWTH FOR SIX YEARS). TOTAL EXPORTS ARE EXPECTED TO HAVE FALLEN BY AROUND \$100 MILLION - MAINLY DUE TO THE SITUATION IN THE MINING SECTOR WHERE THE GOVERNMENT HAS CLOSED 19 UNECONOMIC STATE MINES, BUT THERE HAS BEEN SIGNIFICANT GROWTH IN THE EXPORT OF NON-TRADITIONAL PRODUCTS ESPECIALLY OF TIMBER, GOLD, SILVER AND AGRICULTURAL PRODUCTS. GOVERNMENT INCOME FROM TAXATION AND CUSTOMS REVENUE INCREASED SUBSTANTIALLY AND IS ESTIMATED AT 600 MILLION BOLIVIANOS TO THE END OF THE YEAR. UNEMPLOYMENT REMAINS HIGH AT AROUND 21 PER CENT, ALTHOUGH THE SOCIAL EMERGENCY FUND HAS CREATED OVER 160,000 MAN/MONTH TEMPORARY JOBS.

2. THE GOVERNMENT'S MAJOR SOURCE OF INCOME CONTINUES TO BE THE SALE OF GAS TO ARGENTINA. DEFAULT BY ARGENTINA OF SOME \$53 MILLION DUE TO THE END OF THE YEAR IS A SOURCE OF CONCERN TO THE GOVERNMENT AND HAS CAUSED SOME LIQUIDITY PROBLEMS. THE NET FOREIGN EXCHANGE RESERVES ARE REPORTED TO HAVE FALLEN TO \$150 M. BOLIVIA HAS ENTERED INTO NEGOTIATIONS WITH BRAZIL ON THE SUPPLY OF GAS TO THE MATTO GROSSO AREA AND DISCUSSIONS ON THE SUBJECT ARE EXPECTED AT PRESIDENTIAL LEVEL IN THE FIRST QUARTER OF 1988.

3. AN IMF TEAM VISITED BOLIVIA IN DECEMBER TO NEGOTIATE A NEW 3 YEAR EFF. NEGOTIATIONS ARE EXPECTED TO BE CONCLUDED IN JANUARY.

4. THE GOVERNMENT IS CONTINUING ITS DRIVE AGAINST THE NARCOTICS TRADE. A NEW GOVERNMENT COMMITTEE ON DRUGS ABUSE AND TRAFFICKING WAS SET UP IN OCTOBER. OVER 1000 HECTARES OF COCA WERE ERADICATED

IN THE FINAL QUARTER OF THE YEAR, AND TOTAL DRUG SEIZURES FOR 1987 EXCEEDED 7 TONS. THE BOLIVIAN GOVERNMENT SIGNED AN AGREEMENT WITH THE US GOVERNMENT IN NOVEMBER ON A \$72 MILLION DEVELOPMENT PROGRAMME FOR THE CHAPARE REGION OF COCHABAMBA DEPARTMENT.

5. MUNICIPAL ELECTIONS WERE HELD THROUGHOUT BOLIVIA ON 6 DECEMBER. THE OPPOSITION PARTIES ADN AND MIR TOOK THE MAJORITY OF THE NATIONAL VOTES, WITH THE GOVERNMENT MNR PARTY COMING THIRD. THE ADN/MNR PACT FOR DEMOCRACY, WHICH GIVES THE GOVERNMENT THE SUPPORT IN PARLIAMENT OF THE LARGEST OPPOSITION PARTY, WAS REAFFIRMED IMMEDIATELY AFTER THE ELECTIONS.

6. FINAL FIGURES ON ANGLO BOLIVIAN TRADE ARE NOT YET AVAILABLE, BUT IT APPEARS LIKELY THAT BRITISH EXPORTS TO BOLIVIA WILL HAVE INCREASED SLIGHTLY OVER THE 1986 LEVEL. MANY MORE BRITISH COMPANIES ARE BEGINNING TO TAKE AN INTEREST AGAIN IN BOLIVIA, TAKING INTO ACCOUNT THE GRADUAL IMPROVEMENT IN THE ECONOMIC SITUATION.

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CHIEF SECRETARY	
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<i>Mrs Case</i>	
TO <i>EXIST Sir Geoffrey Lister</i>	
<i>Mr Hanson Mr Monck</i>	
<i>Mr Burgess Mr Monaghan</i>	
<i>Mr Robson Mr Turnbull</i>	

From the Private Secretary

13 January 1988

*Ms Seaman Mr G Th Jones
Mr Call*

CHILE: DEFENCE SALES

The Chilean Ambassador called on me this afternoon to deliver a letter (copy enclosed) from the Commander in Chief of the Chilean Navy to the Prime Minister about the supply of Sea Wolf. The burden of his message was that the Chilean Navy were very keen to purchase Sea Wolf but the price being quoted to them was impossibly high. Unless some reduction could be made, the Chilean Navy's long-standing links with the Royal Navy would be put at risk. The Ambassador said that Admiral Merino had also written to our Ambassador in Chile last November in the same sense.

I said that I knew nothing about the details but would enquire what the position was and draw the problem to the Prime Minister's attention. I would be in touch with him as soon as I had something to report.

I should be grateful if you and the Ministry of Defence could let me have advice both on the substance of a reply and on the most appropriate means for conveying it. I should like to be able to give the Ambassador here at least a preliminary response within a fortnight.

I am copying this letter to Ian Andrews (Ministry of Defence).

CHARLES POWELL

Lyn Parker, Esq.,
Foreign and Commonwealth Office.

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THE CHILEAN ECONOMY IN 1987

Summary

1. A good year, but the debt burden of the past still a heavy weight to bear. Balance of trade still favourable despite 28% growth in imports. Government quick to control interest rates, and preferring tax cuts to increases in public expenditure. Benefits of the rise in world prices for copper.

2. The privatisation programme continued and foreign investment grew with much Government encouragement. The UK did well with a big increase in exports and first Ministerial visit for four years. But much remains to be done to achieve potential in the Chilean market.

3. 1988 should be another good year, but much depends on factors outside Chile's control.

BRITISH EMBASSY
SANTIAGO

27 January 1988

The Rt Hon Sir Geoffrey Howe QC MP
LONDON

Sir

THE CHILEAN ECONOMY IN 1987

1. The World Bank has just issued a list of the 17 most indebted countries in the world (excluding the United States). Chile comes eighth with a total of US\$20,500 million, and has a vastly smaller population than any of those which appear above it: we believe Chile comes something like fourth in the debt per head of population stakes.

2. It is against this sombre background that we have to look at the highly successful performance of the Chilean economy in 1987. Run by an impressive team of technocrats along free market lines, the economy has done well recently, and has every prospect of continuing its steady growth in the short term. But it is still essentially a balancing act. Changes in the international economic situation or in the prices of copper and oil, a wave of protectionism or politically inspired boycotts in the United States, are among factors which could push this country into economic crisis again.

3. Nevertheless, 1987 saw a continuation of steady growth and all the repayment conditions of the international monetary institutions were met. GDP went up by 5.4%, retail price inflation at 21% was kept within reasonable bounds, the overall level of debt was slightly reduced by use of debt capitalisation and other debt reducing programmes, and Chile achieved an export surplus of US\$1,079 million. The agreement in December to grant the third stage of the World Bank's Structural Adjustment Loan reflected international confidence in the management of the economy, which has met all its IMF commitments and is indeed regarded by Chile's creditor banks as the best run in South America.

4. The main planks of the Government's policy continued to be export-led growth; fiscal rectitude and restrictions on Government expenditure leading to lower taxation; a continuing reduction in the size of the public sector; and the encouragement of foreign investment.

/5.

5. Exports increased by 20.2% in 1987 over 1986, largely due to increases in non-traditional sectors such as fruit and manufactured products. The old mainstay, copper, benefited from the doubling of the world price later in the year, but copper exports in volume remained constant. Imports in 1987 on the other hand rose by 28%, partly due to the increased price of oil earlier in the year, but partly also to greater purchases of capital goods, a sign that Chile is investing in the future. Despite this adverse movement the authorities are well satisfied with the trade situation and look to a much lower rise in imports in 1988.

6. Mr Büchi's declared aims for 1987 included further reduction in the size of the fiscal deficit, and this was achieved, with a Public Sector Borrowing Requirement likely to come out at around 0.8% of GDP. With increased income from the higher world copper price producing around US\$260 million and more tax income from greater economic activity, the Government has preferred to concentrate on reducing tax levels rather than increasing public expenditure. The 1988 Budget is essentially conservative with expenditure remaining constant in real terms. The reduction in general tariff levels from 20% to 15% announced at the beginning of 1988 is intended to stimulate exports.

7. Slackness in the control of interest rates at the beginning of 1987 led to some over-heating (the growth rate for the first quarter was 8.1%). But quick action in March-April pushed up interest rates and resulted in a sharp reduction to more sustainable levels.

8. The privatisation programme was vigorously promoted throughout the year. Three firms, including the steel company CAP, moved from partial to full private ownership. A nitrate company, Soquimich, a coal mine Schwager, the monopoly sugar refinery IANSA, and the electricity generating company ENDESA all moved some way down the road. The most significant was the agreement to allow the Australian Bond Corporation to buy 30% of the Compañía de Teléfonos de Chile, with an option on another 17%, the first time a foreign company has been allowed such a position in a public utility. Further privatisations including the state airline LAN Chile and the remainder of the coal mining sector are planned for 1988. The Government has made much of the parallels between its activity in this field and that of the UK Government, which are widely admired here.

9. Total foreign investment reached US\$1,170 million in 1987. The largest operation also belonged to the Bond Corporation which paid US\$500 million for the El Indio gold mine. We still await final decisions on the major prospective UK investment, RTZ's 30% share of the US\$1.1 billion La Escondida copper mine, but Shell and Unilever have been among British companies who expanded their operations in Chile last year.

/Also

Also worthy of note were moves by New Zealand companies into the timber and fruit farming sectors. Despite official discouragement, culminating in the removal of new investments in Chile from cover by the Overseas Private Investment Corporation, there seemed to be no slacking in US enthusiasm for investment in Chile, and the Japanese were also active. It is instructive that foreign investors do not seem to be concerned about political uncertainties.

10. Although the inflation rate at 21.5% was higher than expected, a more important result for a Government facing an election year was the continued reduction in unemployment. Although the overall unemployment rate only fell from 8.8% to 8.5% over the year to November, there was a much bigger drop in the numbers taken up by the Government's make-work programmes, implying a steady shift to permanent employment with 209,000 new jobs created. But there was virtually no movement in the level of real wages in 1987 and public sector salaries are likely to show a fall in real terms.

11. The UK has had a good year in Chile. ECGD lifted its limits on coverage, and British companies at last seem to be taking note of the opportunities. Our exports to November were up by 65% over the same period of 1986. With Chilean exports to the UK down somewhat on previous years we have for the first time achieved near parity. But with only slightly more than 3% of total Chilean imports, there is still a long way to go to achieve our full potential in this market.

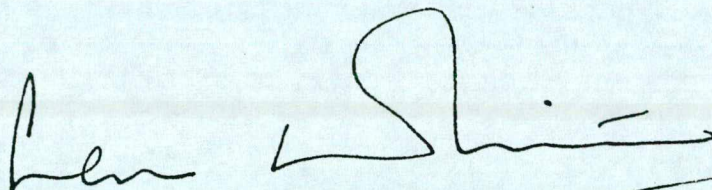
12. It was gratifying that the first Ministerial visit here for four years was by the Minister for Trade (to be followed early in 1988 by the Minister of State for Agriculture). The record of six Outward Missions (including two with more than 30 participants) is already overshadowed by the eight scheduled for 1988. What is needed is the impact of one really big contract. The main hope in this direction is the US\$100 million Biwater/Halcrow tender for a sewage works for Santiago for which a key element is likely to be ATP support. I hope that DTI and ODA will be willing to make a positive decision on this application when it comes. This is not only a worthy project in itself, benefitting the poorest areas of population, but a lead-in to work which could be worth \$2,000 million over the next 20-30 years.

13. The prospects for 1988 are for continued steady growth. Much will depend on external factors, but if the copper price holds up and there is no catastrophic loss of foreign confidence in the country, there seems every prospect of Mr Büchi meeting his targets: GDP growth in the 3-5% range, a higher increase in exports than in imports, inflation around 17%, real wages showing little change and a further reduction in unemployment. Whether internal political factors will affect this scenario remains to be seen.

/14.

14. I am sending copies of this despatch to the Chancellor of the Exchequer, HM Treasury, Secretary of State for Trade and Industry, and to the Bank of England.

I am, Sir
Yours faithfully

A handwritten signature in black ink, appearing to read 'Alan White', written in a cursive style. The signature is positioned above a horizontal line that underlines the printed name below.

ALAN WHITE

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10 DOWNING STREET
LONDON SW1A 2AA

CH/EXCHEQUER	
REC.	16 FEB 1988
ACTION	PS/EST
COPIES TO	Sir G. LITTLE
	Mr LANKESTER
	Mr MOUNTFIELD
	Mr P.G.F. DAVIS

From the Private Secretary

15 February 1988

Handwritten initials

Dear Sir,

PRIME MINISTER'S MEETING WITH THE PRIME MINISTER OF MAURITIUS

The Prime Minister had a meeting this morning with the Prime Minister of Mauritius. Mr. Jugnauth was accompanied by the High Commissioner for Mauritius and a Private Secretary.

Mauritian economy

The Prime Minister said that the Mauritian economy seemed to be doing very well. It was good to see a country succeeding by its own efforts. Mr. Jugnauth confirmed that things were going well, mentioning electronics and textiles as areas of successful growth. Mauritius hoped to expand also into offshore banking and duty free shopping. Indeed, they intended to present themselves as a shopping paradise. Nonetheless, Mauritius still needed help in a number of areas. One was training. The High Commissioner has already mentioned to the Prime Minister Mauritius' hopes that we would look again at the question of student fees. They also hoped that we could increase the number of laureates from 16 to 18. The Prime Minister said that we would look at this. Mr. Jugnauth would discuss it further with Mrs. Chalker and Lady Hooper.

Air Services

Mr. Jugnauth raised the question of Mauritius Airways' desire to start a service to the Gulf. British Airways were being very difficult about this. It had always been understood on the Mauritian side that they would eventually have reciprocal rights. He hoped that the Prime Minister would take a direct interest in the matter and persuade British Airways to be more reasonable. Otherwise Mauritius would have no alternative but to fall back on the previous Air Services Agreement which would restrict British Airways' services. The Prime Minister said that Mr. Jugnauth should discuss this further with Lord Brabazon. Mr. Jugnauth said that he would do so but would wish to leave the Prime Minister in no doubt of his strong feelings on the matter. British Airways were being very unfair.

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Bilateral Relations

Mr. Jugnauth very much welcomed the British Council's return to Mauritius. He spoke of plans to modernise the tea industry while reducing production. Mauritius needed technical help with this. He also recalled that Mauritius relied on Britain's support in maintaining the Lomé sugar arrangements.

Diego Garcia

Mr. Jugnauth said that people would ask whether he had raised the matter of Diego Garcia. So he must do so, although he had nothing particular to say. The Prime Minister said that she understood this. There was no change in the present position. Mr. Jugnauth said there were rumours in Mauritius of a re-negotiation between the United States and the United Kingdom of the terms of the US lease of facilities there. The Prime Minister said that she knew of no such re-negotiation.

Fiji

Mr. Jugnauth sought the Prime Minister's assessment of developments in Fiji and the prospects for restoring democracy. The Prime Minister said that the Fijians needed time to sort out their problems. Their aim seemed to be to get back to a democracy within two years but they seemed at a loss how to do so. She hoped to see Ratu Mara in the spring.

South Africa

Mr. Jugnauth gave an account of his talk with Foreign Minister Botha who had attended a service in Mauritius for the victims of the South African Airways disaster. He had urged him to move faster in dismantling apartheid. Botha told him that the South African government recognised that apartheid was out-dated. But change would take time. The government was under pressure from the extreme right and had to move slowly. The Prime Minister gave Mr. Jugnauth an account of her views on South Africa.

Possible Loan to Mauritius

Mr. Jugnauth said that Mauritius had earlier been offered a £12 million loan by ODA at 10.5 percent interest repayable over five years. They did not feel they could afford to take this up. He wondered whether the Prime Minister could offer softer conditions, for instance interest of 5 percent and repayment over 15 years. The Prime Minister said that she thought this would be very difficult. But she would ask for a report from the Minister for Overseas Development

Bank of Mauritius

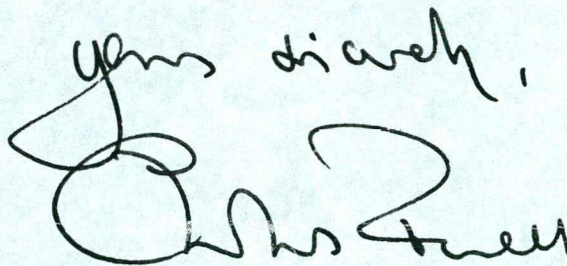
Mr. Jugnauth said that the Bank of Mauritius was trying to open an office in London but were encountering various obstacles (which he did not define). He would be grateful for help in overcoming these. The Prime Minister said that she

was not informed of this but would establish whether Treasury Ministers were aware of the problem.

Possible Visit to Mauritius

Mr. Jugnauth said that he hoped the Prime Minister would find time to visit Mauritius. The Prime Minister said she would like to do so although it was not exactly on the way to anywhere. Mr. Jugnauth said that he had heard that the Prime Minister might visit Southern Africa next year, in which case he hoped that she might include Mauritius. The Prime Minister said that she would keep this in mind.

I am copying this letter to Alex Allan (HM Treasury), Alison Brimelow (Department of Trade and Industry) Roy Griffins (Department of Transport) and Myles Wickstead (Overseas Development Administration).

Yours sincerely,


(C. D. POWELL)

Lyn Parker, Esq.,
Foreign and Commonwealth Office.

UNCLASSIFIED



FROM: P D P BARNES
DATE: 16 February 1988

NOTE OF A MEETING HELD IN ROOM 51/2, TREASURY CHAMBERS, PARLIAMENT STREET AT 11.30 am ON FRIDAY 12 FEBRUARY

Those present: Economic Secretary
Mr S Matthews
Mr Liikanen, Finance Minister of Finland
His Excellency Iikka Pastinen, Finnish Ambassador

ECONOMIC SECRETARY'S MEETING WITH THE FINNISH FINANCE MINISTER

The Finnish Finance Minister explained that he was in London to give a couple of lectures on the Finnish economy. He was grateful to the Economic Secretary for agreeing to see him.

2. Mr Liikanen said that the Finnish economy was in good shape. Inflation was under control, and the economy was growing at about 3% a year. Their ratio of public debt to GDP, at 15%, was below that for other Scandinavian countries. Mr Liikanen said that their main problem was that people might start taking this rate of growth for granted.

3. Mr Liikanen said that Finland had been surprisingly little affected by the fall in financial markets in October. Finland was in the process of deregulating its markets to encourage international investment, since at the moment foreigners could buy only up to 40% of shares on the Finnish stock market. The Finns had still not adjusted to the absence of effective controls on borrowing and there were occasional worries about the increase in bank lending which had obliged the authorities to impose restrictions on the take-up of loans.

4. On international relations, Mr Liikanen said that the Finns were watching closely the moves towards an internal market in the European Community. They had no present plans of applying for membership of the European Community. But they were working within EFTA to ensure that there were no barriers to trade with the European Community.

5. On fiscal matters Mr Liikanen said that their main aim was to reform direct taxes. 25 separate tax concessions limited their tax base and meant that marginal rates had to be kept high. But they had a political problem in altering this state of affairs, since tax changes required a two-thirds majority in the Finnish Parliament. Radical changes were also handicapped by the relatively open Budget-making process, and the extreme difficulty of preventing other Ministries from divulging confidential information to the press. Apart from income tax, the Finns were also considering action on the excessive encouragement which the taxation system gave to house purchase.

6. Mr Liikanen's questions about the UK centred on the likely trend for UK interest rates, and the likely contents of the Budget. The Economic Secretary answered along standard non-committal lines.

RB

P D P BARNES

Private Secretary

cc PS/Chancellor 2
PS/Sir P Middleton
Sir G Littler
Mr Lankester
Mr H Evans
Mr Matthews
Mr Savage

FROM: AMANDA HIGGINS

DATE: 26 February 1988

1. MR MOUNTFIELD ^{RA}
2. ECONOMIC SECRETARY

cc PS/Chancellor
Mr Evans
Mrs Case
Mrs Thomson

VISIT OF PHILIPPINE FINANCE MINISTER AND CENTRAL BANK GOVERNOR

You have agreed to see Messrs Jayme (pronounced HI MAY) and Fernandez on 1 March at 4.30pm. They will be accompanied by Mr Quimson, the Philippine Ambassador. Mr Mountfield will support you at the meeting and will brief you orally at 4.15pm.

2. Messrs Jayme and Fernandez will have spent the week of 20-26 February at a conference in Oxford to discuss "Trends in International Capital Markets: Implications for developing countries". Jayme was due to speak on 23 February on debt/equity matters. On 29 February they will call on Lloyds and Midland banks and Mrs Chalker. On 1 March they will have seen Nat West, ECGD, the Governor and Barclays before you.

3. Their call will provide an opportunity for us to stress the need to adhere strictly to their IMF programme and to stick to the straight and narrow on debt. The Philippine Congress will be pressing for a renegotiation of the recent commercial bank rescheduling agreement later this year. They have asked to discuss International Debt and (if time allows) our experience of privatisation.

4. Your brief consists of

- (i) Line to take
- (ii) Background note on Philippine Economy and Political Situation
- (iii) Note on International Debt
- (iv) Note on privatisation (to follow)
- (v) Personality Notes on Jayme, Fernandez and Quimson.

Amanda Higgins

AMANDA HIGGINS
AEF/2

LINE TO TAKE

1. Commend visitors on progress made so far under IMF Standby Arrangement and emphasise need to adhere to it. We will support requested extension in the Fund Board.
2. Glad United Kingdom able to participate in Paris Club rescheduling last year. Do visitors think a further rescheduling will be needed in 1988?
3. Believe you are considering a "Mexican" type debt scheme - we would be interested in your ideas.

[IF RAISED]

4. [The Phillipines have an obsession with reducing the interest rate charged on rescheduled debt and might seek to reopen last year's commercial bank agreement.]

Cannot intervene in the commercial decisions of UK banks. However do not think it a good idea to try to reopen last year's agreement.

PHILIPPINE ECONOMY

1. The main challenge for the Aquino administration has been to achieve sustained recovery from the Marcos years of misplaced investment and political cronyism. The high external debt (\$29 billion, with a debt service ratio of around 35 per cent) gives little room for manoeuvre. A debt crisis in late 1983 necessitated adjustment policies which eliminated an unsustainable current account deficit and reduced inflation but which resulted in a fall in output. The fall in income per head has been severe, about 70 per cent of the population are thought to be living below the poverty level.

2. In October 1986 the IMF Board approved an 18 month SBA which has stimulated renewed growth. The government has initiated tax reform, abolished monopolies in sugar and coconut markets, and removed some import controls. There has been little progress on the land reform programme, which might help to win rural support away from the communist insurgency. The last two purchases under the SBA have not been made because some performance criteria for September (floor on net international reserves (NIR) of the monetary authority) and December 1987 (NIR floor and the ceiling on base money) were not met. A Fund mission visited Manila in January and the Philippines have requested a 4 month extension to the programme to make it operational again.

3. In January 1987 the Paris Club rescheduled maturities falling due until mid-1988. Late last year 483 commercial bank creditors rescheduled \$13.1 billion of the country's \$28 billion debt. In 1988 the Philippines is due to pay \$2.3 billion of its expected export earnings of \$6-7 billion in debt service. Foreign reserves are low - less than \$1.8 billion - about 3½ months of imports. It is expected that the Philippines will seek further rescheduling in 1988.

4. In 1987, the debt/equity scheme was very successful, about \$155 million was converted. Both visitors are said to be interested in a "Mexican" type scheme. There have been suggestions that they should use negotiations over the US basis as a lever to extract a similar deal. They will have discussed this earlier with the Governor.

5. ECGD have not yet signed their bilateral from last year's Paris Club multilateral agreement. The Philippines have proposed that interest is charged at Treasury Bills +0.5 per cent instead of LIBOR +0.5 per cent. At present rates this would work out cheaper in the short term. ECGD will be discussing this earlier in the day. They are prepared to accept this offer, if the Philippines insist and if their finance people are satisfied that ECGD will cover its costs. I will let you have a report on the outcome of this meeting before your own meeting.

6. Detailed privatisation plans have been prepared for about 56 public corporations whose disposal has already been approved. One has already been sold. Privatisation of a further 35 corporations awaits Presidential approval.

dti

the department for Enterprise

The Hon. Alan Clark MP
Minister for TradeThe Rt Hon The Lord Belstead JP
Lord Privy Seal and Leader of the
House of Lords
Privy Council Office
Whitehall
LONDON
SW1A 2AT**Department of
Trade and Industry**1-19 Victoria Street
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01-215 7877Telex 8811074/5 DTHQ G
Fax 01-222 2629

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Date | March 1988**KOREA: SUSPENSION OF GSP BENEFITS**

I understand that on current plans the technical Statutory Instrument suspending Korea's ECSC GSP benefits will be taken on the floor of the House of Commons at 10.00pm on Monday 7 March. This is not because of any great interest in the issue, but rather reflects the inability of the Opposition Whips to realise this in time for it to be taken in Standing Committee.

However I propose that we should make a virtue of this by dealing with the Scrutiny Committee's request that we debate the substance of suspension of Korea's GSP benefits at the same time. The relevant reports are HC43-x and HC43-xiv both of the 1987-88 session. The matter is procedurally complicated because the Scrutiny Committee have recommended for joint debate on the floor of the House on the basis of unnumbered explanatory memoranda both the withdrawal of EEC benefits (which did not require secondary legislation), and the withdrawal of ECSC benefits (which required the affirmative resolution SI which is the cause of the need now for any debate). Because the SI refers only to ECSC benefits I understand we cannot "tag" the EEC suspension to the motion approving the SI.

I propose that the substantive debate meet the Scrutiny Committee's needs and be on the Motion:

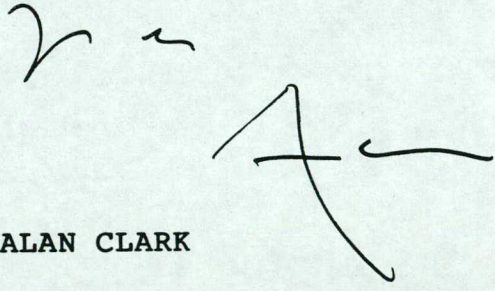
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"That this House takes note of European Community documents 10318/87 and 4406/88 on the suspension of the Republic of Korea's benefits under the European Community Generalized Scheme of Benefits; and supports the Government's aim to achieve equality of treatment in the Republic of Korea between EC and US firms in the field of intellectual property rights".

Following that debate and any vote on that motion I would hope we could then put the SI technical approval directly to the vote that night and without further debate. Given the Opposition's lack of interest in the subject you may feel that this can be arranged easily through the normal channels. Alternatively a business motion could be tabled beforehand that the motion confirming the ECSC order be put forthwith.

I hope you agree that either of these would provide a useful opportunity to discharge two obligations in a single debate.

I am copying this to members of L and OD(E) Committees, and to Sir Robin Butler.



ALAN CLARK

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UKREP FOR PAKENHAM, UKMIS FOR DELL

CHILEAN APPLES

THE CHILEAN AMBASSADOR DELANO CALLED ON OWEN YESTERDAY TO REGISTER CONCERN OVER THE COMMISSION'S DECISION TO SUSPEND LICENCES FOR CHILEAN APPLES FROM 18-29 APRIL. HE WANTED TO KNOW WHAT WOULD HAPPEN WHEN THE TEMPORARY SUSPENSION EXPIRED. HE ALSO ENQUIRED HOW UNLICENSED APPLES CURRENTLY ON THE HIGH SEAS WOULD BE TREATED ON ARRIVAL AT EEC PORTS.

Pirates perhaps??

2 DELANO SAID THAT IN AN ATTEMPT TO INCREASE THEIR FOREIGN EARNINGS AND THEREBY REDUCE THEIR FOREIGN DEBT BURDEN THE CHILEANS HAD INVESTED HEAVILY IN AGRICULTURE. THEY HAD DONE SO IN THE EXPECTATION THAT THE EEC WOULD REMAIN AN OPEN MARKET TO THEM AS CHILE WAS FOR THE EEC. THE COMMISSION'S ACTION NOT ONLY THREATENED LIVELIHOODS IN CHILE BUT WAS SEEN AS THE THIN END OF THE WEDGE. WHAT WAS THERE TO PREVENT THE EC EXTENDING THE REGIME TO OTHER COMMODITIES SUCH AS PEACHES AND GRAPES? CHILE COULD NOT AGREE TO A QUOTA SYSTEM. IT DID NOT OPERATE ONE AND SOUGHT TO REGULATE THE CHILEAN MARKET THROUGH AN IMPORT TARIFF. WHY COULD THE EC NOT DO THE SAME?

3 IN REPLY OWEN SAID WE SHARED THE AMBASSADOR'S CONCERN. WE HAD EXPRESSED CONCERN ABOUT THE COMMISSION'S DECISION TO INTRODUCE LICENCES FOR MONITORING PURPOSES LAST FEBRUARY. WE HAD REITERATED OUR VIEWS LAST WEEK IN BRUSSELS WHEN THE TEMPORARY SUSPENSION WAS ANNOUNCED. WE HAD ALSO COMPLAINED AT THE HASTE WITH WHICH IT HAD BEEN INTRODUCED. WE WERE NOT CONVINCED THAT SUCH ACTION WAS NECESSARY AT PRESENT. NOR DID WE WELCOME THE PROSPECT OF A GATT DISPUTE. WE WOULD PREFER TO SEE AGREEMENT BETWEEN THE EEC AND CHILE OVER THE LEVEL OF SENDINGS AS THIS WOULD PERMIT STEADIER MARKETING. HOWEVER IT HAD TO BE SAID THAT THE LEVEL OF CHILEAN SENDINGS HAD NOT HELPED MATTERS AND THAT THE EC HAD ACTED PROPERLY WITHIN THEIR COMPETENCE.

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4 OWEN TOLD THE AMBASSADOR WE COULD NOT AT PRESENT ANSWER HIS QUESTIONS ON EVENTS AFTER 29 APRIL NOR ON THE POSITION ON APPLES IN TRANSIT. WE WOULD ENDEAVOUR TO CLARIFY. WHAT ACTION DID CHILE INTEND TO TAKE IN GATT? DELANO WOULD NOT BE DRAWN OTHER THAN TO SAY THAT CHILE WOULD NOT ACCEPT QUOTAS.

5 THE MEETING WAS HELD IN A CORDIAL ATMOSPHERE.

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INFO PRIORITY PRETORIA

Pa. Mu 27/4

FRAME AGRICULTURE

EC AND CHILEAN APPLES

1. WE UNDERSTAND THAT COMMISSION AGREED INTERNALLY ON 20 APRIL ON A REGULATION LIMITING IMPORTS OF DESSERT APPLES FROM SOUTHERN HEMISPHERE AND OTHER EXPORTERS TO THE EC MARKET OUT OF SEASON, UNTIL 31 AUGUST 1988. THIS SETS INDIVIDUAL TONNAGE QUOTAS FOR CHILE, NEW ZEALAND, AUSTRALIA, ARGENTINA, SOUTH AFRICA, WITH A SEPARATE JOINT QUOTA FOR OTHER SUPPLIERS. AT PRESENT THE QUOTAS WHICH ARE BASED ON TRADITIONAL TRADE FLOWS, ARE UNLIKELY TO RESTRICT SENDINGS, EXCEPT FROM CHILE WHICH HAS ALREADY EXCEEDED THE PROPOSED QUOTA. NEW ZEALAND MAY BE AFFECTED LATER THIS YEAR. MEMBER STATES HAVE 3 WORKING DAYS IN WHICH TO OBJECT (IE THE DEADLINE IS MONDAY EVENING, 25 APRIL).

2. THE COMMISSION ACTION DOES NOT APPEAR TO BE ULTRA VIRES. ALTHOUGH THEY CLAIM IT IS IN CONFORMITY WITH GATT, IT IS CONTRARY TO THE SPIRIT OF THE STANDSTILL COMMITMENT AT PUNTA DEL ESTE.

3. WE ARE CONSIDERING WHETHER TO OBJECT ON TRADE POLICY GROUNDS. IT WOULD BE HELPFUL TO KNOW WHETHER OTHER MEMBER STATES (IE FRG, NETHERLANDS, DENMARK, BELGIUM, SPAIN) INTEND TO DO SO. (FRG, SPAIN AND NETHERLANDS EXPRESSED DOUBTS ABOUT COMMISSION ACTION TAKEN SO FAR, IN ARTICLE 113 COMMITTEE ON 15 APRIL.) THE FOREIGN AFFAIRS COUNCIL ON MONDAY 25 APRIL WOULD PROVIDE AN OPPORTUNITY (UNDER OTHER BUSINESS).

4. GRATEFUL IF YOU WOULD SPEAK TO CONTACTS FROM THESE 5 COUNTRIES IN BRUSSELS TO ASCERTAIN THEIR VIEWS. WE ARE UNLIKELY TO RAISE THIS ISSUE AT THE FOREIGN AFFAIRS COUNCIL UNLESS OTHERS ARE PREPARED TO DO SO. INFORMATION ADDRESSEES IN EC POSTS HAVE DISCRETION TO RAISE THE QUESTION WITH HOST GOVERNMENTS.

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INFO PRIORITY WELLINGTON

FRAME EXTERNAL AND AGRICULTURE

GATT: EC-SOUTHERN HEMISPHERE APPLES: IMPORT LICENSING COMMITTEE.,
21 APRIL

SUMMARY

1. CHILE WITH STRONG SUPPORT ATTACKED EC ACTION AS CONTRARY TO IMPORT LICENSING CODE. EC WAS UNREPENTANT AND ANNOUNCED GENERAL QUOTAS ON SOUTHERN HEMISPHERE SUPPLIERS.

DETAIL

2. THE ROUTINE MEETING OF THE GATT IMPORT LICENSING COMMITTEE ON 21 APRIL GAVE CHILE THEIR FIRST CHANCE TO COMPLAIN ABOUT THE EC'S SUSPENSION OF IMPORT LICENCES FOR CHILEAN APPLES. THEY ARGUED THAT THE EC HAD CONTRAVENED ARTICLE 2 OF THE CODE: AUTOMATIC LICENSING PROCEDURES SHOULD NOT HAVE A RESTRICTIVE EFFECT ON IMPORTS. THE EC LICENSES WERE IN FACT DISCRETIONARY AND THEREFORE SHOULD BE NOTIFIED TO THE GATT. THE EC HAD ALSO RENEGED ON ITS URUGUAY ROUND STANDSTILL COMMITMENT. AUSTRALIA, NEW ZEALAND, US, HUNGARY AND CANADA SUPPORTED.

3. STADLER (LOCAL COMMISSION) REJECTED CHILE'S COMPLAINT. THE EC HAD RESPECTED THE IMPORT LICENSING CODE. IN ANY CASE IT WAS NOT THE APPROPRIATE FORUM TO DISCUSS THE QUESTION SINCE THE COMMISSION HAD INTRODUCED GENERAL QUOTAS FOR APPLES FROM VARIOUS SOUTHERN HEMISPHERE PRODUCERS. THESE WOULD BE NOTIFIED TO THE GATT SOON. STANDSTILL HAD NOT BEEN BREACHED SINCE IT DID NOT PREVENT NEW MEASURES JUSTIFIED UNDER GATT RULES.

4. ARTICLE XXIII CONSULTATIONS ON THIS ISSUE ARE TAKING PLACE HERE TODAY (22 APRIL) AND WILL BE REPORTED SEPARATELY.

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FRAME EXTERNAL

MY TELNO 224: GATT: EC/CHILAN APPLES - ARTICLE XXXII.1
CONSULTATIONS, 22 APRIL 1988

SUMMARY

1. LOW-KEY FIRST ROUND WAS ENTIRELY EXPLORATORY AND PRODUCED NOTHING NEW. CHILE WAS RESTRAINED BUT LIKELY TO ASK FOR GATT PANEL AT MAY COUNCIL. IN COORDINATION COMMISSION INSISTED ON ARTICLE XI DEFENCE DESPITE RESERVATIONS FROM UK AND NETHERLANDS. COMMISSION TO NOTIFY MEASURES UNDER ARTICLE XI. NEW ZEALAND HAVE NOW ASKED FOR SIMILAR CONSULTATIONS.

DETAIL

EC COORDINATION

2. DISCUSSION FOCUSED ON THE GATT JUSTIFICATION FOR THE EC QUOTAS. DE PASCALE (COMMISSION) PROPOSED THAT THE EC SHOULD USE ARTICLE XI. HE BELIEVED THAT THIS WAS A BETTER BET THAN ARTICLE XIX. IT WOULD AVOID THE PROBLEM OF COMPENSATION AND HE DOUBTED THAT THE SURGE IN IMPORTS WAS SUFFICIENT TO JUSTIFY ARTICLE XIX. FURTHER THE 1979 EC/CHILE PANEL ON A SIMILAR EC QUOTA SET A USEFUL PRECEDENT SINCE IT HAD IN EFFECT SANCTIONED THE EC REGIME TO INVOKE ARTICLE XI. HE EXPLAINED THE HE WAS UNDER INSTRUCTIONS TO NOTIFY EC ACTION TO THE GATT UNDER ARTICLE XI.

3. UK WITH STRONG SUPPORT FROM THE NETHERLANDS EXPRESSED CONCERN THAT THE 113 COMMITTEE HAD NOT HAD TIME TO DISCUSS THE TRADE POLICY ASPECTS OF THE COMMISSSION ACTION. IT WAS ALSO UNFORTUNATE THAT IT WAS ONLY AFTER IMPLEMENTATION THAT THE COMMISSION STARTED TO DISCUSS HOW TO JUSTIFY THE QUOTAS IN GATT. IT WAS CLEAR THAT THE FC ACTION WOULD PROVOKE A STRONG REACTION IN GATT AND WOULD BE SEEN AS A BREACH OF STANDSTILL IN SPIRIT, IF NOT LETTER. BOTH THE UK AND NETHERLANDS HAD DOUBTS ABOUT ARTICLE XI. IT WAS RAPIDLY BECOMING A CONTROVERSIAL ARTICLE. RECENT PANELS HAD INTERPRETED IT STRINGENTLY. THE MAIN DIFFICULTY WAS THE PROPORTIONALITY OF

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IMPORTS TO DOMESTIC PRODUCTION. WOULD THE EC CASE STAND UP ON PROPORTIONALITY? ARTICLE XIX MIGHT BE MORE APROPRIATE. THE COMMISSION HAD CLAIMED A SUDDEN SURGE IN CHILE IMPORTS AS JUSTIFICATION FOR THEIR ACTION. IF THIS WAS THE CASE ARTICLE XIX WAS DESIGNED FOR SUCH EMERGENCY ACTION. IN ANY EVENT THE MAIN POINT WAS THAT THE EC SHOULD BE SURE IT CHOSE THE BEST GATT DEFENCE. FRANCE ARGUED STRONGLY FOR ARTICLE XI. MOST OTHER MEMBER STATES WERE SILENT.

4. DISCUSSION WAS LARGELY SUPERFLUOUS SINCE IT BECAME CLEAR THE COMMISSION HAD THE POWER TO NOTIFY THE QUOTA UNDER ARTICLE XI WITHOUT MEMBER STATES' ENDORSEMENT. DE PASCALE WAS SENSITIVE TO THE UK CONCERN ON PRIOR ARTICLE 113 DISCUSSION. IT WAS HOWEVER FINALLY ACCEPTED THAT DE PASCALE WOULD NOIFY UNDER ARTICLE XI. THE PRESIDENCY WOULD ADD THE ISSUE TO THE AGENDA FOR 113 DEPUTIES ON 29 APRIL.

CONSULTATIONS

5. BARRAS (AMBASSADOR) LED THE CHILE DELEGATION OF FIVE INCLUDING THEIR EC AMBASSADOR. HE PRESENTED THE CHILE COMPLAINT CALMLY (FULL TEXT MUFAXED TO MAFF) AND AVOIDED A CONFRONTATIONAL APPROACH. IT WAS DISAPPOINTING THAT THE EC HAD CLOSED THE DOOR ON A MAJOR CHILEAN EXPORT AS SHE STRUGGLED TO EXPAND EXPORTS TO PAY OFF ITS DEBT. THIS WOULD SERIOUSLY DAMAGE CHILEAN PRODUCTION AND EMPLOYMENT. THEY HAD INSCRIBED A REQUEST FOR A PANEL ON THE MAY GATT COUNCIL ONLY AS A PRECAUTION. DESPITE EC ASSURANCES IN THE GATT THEY HAD NOW IMPOSED QUOTAS ON CHILE EXPORTS. AT FIRST THESE HAD BEEN DISCRIMINATORY. THEY WERE CONTRARY TO THE EC STANDSTILL COMMITMENT AND THE GATT. THE EC SHOULD WITHDRAW THEM FORTHWITH. THE QUOTA LEVELS SET FOR CHILE WERE QUITE UNJUSTIFIED AND BASED UNFAIRLY ON OUT-OF-DATE PRODUCTION FORECASTS. AN ADDED HEADACHE WAS 10,000 TONNES OF CHILE APPLES ALREADY IN TRANSIT, WHICH NOW COULD NOT BE LANDED IN THE EC. THE EC SHOULD ACCOMMODATE CHILE APPLES ALREADY IN TRANSIT. HE (SURPRISINGLY) DID NOT PRESS THE EC FOR ITS GATT JUSTIFICATION.

6. DE PASCALE (COMMISSION) WAS SOOTHING BUT PLAYING A DOUBTFUL HAND. THE EC ACTION WAS NOT A BREACH OF STANDSTILL WHICH ALLOWED FOR GATT LEGITMATE ACTION. THE EC HAD NOT HAD ANY ULTERIOR MOTIVES. IT HAD SIMPLY BEEN SWAMPED WITH APPLES. HE TOOK NOTE OF THE APPLES IN TRANSIT BUT MADE NO PROMISES.

7. CHILE RETURNED TO THE CHARGE ON THE 10,000 TONNES OF APPLES IN TRANSIT AND THE LEVEL OF THE QUOTA. THE EC MUST RESOLVE THIS

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URGNETLY. DE PASCALE WAS A LITTLE SCEPTICAL ABOUT CHILE'S FIGURES BUT AGREED TO HOLD A FURTHER ROUND OF CONSULTATIONS IN ABOUT 10 DAYS.

COMMENT

8. NO SURPRISES AND THE NEXT STEP FROM CHILE WILL BE A PANEL REQUEST. IT IS GALLING THAT THE COMMISSION DID NOT EVEN GO THROUGH THE MOTIONS OF DISCUSSING THE GATT DEFENCE OF ITS ACTION WITH MEMBER STATES IN ADVANCE. ON THIS BASIS IT IS HARD TO SEE WHAT THE COMMISSION VIEW THE ARTICLE 113 COMMITTEE'S ROLE AS BEING AS FAR AS AGRICULTURE TRADE RESTRICTIONS ARE CONCERNED. TO JUSTIFY THIS ACTION UNDER ARTICLE XI IS RISKY, BUT THE TRUTH PROBABLY IS THAT THERE IS NO REALLY RESPECTABLE GATT DEFENCE.

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FRAME EXTERNAL

EC AND CHILEAN APPLES

1. TOGETHER WITH OTHER EC HEADS OF MISSION AND LOCAL COMMISSION REP. I WAS CALLED IN LATE ON 29 APRIL TO HEAR FURTHER PROTESTS FROM MINISTERS OF FINANCE AND FOREIGN AFFAIRS.
2. BUCHI SAID THE EC ACTION WAS A DIRECT CONTRADICTION OF EC STATEMENTS ON PROTECTIONISM AND COMMITMENTS TO FREE ACCESS TO MARKETS. IT WAS INCOMPREHENSIBLE AT A TIME WHEN CHILE WAS BEING URGED BY THE WEST TO EXPORT AND CONTINUE REPAYING ITS FOREIGN DEBT. APPLE EXPORTS WERE ONE OF THE FEW AREAS WHERE CHILE ENJOYED A COMPARATIVE ADVANTAGE. EUROPE WAS THE PRINCIPLE MARKET AND THOUSANDS OF JOBS WERE AT STAKE. THIS WAS NOT SOLELY AN AGRICULTURAL PROBLEM AND WAS TOO IMPORTANT TO BE CONSIDERED ONLY AT A TECHNICAL LEVEL. CHILE WAS ONE OF THE FEW COUNTRIES MEETING ITS OBLIGATIONS YET THE EC APPEARED TO BE DOING ITS BEST TO TORPEDO THIS.
3. GARCIA ADDED THAT ONCE AGAIN THE DEVELOPED NATIONS WERE CHANGING THE RULES WHEN IT SUITED THEM. HE URGED OUR GOVERNMENTS TO THINK AGAIN ABOUT THE PRINCIPLES AT STAKE.
4. PRESIDENCY AND EC REP. REPLIED ON STANDARD LINES. WE ALL AGREED TO INFORM OUR GOVERNMENTS.

WHITE

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FROM: MRS JULIE THORPE

DATE: 4 May 1988

SIR G LITTLER

cc PS/Economic Secretary
Mr H P Evans
Mr Mountfield

COURTESY CALL FROM CHILEAN AMBASSADOR

The Chilean Ambassador would like to pay a courtesy call on the Chancellor to deliver a letter from his Minister of Finance, sometime during the ^{next} few weeks.

2. The Chancellor has said he would be grateful for your advice on whether he should see him.

Julie Thorpe

MRS JULIE THORPE
Diary Secretary

9/ Please see Sir G Littler
advice below.

Pass to EST?

Julie
5/5

From: Sir G. Littler
Date: 5 May 1988

c.c. PS/Econ Sec 5127.
Mr Huw Evans
Mr Mountfield

MRS THORPE ✓

Matters State

you ps -
puf.

COURTESY CALL BY CHILEAN AMBASSADOR

As far as we are aware, it is unlikely that any message from the Chilean Finance Minister at present would contain anything of substance: no known bilateral financial issues; no approaches to creditors imminently needed; no role as representatives of the Latin Americans. Our guess it might simply be a friendly contact letter inspired by the fact that a projected visit to London by the Chilean Finance Minister recently had to be cancelled.

2. We should agree to receive a call. But I think it need not be the Chancellor himself. If the Economic Secretary is willing to take on the chore, I recommend arranging for him to receive the Ambassador, and for Mr Mountfield to sit in.



(Geoffrey Littler)

The Ambassador of Chile

Ch. Sr. Delano is clearly pressing to see you rather than EBT. Shall we try to slot him in?

5th May 1988

25 10/5 FCO advise, psr

~~Highly urgent 10/5
1/8/88 to be taken to Delano~~

Dear Minister Lawson:

Further to my office's telephone request for an appointment to call on you, I am writing to remind you that I have been entrusted by Chilean Minister of Finance, Sr. Hernán Buchi to personally deliver a letter on his behalf at your earliest convenience.

At the same time, having previously been Minister of Economy before my present assignment in London and in my capacity as newly appointed Chilean Ambassador to the United Kingdom, I shall very much welcome the opportunity to meet you.

I thank you for your help and look forward to hearing from you soon,

yours sincerely,

JUAN CARLOS DELANO

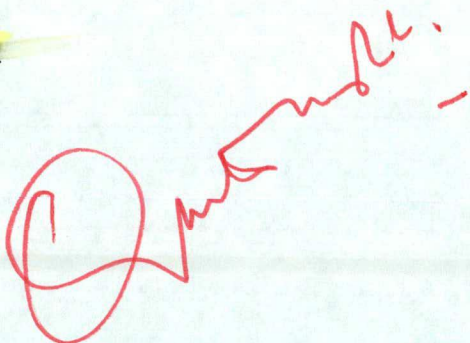
Rt. Hon. Nigel Lawson, MP
Chancellor of the Exchequer
H.M. Treasury
Parliament Street
London SW1P 3AG

James Sharp 26/2

CONFIDENTIAL

From: T P Lankester
Date: 5 May 1988

CHANCELLOR



cc

Economic Secretary
Sir Peter Middleton
Sir Geoffrey Littler
Mr H Evans
Ms J Noble

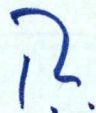
PANAMA

I was approached by the American Embassy today with a request from Washington that we ask the Hong Kong authorities to freeze \$20 million in a Hong Kong bank account which is likely to be paid out to General Noriega in Panama in the next 24 hours.

2. The Americans, as you may have seen, are trying to bring down the Noriega regime by economic sanctions. President Reagan has issued an Executive Order banning the payment of funds from the US to Panama. The counsellor from the American Embassy told me that the US was now trying to persuade other countries to cooperate in stopping the payment of funds from other sources.

3. I told the counsellor that, much as we shared the US distaste for Noriega, we were unable to help. This was essentially an internal matter for Hong Kong; I doubted whether the Hong Kong authorities had powers to block the account; and given our well known views on American attempts to have assets frozen in London, they would not take kindly to any persuasion from us.

4. The FCO have also been approached and gave a similar answer. The Hong Kong authorities are being informed.



T P LANKESTER

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09 MAY 1988		
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COPIED TO: FCO, DTI, UKMIS GENEVA, UKREP BRUSSELS

FRAME EXTERNAL

CHILEAN APPLE EXPORTS TO THE EC

THE CHILEAN MINISTER HAS SENT ME A LETTER FOR MR GUMMER PROTESTING AT THE EC MEASURES. THIS REFERS TO LETTERS WHICH THE CHILEAN MINISTER OF FINANCE HAS WRITTEN TO CHANCELLOR OF THE EXCHEQUER AND MINISTER OF TRADE (WHICH WE HAVE NOT YET SEEN).

THE LETTER DRAWS ATTENTION TO CHILE'S EFFORTS TO DEAL WITH ITS DEBTS BY EXPANDING AND DIVERSIFYING ITS EXPORTS. THE DYNAMISM OF CHILE'S AGRICULTURAL SECTOR HAS COME FROM THE PRIVATE SECTOR BY MEANS OF INVESTMENT, TECHNOLOGICAL INNOVATION AND ADAPTATION TO INTERNATIONAL MARKETS, WITHOUT STATE SUBSIDY OR SPECIAL AID.

THE EC MEASURES ARE A BLOW AND YET ANOTHER BARRIER TO THE COUNTRY'S EFFORTS TO ESTABLISH A HEALTHY, INDEPENDENT AND PROSPEROUS ECONOMY.

CHILE REGARDS THE MEASURES TAKEN TO BE CONTRARY TO THE FUNDAMENTAL PRINCIPLES OF FREE TRADE AND NON-DISCRIMINATION OF THE GATT, AND OF NO HELP IN ACHIEVING THE OBJECTIVES OF THE URUGUAY ROUND. THEY ARE AT VARIANCE WITH EC'S STATED POSITIONS ON INTERNATIONAL TRADE.

SR PRADO WOULD BE GRATEFUL IF MR GUMMER WOULD CONSIDER THE ABOVE AND HOPES THAT CHILE CAN COUNT ON HIS COMPREHENSION AND GOOD WILL IN ARRIVING AT AN EARLY SOLUTION OF THE PROBLEM.

WHITE

YYYY

CONFIDENTIAL



FROM: J M G TAYLOR

DATE: 6 May 1988

A handwritten signature in the top right corner of the page.

MR LANKESTER

cc PS/Economic Secretary
Sir P Middleton
Sir G Littler
Mr H P Evans
Miss C Noble

PANAMA

The Chancellor has seen your minute of 5 May. He has commented:
"Quite right".

Handwritten initials, possibly "JMT", in the center of the page.

J M G TAYLOR

Nick

I think you are
funding methopson
this,

MR MOUNTFIELD

file
195



FROM: P J WALES
DATE: 9 May 1988

cc Sir G Littler
Mr H Evans
Mrs J Thorpe 2

COURTESY CALL BY THE CHILEAN AMBASSADOR

The Economic Secretary has now agreed to receive a courtesy call from the Chilean Ambassador on Wednesday 18 May at 10.30am. I would be grateful if you could arrange for the necessary briefing to reach this office by close of play on Monday 16 May and also attend a short pre-meeting at 10.15am on the 18 May.

P J WALES
Diary Secretary



Treasury Chambers, Parliament Street, SW1P 3AG

Mrs Smith
Chilean Embassy
12 Devonshire Street
LONDON
W1

9 May 1988

Dear Mrs Smith

I refer to our telephone conversation earlier today. I would just like to confirm that the Economic Secretary is looking forward to receiving a courtesy call from the Chilean Ambassador on Wednesday 18 May at 10.30am in the Treasury.

Yours Sincerely
Peter Wales

P J WALES
Diary Secretary

BF 2/6

OFFICE OF MINISTER FOR TRADE MINUTE NO: 478

To:
Mr Owen
OT4/2

PS/Secretary of State
PS/Sir Brian Hayes
Mr Dell
Mr Roberts
Mr Muir OT4
Mr Johnson EEP1

From:
MARJORIE DAVIES
PS/MFT
Room 833a
1 Victoria St
215 5144

MW Sharp FCO S&MD. ✓

11 May 1988

CALL ON MINISTER FOR TRADE BY THE CHILEAN AMBASSADOR

11 MAY 1988

You were present when the Chilean Ambassador, Sr Delano, and the First Secretary Commercial, called on Mr Clark to deliver a letter from the Chilean Finance Minister to protest at the EC import quota on apples. (You have the letter).

2 Sr Delano said that the immediate problem was the 12,000 tons already shipped. You understood that the Commission had talked about flexibility and thought it might refer to those apples. Sr Delano said that the Commission were only talking about 5,000 tons, which still left the remaining 7,000 tons. He confirmed that a copy of the letter had been sent to the Chancellor of the Exchequer but not to the Minister for Agriculture; Mr MacGregor was however meeting a group of fruit importers tomorrow.

a letter has been sent to Mr Gummer, who visited Chile in January. Mr Clark visited Chile October-November last year.

3 Mr Clark said that he was very sympathetic to Chile's case and recognised that economically Chile had exceptional status in Latin America; he would try to do what he could to help. After the meeting Mr Clark said he would try to have a word with Mr MacGregor at the vote tonight (may not be possible as Mr MacGregor is returning late from Munich). He also asked for a draft letter to send to Mr Gummer (which you have provided and which Mr Clark has signed).

Marjorie Davies

MISS M DAVIES



The Chilean Ambassador
would like to pay you
a Courtesy Call to deliver
a letter from his Minister
of Finance - Whenever
you will be free.

Content for me to arrange
something for 15-30 minutes?

Julie
3/5.

[Handwritten red notes]
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Mania 580 6392 x 12 ..





the department for Enterprise

The Hon. Alan Clark MP
Minister for Trade

Rt Hon John Gummer MP
Minister of State
Ministry of Agriculture, Fisheries and Food
Whitehall Place
LONDON
SW1A 2HH

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

Direct line 01-215 5144
Our ref L02AHO
Your ref
Date 11 May 1988

CH/EXCHEQUER	
REC.	13MAY1988
ACTION	Mr MOUNTFIELD
COPIES TO	PS/CST, PS/EST,
	Sir G. LITTLER,
	Mr A.P. EVANS
	Mr MOUNTFIELD

✓
13/5

Mr ROBSON

Jan John

The Chilean Ambassador called on me this afternoon to hand over a letter from his Finance Minister complaining about the EC's decision to impose a quota on the import of Chilean apples. I understand that similar letters are on their way to you and to Nigel Lawson.

I am bound to say that I am most sympathetic to the Chilean case. There must be doubt that the Commission's action can be defended in the GATT and it certainly runs counter to all we are trying to achieve in the current Uruguay Round.

Furthermore, it has to be seen against a background of commendable responsibility in putting the Chilean economy in order and paying their overseas debts through an export-led expansion.

You should also be aware that we think we are close to winning a most important defence contract for the sale of Sea Wolf to the Chilean Navy. There are therefore good grounds in several respects for supporting the Chileans as much as we can.

I am copying this to Nigel Lawson.

Alan Clark
[Signature]

ALAN CLARK

PSM (D1)
 PSTE D3 A5
 PSTE D5 A5

11.7

New Zealand growers squeezed by EC-Chile apple trade wrangle

BY DAI HAYWARD IN WELLINGTON

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 IDIONALITY.TREATY PSTE D3 A5
 RL.TAMENT PSTE A5
 ERGY.SCI.SPAC P55 R6 (D2 A4)
 CLEAR ENERGY PSM R6 (A13)
 D.RELS.ECO.ADV R6 (D2 A3)
 **S..P PSTE D3
 SCUP.ADV P55 (D1)
 GCL.ADVISERS ASS.LEGAL.ADVISERS
 COITION.ATOS PSTE R6
 FICE.SERVICES P55 D3
 ERSEAS.FS* P55 D3
 ERSEAS.POL.ADV P55 A11
 SONNEL.DPS P55 D3 D1P54 A5
 SONNEL.POL P55 D3 D1P54 A5
 HVE.BRION.SIDE D1P54
 AGING P55 D3 D1P54 A5

NEW ZEALAND'S delicately-balanced apple industry faces a crisis because of the sudden cut in its apple exports to Europe imposed by the European Community.

The country was told it could ship only 115,000 tonnes, about 15 per cent less than the 135,000 tonnes it had earmarked.

The blow is undoubtedly a devastating one for New Zealand's apple-growers and the effects will be much worse than might appear from the actual tonnage involved.

Many of the country's apple varieties are premium types produced in modest quantities. The economics of their production depend on the best possible price being obtained.

Last year about two-thirds of the NZ\$300m (£110m) earned from apple exports came from sales to Europe. If the good-quality apples

have to be switched from Britain or the Continent to alternative markets offering much lower returns, or turned into juice of manufactured products, the delicate economics of the industry could be undermined.

The New Zealand Apple and Pear Board says that if the future quota imposed by the EC remains at this year's level the country's apple industry will be destroyed.

The board and its officers have reacted angrily against Chile, which they blame for provoking the EC into imposing the curbs.

Chile has flooded the European apple market for two successive years: in 1984 it sent 97,000 tonnes; the figure climbed rapidly to 140,000 tonnes last year; Chile planned to ship as much as 250,000 tonnes this year.

As a result prices for European-grown apples have plummeted and large quantities

A DELEGATION representing UK fruit traders and consumer bodies will meet Mr John MacGregor, Minister of Agriculture, this week to protest against curbs on apple imports from outside the European Community.

have been diverted into stock feed. It has also meant a rise in the cost of farm subsidies to EC growers.

Southern Hemisphere apple suppliers were warned last year that curbs could be imposed if shipments to the EC were not controlled.

New Zealand says it has always been a responsible supplier to Europe; it has controlled its shipments to arrive only after locally-grown apples were ended; it quits the market before the EC's own new-season

Mr Sidney Garber, of the National Federation of Fruit & Potato Trades, yesterday said the EC's "unilateral" action was effectively "dictating to the British consumer what type of apples she or he could buy."

apples arrive, making sure prices for locally-grown fruit are at a satisfactory level.

The EC initially acted against Chile by using a controversial surveillance scheme introduced in February to suspend Chilean import licences.

Chilean exporters threatened to appeal to the General Agreement on Tariffs and Trade because Chile was being singled out. The EC extended the sanctions to all overseas suppliers.

New Zealand's Minister of

Overseas Trade, Mr Mike Moore, has started proceedings in Gatt on behalf of New Zealand. He will pursue the case if no other solution can be found.

Mr Moore has also criticised the EC for breaking the Gatt agreement, established at Punta del Este, Uruguay, not to introduce new trade barriers.

One problem, says a NZ Apple Board official, is that Chile, with its free marketing methods, does not have any mechanism or body which can control exporters, and the Chilean Government says it does not interfere in commercial matters.

Chile has been steadily increasing apple output along with many other horticultural products which compete directly with New Zealand. It has also been working to improve the poor-quality image of its apples and other fruit.

Chilean apples now reach the Northern Hemisphere a month before New Zealand's fruits, which are controlled to meet European requirements.

New Zealand apple-growers are confident that the traditional quality and its long-established reputation for quality in Europe will enable them to more than hold their own with Chilean exports. To have their exports compulsorily cut is a far more severe blow than having to face increased competition in the market-place.

Last week Mr Moore said an approach would be made to Chile over the shipment of apples to the EC. He would not specify its form.

New Zealand will also be trying to persuade the EC to raise the level of its quota - at least to the tonnage scheduled initially.

27

11 May 88

Handwritten notes:
 + copy of ...
 Council ...
 ...
 ...
 ...



~~PHF~~
Foreign and Commonwealth Office

London SW1A 2AH

13.5.88

Julie

~~PHF~~

As promised, I enclose some background papers on the Chilean apples problem. As they say, HMG has sympathy for Chile's position. We expressed concern when the licensing system was introduced, protested the unilateral suspension of Chile's licence and the imposition of a quota system, and have made representations to the Commission about their lack of flexibility over the apples already shipped.

Having said this, the large increase in the level of Chilean

sending has not helped matters, and the Commission has acted within its competence.

I have spoken to the Chilean Embassy and have explained how difficult it would be for the Chancellor to see the Ambassador. They understood this, and would be happy for Peter Lilley to see the Ambassador.

James Sharp

South America Dept
270 2612

The Ambassador

18 May 1988

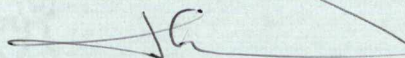
Dear Mr. Lilley:

Please find enclosed a letter from Chilean Minister of Finance, Sr. Hernán Buchi Buc to The Chancellor of the Exchequer, Rt. Hon. Nigel Lawson, MP, and an unofficial translation, which I would appreciate it if you could hand over to the Chancellor.

I avail myself of this opportunity to thank you very much for receiving my Commercial Attaché, Sr. Hans von Leyser and myself and sparing the time to discuss Anglo-Chilean relations at present.

With renewed appreciation, I remain,

Yours sincerely,



JUAN CARLOS DELANO

Mr. Peter Lilley
Economic Secretary
Treasury Chambers
Parliament Street
London SW1P 3AG

EMBASSY OF CHILE

12 DEVONSHIRE STREET
LONDON, W1N 2DS
TELEPHONE 01-580 6392/4

UNOFFICIAL TRANSLATION

Dear Minister,

I would hereby like to express to Your Excellency, the concern of the Government of Chile (also being conveyed to the Chancellor of the Exchequer), about the recent important limits on apples set by the European Economic Community. As you probably know, the Community has imposed a quota on the importation of Chilean apples.

Protectionism is undoubtedly a delicate matter as barriers to world trade could aggravate the enormous financial difficulties of those countries with high external borrowings. Some of the most critical cases are those Latinamerican countries whose foreign debt call for the generation of commercial surpluses just to pay the interest on those debts. To this end, and just as Chile has been doing in the past decade, it is necessary to expand and diversify exports rather than just reducing imports. It is the only way to produce the growth necessary to expand the economy and by consequence, permit Chile to pay her foreign debt.

With regard to protectionism, Your Excellency is well aware that at a recent meeting of the Acting Committee of Governors of the International Monetary Fund it was emphatically re-emphasized that "protectionist measures would be self defeating, for instead of reducing external imbalances, they risk widespread falls in countries' growth rates.

EMBASSY OF CHILE

12 DEVONSHIRE STREET
LONDON, W1N 2DS
TELEPHONE 01-580 6392/4

- 2 -

The increase in exports of Chilean apples to European Economic Community markets is set within a national export plan. This is design to enable the country to reach certain economic growth rates which will allow her to pay off her financial commitments in an orderly and prompt manner. It is not easy for our country to meet this international commitments but we have assumed responsibility without transferring to others the costs of our difficulties.

In this respect I would like Your Excellency to know that the activity shown in the last ten years by Chilean agriculture, is due to the efforts of the private sector which does not get any special subsidy from the State. As a result of constant private investment, technological innovation and adapting to overseas markets, it has been possible not only to diversify agricultural exports, but also to turn this sector into one of the most dynamic within the national economy.

For all these reasons, Chile is greatly concerned about the restrictive measure(s) set by the European Community on the importation of apples. I would like to express to Your Excellency that this decision disregards the basic principles of free trade and non-discriminatory treatment to contracting parties, contained in the General Agreement of Tariffs and Trade (GATT). It also hinders the achievement of the objectives we seek through the actual Montevideo Round.

It does represent an additional difficulty in the good and balance handling of the economy. Notwithstanding the above however, our country will not consider this restriction as an excuse to avoid fulfilling its external debt responsibilities.

I avail myself of this opportunity to express to Your Excellency the assurance of my highest consideration.

Hernán Buchi Buc
MINISTER OF FINANCE

SANTIAGO, Abril 27 de 1988

SEÑOR
Rt. Hon. Nigel Lawson
Chancellor of the Exchequer
Reino Unido

Excelentísimo Sr. Ministro:

Por intermedio de la presente deseo manifestar a Vuestra Excelencia la preocupación del Gobierno de Chile, preocupación que simultáneamente estoy haciendo llegar a su colega el Sr. Ministro de Comercio, por la reciente restricción aplicada por los países miembros de la Comunidad Económica Europea a las importaciones de manzanas. Como es de conocimiento de US. los países comunitarios fijaron una cuota para la importación de manzanas chilenas.

Sin lugar a dudas el proteccionismo es un tema delicado, porque nuevas barreras al comercio mundial pueden acentuar las ya enormes dificultades financieras en países altamente endeudados. Los casos tal vez más críticos son los de algunos países latinoamericanos cuya deuda externa requiere de superávit comerciales crecientes que faciliten el pago de los intereses. Para ello y tal como lo viene desarrollando Chile en la última década, es indispensable expandir y diversificar las exportaciones más que reducir las importaciones, es éste el único modo en que el ajuste puede producirse con crecimiento, permitiendo además mejorar la capacidad de pago del país y en consecuencia de hacer frente a sus compromisos con el exterior.


Respecto del proteccionismo y como es de conocimiento de Vuestra Excelencia, en reciente reunión celebrada por el Comité Interino de la Asamblea de Gobernadores del Fondo Monetario Internacional, se enfatizó nuevamente "que las medidas proteccionistas se auto-derrotarían, y que éstas en vez de reducir los desequilibrios externos, arriesgan una caída generalizada del crecimiento de los países".

El aumento de las exportaciones de manzanas de Chile al mercado de la Comunidad Económica Europea está inserto en el importante esfuerzo exportador que realiza el país para poder alcanzar niveles de crecimiento económico compatibles con un fiel y oportuno cumplimiento de sus compromisos financieros. Para nuestro país no es fácil cumplir los compromisos internacionales y en este sentido hemos asumido nuestra responsabilidad sin traspasar a terceros los costos de nuestras dificultades.

En esta materia quisiera manifestar a Vuestra Excelencia que el dinamismo reflejado por el sector agrícola chileno en los últimos diez años, es producto del trabajo del sector privado nacional, el cual no se beneficia de subsidio o ayuda especial alguna proveniente del Estado. Es así que como resultado de un constante esfuerzo de inversión, innovaciones tecnológicas y adaptación a los mercados internacionales, se ha podido no tan sólo diversificar las exportaciones agrícolas sino además transformar a este sector en uno de los más dinámicos de la economía nacional.

Por lo expuesto el Gobierno de Chile vé con gran preocupación las medidas restrictivas aplicadas por los países comunitarios a las importaciones de manzanas. Junto con expresar a Vuestra Excelencia que esta decisión constituye un desconocimiento a los fundamentos y principios básicos de libre comercio y trato no discriminatorio a las partes contratantes del Acuerdo General sobre Aranceles Aduaneros y Comercio (GATT), y en nada ayudan al logro de los objetivos que buscamos a través de la actual Ronda de Negociaciones Comerciales Multilaterales, Ronda de Uruguay, sí representan, dificultades adicionales importantes para el buen y equilibrado manejo de la economía. No obstante ello, nuestro país no estima que esta restricción pueda constituirse en excusa o justificar incumplimientos en el pago de su deuda externa.

Hago propicia esta oportunidad para expresar a Vuestra Excelencia los sentimientos de mi más alta y distinguida consideración.


HERNAN BUCHI BUC
MINISTRO DE HACIENDA



FROM: G R WESTHEAD
DATE: 19 May 1988

PS/CHANCELLOR

cc Sir G Littler
Mr Evans
Mr Mountfield
Mr P G F Davis
Mr Bottrill
Mrs Thomson
Miss Higgins

COURTESY CALL BY CHILEAN AMBASSADOR SNR DELANO ORTUZAR

The Chilean Ambassador paid the Economic Secretary a courtesy call on Wednesday 18 May.

Apples

2. The purpose of the call was for the Ambassador to pass to the Economic Secretary a letter from the Chilean Finance Minister, Snr Hernan Buchi Buc to the Chancellor, which, as we discovered at the meeting, was about limits placed on imports of Chilean apples into the EEC.
3. The Economic Secretary told the Ambassador that Government policy was to support free trade throughout the world. However, the question of quota limits on apples was primarily one for the Department of Trade and Industry, rather than the Treasury.
4. The Ambassador said that he had already seen the Minister for Trade. He wanted to put Treasury Ministers in the picture too about EC constraints on Chilean imports. He stressed that the Chilean economy was a very open one. In Chile, there were no regulations on exporters. On imports only a 15 per cent duty applied. The EC was Chile's most important market for apples.
5. The Economic Secretary asked what response Chile had had from the EEC about their objections to the restrictions. The Ambassador said they might get an answer from the EEC within the next 1-2 months, but their problem was a short term one. The Economic

Notes:

*BT has advised
out this letter about apples.*

23/5

6/7/16

*When we can expect a draft reply
Need a draft reply
BT has advised
out this letter about apples.*

Handwritten signature and initials

Secretary asked about other countries to which similar EC quota constraints on apples applied - eg Australia and New Zealand. The Ambassador said that these countries were better placed to restrict their output, whilst Chile was not.

6. The Economic Secretary said that the Chancellor had been pushing for liberalisation in agriculture world-wide, including structural reforms. Nevertheless, we had obligations to our EC partners including the Common Agricultural Policy.

Chilean Economy

7. The Economic Secretary asked about the Chilean economy more generally. The Ambassador said that output had grown by almost 5 per cent per annum in recent years. Inflation was under control compared with other Latin American countries. Chile had been paying its debts. Exports were forecast to increase 20 per cent this year. The balance of payments was already showing a \$1 billion surplus for the current year, set against a forecast surplus of \$1.15 billion for the whole year.

8. The Ambassador said there had been an important shift in the mentality of the Chilean population in recent years. They had once been socialists, but now the private sector and the corporate sector were the most important. He mentioned private sector health provision. Out of a population of 12 million, 1 million people were covered by private sector health arrangements. The Economic Secretary said that in the UK almost 5 million people were covered by private health insurance, but that this was additional to the National Health Service. Thought was currently being given to restructuring the UK health provision.

9. The Economic Secretary thanked the Chilean Ambassador for coming to see him. He said he would convey to the Chancellor Chile's problems regarding the EC quota on apples, but stressed that this was primarily a matter for the Department of Trade and Industry.

Guy Westhead

GUY WESTHEAD

Assistant Private Secretary



Ministry of Agriculture, Fisheries and Food
Whitehall Place London SW1A 2HH

From the
Minister of State

The Hon Alan Clarke MP
Minister of Trade
Department of Trade and Industry
1-19 Victoria Street
LONDON
SW1 0ET

21 May 1988

CHILE : APPLES

Thank you for letting me know in your letter of 11 May that the Chilean Minister of Finance had written to you to complain about the European Commission's restrictions on the imports of apples.

I have had a similar approach from the Chilean Minister of Agriculture, whom I met when I visited Chile earlier this year. I was impressed by the efforts the Chileans are making to develop their agriculture on competitive, market-orientated lines.

The question of the conformity of the Commission's action with the GATT will be decided by the GATT Panel that has now been established. I certainly agree that the import restrictions imposed will do nothing to help the Community's wider stance on international trade matters, particularly in the Uruguay Round.

I am enclosing a copy of the reply I am sending to Senor Prado (together with a copy of his letter to me) which incorporates these points; you may find it helpful in making your response to the Chilean Minister of Finance.

I am also copying this correspondence to Sir Geoffrey Howe and Nigel Lawson.

CH/EXCH	
REC.	26 MAY 1988
ACTION	Mr MOUNTFIELD,
COPIES TO	PS/CSF, PS/EST, Sir P. MIDDLETON, Sir G. LITTLE, Mr H. P. EVANS, Mr ROBSON.

JOHN SELWYN GUMMER



Ministry of Agriculture, Fisheries and Food
Whitehall Place London SW1A 2HH

From the
Minister of State

Jorge Prado Aranguiz
Minister of Agriculture
Republic of Chile

21 May 1988

Thank you for your letter of 4 May concerning the restrictive measures on apple imports recently imposed by the European Commission on behalf of the European Community.

In my recent visit to Chile I was impressed by the progress being made in the market-orientated development of Chilean agriculture. I can therefore appreciate that the Community's ban will be seen as a discouraging response to Chile's efforts.

The United Kingdom expressed concern about the Commission's original action to introduce import licensing in February. Then the Commission argued that the surveillance arrangements were necessary because stocks of apples in the main producing countries of the Community were at high levels; EC prices were at low levels; and Southern Hemisphere suppliers had not been prepared to give adequate undertakings about orderly marketings in 1988. Nonetheless, we made it clear that we would have preferred any problems to be resolved by discussion between the Commission and the Community's suppliers, as in previous years.

When the Commission subsequently suspended licensing in respect of Chile, we made our misgivings clear within the Community, and with some other member states we warned that further action would not be in the Community's wider interests. When the Commission extended action to all suppliers and effectively banned imports of apples from Chile, we made it plain in the Council of Foreign Ministers of the Community on 25 April that such a move did not in our view help the Community's wider stance on world trade liberalisation. I was not surprised to see that you made that very point in your letter.

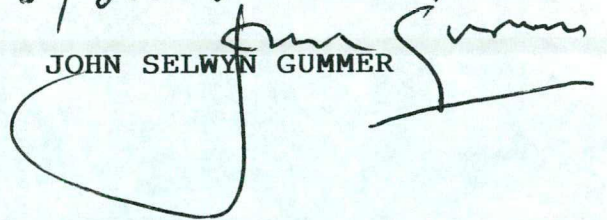
On the positive side, I am pleased that the Community has accepted your country's request for a GATT Panel to investigate the conformity of the measures taken with the principles of the GATT. As you will appreciate, I cannot prejudge the outcome of such an investigation - the question of the GATT-legitimacy of the Community's actions is now to be resolved in GATT.

I should finally comment on one further practical matter, namely the fate of apples which were en route to the Community, without licences, when licensing was suspended. We have repeatedly requested the

Commission to allow such sendings into the Community, but I have to say that the Commission has shown no signs of flexibility on the point, maintaining that traders were aware of the need to have licences before these shipments here put on the water. I cannot promise that we shall persuade the Commission on this point, especially as our indications are that other member states do not see this as a problem. We shall, however, continue pressing the arguments for the Community to be flexible in this area.

My very best regards to your wife
and the happiest memories of our visit to you

JOHN SELWYN GUMMER



49 MAY 1988 17.

CARTA Nº 149

FAX 2 OF 3

SANTIAGO, - 4 MAY 1988

Señor
Hon. John Gummer M.P.
Ministro de Estado de
Agricultura, Pesca y Alimentación
Gran Bretaña

Excelentísimo Sr. Ministro:

Como es de su conocimiento, la Comunidad Económica Europea ha adoptado recientemente, medidas que limitan el ingreso de manzanas provenientes de los países del Hemisferio Sur, entre ellos Chile.

Ante la preocupación que dicha situación ha causado al Gobierno y al sector privado nacional, nuestro Ministro de Hacienda ha enviado sendas comunicaciones a los Sres. Ministros de Hacienda y de Comercio de su país, informándoles del gran esfuerzo exportador desarrollado por Chile en el área agropecuaria, así como del efecto que las medidas comunitarias aludidas tienen sobre él.

Con similar propósito he estimado conveniente dirigirme a US., atendiendo a que, por su reciente estadía en nuestro país, entenderá nuestra aprehensión a la luz de la realidad que personalmente pudo apreciar.

Por otra parte, no escapará a la atención del Sr. Ministro que nuevas barreras al comercio acentúan las dificultades financieras de los países que como el nuestro, tratan de solucionar su actual situación de endeudamiento. Para Chile es indispensable expandir y diversificar sus exportaciones, a fin de mejorar su capacidad de pago, sin lesionar su propio crecimiento.

Como US. pudo enterarse en su visita, el dinamismo de nuestro sector agrícola ha sido el producto del trabajo del sector privado nacional, el cual no se beneficia de subsidio o ayuda especial alguna de parte del Estado. El resultado de un constante esfuerzo de inversión, de la aplicación de innovaciones tecnológicas y de adaptación a los mercados internacionales han permitido diversificar las exportaciones agrícolas y además, transformar a este sector en uno de los más dinámicos de nuestra economía.

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La reciente suspensión de las licencias y la fijación de una cuota a nuestras exportaciones de manzanas a la CEE constituye, como US. podrá comprender, un golpe y una barrera más a que el país se ve enfrentado en su lucha por consolidar una posición sana, independiente y próspera.

Junto a lo expuesto, me permito señalar a US. que nuestro país considera que las medidas adoptadas constituyen un desconocimiento a los fundamentos y principios básicos del libre comercio y trato no discriminatorio del Acuerdo General sobre Aranceles Aduaneros y Comercio, y en nada ayudan al logro de los objetivos perseguidos en la actual Ronda de Negociaciones Comerciales Multilaterales, Ronda Uruguay. A su vez, dichas medidas contravienen la posición de la Comunidad Económica, en favor de la liberación del comercio internacional, según ha sido expuesta en los más importantes foros mundiales sobre la materia.

Solicito a US. considere lo expuesto a fin de que nuestro país pueda contar con la comprensión y mejor voluntad de su parte en relación a una eventual y pronta solución del problema suscitado.

Hago propicia la ocasión para reiterar a US. mi más alta y distinguida consideración.



JORGE PRADO ARANGUIZ
MINISTRO DE AGRICULTURA

TRANSLATION OF LETTER FROM THE
CHILEAN MINISTER OF AGRICULTURE

The Republic of Chile
Ministry of Agriculture
Fisheries and Food
Minister's Office

LETTER No 149
Santiago - 4 May 1988

The Honourable John Gummer MP
Minister for Agriculture, Fisheries
and Food
Great Britain

Dear Minister

As you know, the EEC has recently adopted some measures which restrict the entry of apples from Southern Hemisphere countries, Chile being amongst these.

In view of the growing concern which this situation has created within the Government and the private sector, our Finance Minister has sent individual communications to both Ministers of Trade and Finance in your country outlining the enormous efforts which Chile has made to maintain her growth of agricultural exports and how these EEC measures can affect this development.

In similar vein, I thought it appropriate to address my letter to you, in the hope that your recent visit here might enable you to understand, having seen our situation for yourself, our anxiety.

Moreover, you will no doubt be aware that new barriers to trade can only highlight the already existing problems of indebtedness which countries such as Chile are currently trying to resolve. Chile needs to step up and diversify her exports to improve her financial standing without damaging her own economic development.

As you were able to discover during your stay in Chile, the dynamism of the Chilean agricultural sector is due entirely to the work of the private sector which does not benefit from any subsidised grants or specialist Government aid. The diversification of agricultural exports is the direct result of continued high investment, technological development and meeting the needs of international markets furthermore turning this into one of the most economically dynamic sectors in Chile.

The recent withdrawal of licences and fixing of quotas on our exports of apples to the EEC is, as I am sure you will understand, a blow and an additional barrier confronting Chile in her endeavour to secure a sound, independent and prosperous position.

I would also like to point out that Chile considers that these adopted measures constitute a disregard of the basic principles underlying free trade and non-discriminatory relations under the GATT, which do not in any way help to achieve the aims pursued in the present Round of Multilateral Trade Negotiations, the Uruguay Round. At the same time, these measures contravene the EEC position in favour of the liberalisation of World Trade which has been expounded in the most influential commercial fora dealing with this subject.

I therefore, request that you consider the above in the knowledge that you will do whatever possible to resolve the issue at an early date.

Yours sincerely

JORGE PRADO ARANGUIZ
Minister of Agriculture



Ministry of Agriculture, Fisheries and Food
Whitehall Place London SW1A 2HH

From the
Minister of State

Jorge Prado Aranguiz
Minister of Agriculture
Republic of Chile

21 May 1988

Thank you for your letter of 4 May concerning the restrictive measures on apple imports recently imposed by the European Commission on behalf of the European Community.

In my recent visit to Chile I was impressed by the progress being made in the market-orientated development of Chilean agriculture. I can therefore appreciate that the Community's ban will be seen as a discouraging response to Chile's efforts.

The United Kingdom expressed concern about the Commission's original action to introduce import licensing in February. Then the Commission argued that the surveillance arrangements were necessary because stocks of apples in the main producing countries of the Community were at high levels; EC prices were at low levels; and Southern Hemisphere suppliers had not been prepared to give adequate undertakings about orderly marketings in 1988. Nonetheless, we made it clear that we would have preferred any problems to be resolved by discussion between the Commission and the Community's suppliers, as in previous years.

When the Commission subsequently suspended licensing in respect of Chile, we made our misgivings clear within the Community, and with some other member states we warned that further action would not be in the Community's wider interests. When the Commission extended action to all suppliers and effectively banned imports of apples from Chile, we made it plain in the Council of Foreign Ministers of the Community on 25 April that such a move did not in our view help the Community's wider stance on world trade liberalisation. I was not surprised to see that you made that very point in your letter.

On the positive side, I am pleased that the Community has accepted your country's request for a GATT Panel to investigate the conformity of the measures taken with the principles of the GATT. As you will appreciate, I cannot prejudge the outcome of such an investigation - the question of the GATT-legitimacy of the Community's actions is now to be resolved in GATT.

I should finally comment on one further practical matter, namely the fate of apples which were en route to the Community, without licences, when licensing was suspended. We have repeatedly requested the

Commission to allow such sendings into the Community, but I have to say that the Commission has shown no signs of flexibility on the point, maintaining that traders were aware of the need to have licences before these shipments here put on the water. I cannot promise that we shall persuade the Commission on this point, especially as our indications are that other member states do not see this as a problem. We shall, however, continue pressing the arguments for the Community to be flexible in this area.

*My very best regards to your wife
 and the happiest memories of our visit to you*

John Selwyn Gummer

JOHN SELWYN GUMMER

PS/CHANCELLOR

FROM: MRS S THOMPSON

DATE: 7 June 1988

cc PS/Economic Secretary
Sir G Littler
Mr Evans
Mr Mountfield
Mr P G F Davis
Mr Bottrill
Miss Higgins

Thompson
Ch.
Content to write
as suggested?
JK
7/6

EC RESTRICTIONS ON CHILEAN APPLE IMPORTS

I attach a draft letter for the Chancellor to send to the Chilean Finance Minister following the Chilean Ambassador's call on the Economic Secretary on 18 May.

The reply is deliberately short as John Gummer's reply (copy also attached) is full and detailed and there is little we can add.

S Thompson
MRS S THOMPSON

Pre type final.

DRAFT LETTER FROM THE CHANCELLOR TO HERNAU BUCHI BUC, CHILEAN FINANCE MINISTER

Thank you for your recent letter about the European Commission's restrictions on the imports of Chilean apples to the EEC.

My colleague John Gummer has already written to Sr Prado setting out the United Kingdom's position and I have nothing further to add to his letter. However, I would like to express our sympathy for your case. The United Kingdom supports worldwide trade liberalisation and is concerned that the restrictions may breach the EC commitment to standstill in the Gatt round.

I hope that this matter will be satisfactorily resolved when it is heard in GATT.



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

Russell Dixon Esq
Assistant Private Secretary to the
Secretary of State for Foreign and
Commonwealth Affairs
Foreign and Commonwealth Office
Downing Street
SW1

10 June 1988

Dear Russell

... I should be grateful if you could forward the enclosed letter from the Chancellor of the Exchequer to Sr. Hernau Buchi Buc.

Yours Sincerely
A A Dight

A A DIGHT



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

9 June 1988

Sr. Hernau Buchi Buc
Minister of Finance
Republic of Chile

H. Minister

Thank you for your recent letter about the European Commission's restrictions on the imports of Chilean apples to the EEC.

My colleague John Gummer has already written to Sr Prado setting out the United Kingdom's position and I have nothing further to add to his letter. However, I would like to express our sympathy for your case. The United Kingdom supports worldwide trade liberalisation and is concerned that the restrictions may breach the EC commitment to standstill in the GATT round.

I hope that this matter will be satisfactorily resolved when it is heard in GATT.

Nigel Lawson

NIGEL LAWSON

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TO ROUTINE FCO
TELNO 165
OF 022300Z AUGUST 88
INFO ROUTINE BIS BUENOS AIRES

IMF: ARGENTINA

1. AT THE END OF THE FUND BOARD MEETING LAST NIGHT, BEZA (HEAD, WESTERN HEMISPHERE DEPT) BRIEFED FUND DIRECTORS ON DEVELOPMENTS ON ARGENTINA. DISCUSSIONS HAD ENDED IN WASHINGTON THE PREVIOUS DAY, WITH CAMDESSUS CUTTING SHORT A VISIT TO MOROCCO TO PARTICIPATE IN THEIR FINAL STAGES.
2. BEZA CONFIRMED THAT ARGENTINA'S DOMESTIC RESERVES AND DOMESTIC ASSETS TARGETS HAD BEEN OVERSHOT IN Q1. BECAUSE OF INFLATION END-JUNE CEILINGS ON ALL NOMINAL AGGREGATES HAD BEEN OVERSHOT BY SUBSTANTIAL MARGINS. THE SBA WAS THEREFORE EFFECTIVELY INOPERATIVE.
3. THE FUND HAD BEEN DISCUSSING A NEW PACKAGE WITH THE ARGENTINIANS. THIS WOULD INVOLVE THE IMMEDIATE IMPLEMENTATION OF POLICY MEASURES TO REDUCE THE PSBR TO 1 1/2 PER CENT OF GNP THIS YEAR FROM A BASELINE OF 4 1/2 PER CENT. A PRINCIPAL ELEMENT WOULD BE THE INTRODUCTION OF AN EXCHANGE TAX TO GIVE 1 PER CENT OF GNP, TO BE RAISED BY SHIFTING ALL INDUSTRIAL TRADE TO THE FREE EXCHANGE RATE WHILST KEEPING AGRICULTURAL TRADE AT THE OFFICIAL RATE. THIS TAX WOULD BE PHASED OUT BY AROUND NEXT APRIL, TO BE REPLACED BY A LAND TAX, AS THE TWO EXCHANGE RATES WERE BROUGHT TOGETHER. ELECTRICITY AND FUEL PRICES WERE TO BE RAISED, SUBSIDIES CUT, AND A SPECIAL TAX IMPOSED ON PUBLIC ENTERPRISES. THERE WOULD BE A TEMPORARY FREEZE OF ALL PRICES AS WELL AS PUBLIC SECTOR WAGES, AND A SUBSTANTIAL TIGHTENING OF THE REDISCOUNT POLICY. TAX LIBERALISATION MEASURES WOULD BE INTRODUCED, CUSTOMS DUTIES AND QUANTITATIVE IMPORT RESTRICTIONS REDUCED.
4. THE AUTHORITIES HAD WANTED TO INTRODUCE THE COMPLETE PACKAGE IN MID-AUGUST. HOWEVER, A PRESS LEAK HAD FORCED THE CLOSURE OF THE EXCHANGE MARKETS, AND PARTIAL ANNOUNCEMENTS WOULD BE MADE IMMINENTLY.
5. THE FUND INTENDED TO CONTINUE DISCUSSIONS, WITH A VIEW TO CLARIFYING THE AUTHORITIES' INTENTIONS TO REDUCE FURTHER IN 1989 H1. UP-FRONT ACTION WOULD BE REQUIRED TO REDUCE IMBALANCES, REDUCE PROTECTION, AND ACCELERATE STRUCTURAL REFORMS. BEZA ADMITTED THAT THE PRESENT PACKAGE

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RELIED HEAVILY ON TEMPORARY REVENUE MEASURES, WITH IMPORTANT EFFECTS ON COSTS. A MAJOR WEAKNESS WAS THAT THERE WAS TO BE NO FREEZE ON PRIVATE SECTOR PRICES. THERE WAS NO GUARANTEE THAT ANY CUTS WOULD BE MAINTAINED BEYOND THE PROGRAMME PERIOD.

6. BEZA REPORTED THAT BOARD DISCUSSION WAS ENVISAGED ONLY ONCE CRITICAL MASS WAS ACHIEVED ON THE BANK FINANCING AND ALL THE MAIN MEASURES TAKEN, POSSIBLY AROUND NOVEMBER. THE PROGRAMME WOULD HAVE TO BE ON TRACK AND OPERATIONAL AT THAT STAGE. IN THE MEANTIME THE FUND WOULD WORK TO AGREE FURTHER POLICY MEASURES.

7. ARGENTINA WAS NOW LOOKING FOR BRIDGE AND INTERIM FINANCING. IT WAS OVER 90 DAYS BEHIND IN ITS PAYMENTS TO THE BANKS. THE AUTHORITIES FEARED INSUFFICIENT FINANCE WOULD BE AVAILABLE IN TIME TO AVOID FURTHER ARREARS ACCUMULATION.

8. BEZA GAVE ASSURANCES THAT THE STAFF WOULD COME BACK TO THE BOARD TO REPORT FUTURE DEVELOPMENTS.

9. IN REPLY TO ZECCHINI (ITALY), BEZA ADMITTED THAT THE PACKAGE INVOLVED THE INTRODUCTION OF A MULTIPLE CURRENCY PRACTICE, BUT DEFENDED IT AS BEING A TRANSITIONAL STEP TOWARDS A UNIFIED EXCHANGE RATE. IN REPLY TO MYSELF, BEZA REPORTED THAT HE DID NOT KNOW HOW MUCH OF THE OVERALL PACKAGE WOULD BE ANNOUNCED THIS WEEK AND HOW MUCH LEFT UNTIL LATER

10. FCO PLEASE PASS TO WALSH (HMT), WARE (BOE), T RICHARDSON (ERD) AND BREACH (ECGD)

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FROM: MRS S THOMSON
 DATE: 17 August 1988

CHANCELLOR

cc Economic Secretary
 Sir G Littler o/r
 Mr Lankester
 Mr Mountfield o/r
 Mr Bottrill o/r
 Mr Walsh o/r
 Ms Life

ARGENTINA: BRIDGING FINANCE

You may have seen Press reports that the US Treasury is arranging a bridging loan of \$500 million for Argentina. The money is needed to pay interest due over 90 days ago to commercial banks which, if not paid, would lead to US banks placing the loans on a non-accrual basis. (Argentina did not make the last two drawings under its last stand-by arrangement because of financing problems and failure to meet performance criteria. Talks have started with the IMF for a new SBA - reportedly for \$1.2 billion: the economic measures taken on 2 August (10% devaluation of the austral, 25% increase in public salaries followed by a 60 day freeze, a reduction in interest rates and price controls) are part of an overall package that has been discussed with Fund staff.)

2. In February this year the US Treasury itself provided a bridging loan to Argentina of \$500 million (which was repaid in June). This time the US is suggesting a joint loan through the BIS, with \$250-280 million for the US and the remainder from the participating central banks. The Bank of England has not been asked to contribute (it was also not asked in March 1987) but has seen the telex sent to eleven other central banks inviting their reactions to the proposals.

3. There are a number of features which concern us about the arrangements notified in the telex. The bridging finance would be made available before an IMF programme was in place - possibly before a letter of intent was signed - on the strength of a statement from the President of the World Bank that two World Bank

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loans had become effective. These proposals are explained in a letter from Camdessus to Lamfalussy, reproduced in the telex. The bridge would be repaid from disbursements from the World Bank loans.

4. If the other central banks agree to these conditions it will create two undesirable precedents for future bridging operations. It is unprecedented in recent years for a bridging loan to be paid before, at the least, a letter of intent with the IMF has been signed. (The only previous one was Mexico's 1982 bridging loan). Secondly, although World Bank loans have been used as part of the repayment of a bridge before they have never been the sole source of repayment. With no certainty that a Fund programme would be agreed, some of the Bank's lending would simply go on to other creditors who would not provide funding (commercial banks) or reschedule (Paris Club) without an IMF programme.

5. Breaking the linking between policy based lending and an IMF programme also represents a major weakening of conditionality in the World Bank. The two World Bank loans concerned should require an SBA to be in place before they become effective. They support policy reforms in the Trade and banking sectors which will have little effect without a sound macroeconomic framework.

6. We are now expecting the BIS to draft a loan agreement on these terms by the end of this week. Banks' shares will be similar to October 1987. As non-participants we do not have any basis to intervene on the terms of the bridging loan but if it seems likely that the loan will go ahead on these terms we shall be taking up our concerns about Fund and Bank conditionality with staff. We understand that Bank of England will suggest that the Governor takes up these points next month in Basle.

8
MRS S THOMSON
n/c.

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TO PRIORITY FCO
TELNO 300
OF 191510Z AUG 88
INFO PRIORITY BANK OF ENGLAND, WASHINGTON

ARGENTINA: NEW ECONOMIC MEASURES
BISBA TELNO 281

SUMMARY

1. THE GOVERNMENT'S IMPROVISED MEASURES ARE ENJOYING TEMPORARY SUCCESS. 25 PERCENT RETAIL PRICE INFLATION EXPECTED IN AUGUST BUT SEPTEMBER INFLATION SHOULD BE MUCH LOWER. FREELY FLOATING EXCHANGE RATE RELATIVELY CALM DUE TO POSITIVE REAL INTEREST RATES. BUT OMENS NOT PROMISING. MAJOR UNKNOWN IS WAGE BEHAVIOUR. GOVERNMENT FIGURES EXAGGERATE REDUCTION IN FISCAL DEFICIT. GOVERNMENT UNLIKELY TO HOLD LINE ON PRICES BEYOND TWO MONTHS.

DETAIL

2. TWO WEEKS AFTER THE INTRODUCTION OF THE NEW PLAN THE PICTURE IS A LITTLE CLEARER.

BACKGROUND

3. THE GOVERNMENT WERE FORCED BY DELIBERATE LEAKS TO BRING THE PLAN FORWARD FROM MID-AUGUST AND IT HAS THE MARK OF IMPROVISATION. PRESSURE FROM THE AGRICULTURAL AND INSUTRAIL SECTORS ALSO FORCED THE GOVERNMENT TO GRANT LAST-MINUTE CONCESSIONS. THE AGRICULTURE LOBBY SECURED A FURTHER REDUCTION IN AGRICULTURAL EXPORT DUTIES AND REDUCTION TO 50 PERCENT (RATHER THAN 100 PERCENT AS ORIGINALLY PLANNED) OF INDUSTRIAL EXPORTS TO BE TRADED AT THE FINANCIAL RATE. IN COMPENSATION THE INDUSTRIALISTS WERE GRANTED RETENTION OF THE SYSTEM OF TAX REIMBURSEMENTS ON EXPORTS AND A REDUCTION OF VAT FROM 18 TO 15 PERCENT (WHICH ALONE WILL REDUCE REVENUE BY APPROX US DOLLARS 350 PA MILLION ACCORDING TO OFFICIAL STATISTICS).

4. THE SUBSTANTIAL PRICE INCREASES GRANTED IMMEDIATELY BEFORE THE PLAN ON 1 AUGUST MEAN THAT MEASURED INFLATION FOLLOWING THE FIRST MONTH OF IMPLEMENTATION WILL BE OVER 25 PERCENT RETAIL AND ANYTHING UP TO 40 PERCENT WHOLESALE. ONLY AT THE END OF SEPTEMBER WILL OFFICIAL STATISTICS REGISTER SUBSTANTIALLY LOWER INFLATION.

FISCAL DEFICIT

5. THE LATIN AMERICAN ECONOMIC RESEARCH FOUNDATION (FIEL) HAVE

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ARGUED THAT THE MAIN REDUCTION IN THE QUASI-FISCAL DEFICIT (ON A CASH-FLOW RATHER THAN IMPUTED PAYMENTS BASIS) WILL COME FROM THE CHANGES IN THE WAY THE CENTRAL BANK REMUNERATES BANKING SECTOR RESERVE REQUIREMENTS AND FORCED DEPOSITS. INITIAL ESTIMATES SUGGEST THIS COULD REDUCE THE QUASI-FISCAL DEFICIT BY 2 TO 3 PERCENT -AGE POINTS OF GDP. FIEL CALCUALTE THAT THE EXCHANGE RATE MODI- FICATIONS WILL YIELD US DOLLARS 205 MILLION, IE APPROXIMATELY 0.4 PERCENT OF GDP, IN THE REMAINDER OF 1988. (THIS ASSUMES A 20 PERCENT GAP BETWEEN THE FINANCIAL AND COMMERCIAL RATES, AGRICULTURAL EXPORTS OF (MILLION DOLLARS) 1700, AGRICULTURAL IMPORTS OF 50, INDUSTRIAL EXPORTS OF 1350 AND INDUSTRIAL IMPORTS OF 2700.) THIS IS IN LINE WITH OFFICIAL ESTIMATES. SINCE FIEL AND OTHER LEADING PRIVATE SECTOR CONSULTANTS (EG FUNDACION MEDITERRAN- EA) CALCULATE THE CURRENT COMBINED FISCAL DEFICIT AT APPROXIMATELY 10 PERCENT OF GDP, THE MEASURES WILL REDUCE THIS FIGURE TO APPROX 6.5/7 PERCENT. THIS IS OF COURSE NOWHERE NEAR THE GOVERNMENT'S CLAIMED 1.5 PERCENT.

EXCHANGE MARKET

6. THE FREELY FLOATING FINANCIAL DOLLAR HAS SO FAR REMAINED REASONABLY STABLE. THIS WAS TO BE EXPECTED IN THE EARLY STAGES OF THE PLAN. DESPITE HIGH MEASURED INFLATION, ACTUAL INFLATION FROM 2 AUGUST WILL BE LOW BECAUSE OF THE LARGE PREEMPTIVE PRICE INCREASES. REAL RATES OF INTEREST ARE THEREFORE HIGHLY POSITIVE DESPITE THE FALL IN NOMINAL RATES. WITH THE COMMERCIAL EXCHANGE RATE FROZEN UNTIL THE END OF SEPTEMBER, TRADERS HAVE A STRONG INCENTIVE TO SELL THE DOLLARS GAINED FROM EXPORTS AND PLACE THE MONEY ON DEPOSIT IN AUSTRALES. SIMILARLY, THEY HAVE AN INCENTIVE TO BRING FORWARD EXPORTS AS MUCH AS POSSIBLE AND DELAY IMPORTS. HENCE A STRONG SUPPLY OF DOLLARS AND DEMAND FOR AUSTRALES KEEPING THE FINANCIAL EXCHANGE RATE DOWN.

7. THE QUESTION IS HOW LONG THIS CAN LAST. EXPECTATIONS ARE CRUCIAL. ONCE THE TRADERS EXPECT THE FIXED RATE TO BE DEVALUED, INCENTIVES WILL WORK THE OTHER WAY AND FORCE A DEVALUATION SOONER THAN PLANNED IF THE 20 PERCENT GAP BETWEEN THE TWO RATES IS TO BE MAINTAINED. AFTER THE INTRODUCTION OF THE PLAN THE GAP BETWEEN THE FREELY FLOATING AND FIXED COMMERCIAL EXCHANGE RATES FELL TO 12 PERCENT. IT HAS SINCE RISEN TO ABOUT 19 PERCENT AND PEOPLE ARE ALREADY WONDERING WHETHER THE GOVERNMENT WILL BE ABLE TO HOLD THE COMMERCIAL RATE FIXED UNTIL THE END OF SEPTEMBER (WHICH THEY HAVE SAID THEY WILL) DESPITE THE DAILY AUCTIONS OF 30 MILLION US DOLLARS.

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PRICES

8. SINCE THE ANNOUNCEMENTS THE GOVERNMENT HAVE NEGOTIATED FURTHER AGREEMENTS WITH THE BUSINESS SECTOR TO REINFORCE PRICE RESTRAINT. THEIR ABILITY TO DO SO REFLECTS THE SIZE OF THE INCREASES BEFORE 2 AUGUST (IN SOME CASES AS MUCH AS 70 PERCENT). THE LEADING FIRMS THEREFORE HAVE SOME MARGIN FOR MANOEUVRE. SMALLER RETAIL FIRMS HAVE CONTINUED TO MARK UP PRICES AFTER 2 AUGUST. DESPITE THE AGREEMENTS THE CHANCES OF THE GOVERNMENT CONTROLLING PRICES BEYOND A BREATHING SPACE OF TWO MONTHS LOOK SLIM.

WAGES

9. WAGE BEHAVIOUR REMAINS A MAJOR QUESTION MARK. THE GOVERNMENT'S STRATEGY APPEARS TO ASSUME THAT THE PRIVATE SECTOR, HELPED BY DEPRESSED DOMESTIC DEMAND, WILL BE ABLE TO CONTAIN WAGE DEMANDS. IN THE PUBLIC SECTOR THEY HAVE GIVEN SELECTIVE INCREASES IN REAL WAGES IN AN ATTEMPT TO KEEP THE UNIONS SWEET. BUT REAL WAGES IN GENERAL HAVE CONTINUED TO FALL OR REMAIN LOW THROUGHOUT 1988 AND, AFTER INFLATION OF OVER 25 PERCENT IN AUGUST, THE UNIONS ARE UNLIKELY TO BE IN THE MOOD TO ACCEPT FURTHER CUTS. THE LARGEST AND MOST INFLUENTIAL PRIVATE SECTOR UNIONS, THE METALLURGICAL WORKERS UNIONS (UOM), HAS JUST OPENED NEGOTIATIONS FOR A 55 PERCENT WAGE INCREASE. MANY LEADING UNIONS, UOM INCLUDED, ALSO HOLD ELECTIONS IN THE NEXT FEW MONTHS, A FURTHER SPUR TO MILITANCY.

CONCLUSION

10. THE AGRICULTURAL SECTOR AND THE TRADES UNIONS ARE MAINTAINING A BARRAGE OF CRITICISM. BUSINESS IN GENERAL AND NON-GOVERNMENT ECONOMISTS ARE EXTREMELY SCEPTICAL OF THE PROSPECTS OF THE PLAN SUCCEEDING FOR MORE THAN A COUPLE OF MONTHS. THE GOVERNMENT APPARENTLY DARE NOT GRASP THE NETTLE OF A CUT IN GOVERNMENT EXPENDITURE WHICH WOULD THROW PUBLIC SECTOR EMPLOYEES INTO THE STREETS. CONFIDENCE REMAINS A SCARCE COMMODITY. ALL THE OLD PROBLEMS LOOK LIKELY TO RETURN BY EARLY OCTOBER.

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TELNO 178
OF 232300Z AUGUST 88
AND TO PRIORITY BIS BUENOS AIRES

YOUR TELNO 139: ARGENTINE BRIDGE LOAN

I HAVE SPOKEN TO BEZA (DIRECTOR, WHD) ON THE LINES OF PARA 5 OF TUR AND EXPRESSED OUR WORRIES ABOUT THE IMPLICATIONS OF THE PROPOSED BRIDGING LOAN FOR THE STATUS OF THE IMF ITSELF. I WILL SPEAK TO BANK STAFF WHEN THEY RETURN FROM MISSION IN ARGENTINA NEXT WEEK.

2. BEZA EXPRESSED MILD SURPRISE AT MY CONCERNS, THOUGH HE ACCEPTED THAT BRIDGES DID CHANGE THE WAY IN WHICH PARTICIPATING COUNTRIES LOOKED AT THE CONDITIONS ATTACHED TO THE CREDIT THAT WOULD REPAY THE LOAN. OVERALL, HE SAW THE APPROACH TAKEN TO THE BRIDGE LOAN AS HELPFUL TO THE FUND AS IT WOULD RELIEVE PRESSURE ON THE FUND MANAGEMENT AND BOARD TO RUSH THROUGH AN INADEQUATE PROGRAMME. HE AGREED HOWEVER THAT IT COULD GENERATE SIMILAR PRESSURE ON THE BANK. DIRECT LINKAGE TO A LETTER OF INTENT (LOI) WOULD HAVE GIVEN RISE TO SUCH PRESSURE, AND FUND MANAGEMENT WERE ANXIOUS TO AVOID SUCH A SITUATION IN THE LIGHT OF PAST BOARD CRITICISM. NONETHELESS, THE BRIDGE WAS IMPORTANT, BOTH BECAUSE OF COMMERCIAL BANK ARREARS (ABOUT WHICH THE AMERICANS WERE PARTICULARLY CONCERNED) AND AS A SIGNAL OF INTERNATIONAL SUPPORT FOR ARGENTINA.

3. BEZA ARGUED THAT THE MOST OBVIOUS OPTION WOULD HAVE BEEN TO BRIDGE TO THE CURRENTLY UNDISBURSED PORTION OF THE PRESENT SBA (ABOUT SDR 300M), BUT THIS WAS REJECTED BECAUSE OF ARGENTINA'S POOR PROGRESS UNDER THE PROGRAMME. THE MD HAD ALSO REJECTED APPROVAL IN PRINCIPLE (AIP) OF A NEW PROGRAMME, IN VIEW OF CRITICISMS OF THE MAJOR REVISIONS TO THE PRESENT SBA BETWEEN AIP AND EFFECTIVENESS AND THE RISK OF THIS SITUATION RECURRING. IT WAS THEREFORE PROPOSED TO AWAIT CRITICAL MASS, WHICH MIGHT BE ACHIEVED IN NOVEMBER/DECEMBER, AND TO SEEK OUTRIGHT APPROVAL FROM THE BOARD THEN. MEANWHILE, A LOI WOULD BE NEGOTIATED (A FUND MISSION IS TO DEPART FOR ARGENTINA NEXT WEEK), AND COULD BE AGREED IN SEPTEMBER - ALTHOUGH BEZA WAS EXTREMELY CAUTIOUS ABOUT TIMING. THIS APPROACH WOULD ALSO ALLOW MANAGEMENT TO ASSESS PERFORMANCE UNDER THE PROGRAMME BEFORE BRINGING IT TO THE

BOARD. HE ATTACHED GREAT IMPORTANCE TO SECURING TIME TO LOOK AGAIN AT ARGENTINA'S TRACK RECORD.

4. BEZA CONFIRMED THAT CONABLE MIGHT NOT AWAIT AGREEMENT OF A LOI BEFORE MAKING TPL II AND BSL EFFECTIVE, BUT THAT THERE WOULD BE CONSULTATION BETWEEN BANK AND FUND ON THE MACROECONOMIC SITUATION. AS HE SAW IT THERE WOULD BE AN INDIRECT LINKAGE BETWEEN THE REPAYMENT OF THE BRIDGING LOAN AND PROGRESS ON A FUND PROGRAMME.

5. FCO PLEASE PASS TO WALSH (HMT), WARE (BOE) AND BREACH (ECGD).

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FROM: MISS M P WALLACE
DATE: 24 August 1988

MRS S THOMSON

cc Economic Secretary
Sir G Littler
Mr Lankester
Mr Mountfield
Mr Bottrill
Mr Walsh
Ms Life

pyo

ARGENTINA: BRIDGING FINANCE

The Chancellor was grateful for your minute of 17 August. He has commented that he very much hopes the Governor will raise our concerns about these arrangements in Basle.

M. P. Wallace

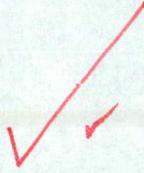
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AND TO ROUTINE BANK OF ENGLAND
AND TO ROUTINE HM TREASURY



ECUADOR: EMERGENCY ECONOMIC PACKAGE

1. AN EMERGENCY ECONOMIC PACKAGE WAS ANNOUNCED LAST NIGHT. IT HAS THE EXPRESSED INTENTIONS OF REDUCING INFLATION TO 30 PER CENT WITHIN 12 MONTHS, STABILISING EXTERNAL TRADE AND THE EXCHANGE RATE, BRINGING THE ECONOMY UNDER CLOSER GOVERNMENT CONTROL AND REDUCING THE BUDGET DEFICIT THROUGH PUBLIC SPENDING CUTS AND INCREASED TAXES:

2. MAIN MEASURES ARE:

A) ALL PRIVATE SECTOR EXPORT GENERATED FOREIGN CURRENCY MUST BE SOLD TO THE CENTRAL BANK, WHOSE INTERVENTION RATE HAS BEEN DEVALUED FROM 250 TO 390 SUCRES/US DOLLAR. 90 PER CENT OF THIS FOREIGN CURRENCY WILL BE USED TO FINANCE PRIORITY PRIVATE SECTOR IMPORTS. THE OTHER 10 PER CENT WILL BE USED TO REBUILD MONETARY RESERVES. THE INTERVENTION RATE WILL BE FURTHER DEVALUED EACH WEEK BY 2.5 (TWO AND A HALF) SUCRES.

B) ALL FUEL PRICES (EXCEPT THOSE FOR REGULAR GRADE PETROL AND KEROSENE -BOTH WIDELY USED AS COOKING FUELS- ARE INCREASED E.G. THE MOST COMMONLY USED 82 OCTANE PETROL HAS BEEN DOUBLED IN PRICE FROM 90 TO 180 SUCRES PER US GALLON.

C) A LIMIT IS TO BE PLACED IMMEDIATELY ON THE MARGIN BETWEEN INTEREST RATES PAID TO INVESTORS AND CHARGED TO BORROWERS WHICH MEANS EFFECTIVELY THAT RATES TO BORROWERS WILL BE REDUCED:

D) IMPORTS OF VEHICLES (BOTH PUBLIC AND PRIVATE SECTOR) ARE BANNED AND CAPITAL GOODS IMPORTS WILL NOW ONLY BE ALLOWED IF FINANCED BY AN INTERNATIONAL CREDIT ORGANIZATION:

E) TAXES ARE TO BE INCREASED ON CIGARETTES, BUSINESS TRANSACTIONS

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AND IMPOSED ON DEBT SUCRETISATION STABILISATION CREDITS AND LUXURY VEHICLES.

F) ELECTRICITY PRICES ARE TO RISE BY AN AVERAGE OF 30 PER CENT ACROSS THE BOARD.

G) NATIONAL MINIMUM WAGE IS INCREASED FROM BASIC 19,000 TO 22,000 SUCRES PER MONTH.

3. FURTHER DETAIL AND COMMENT FOLLOW BY BAG.

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TELECON LOW-ROUSE OF 2 SEPTEMBER

MINISTERIAL CHANGES

1. THE PICTURE IS NOW CLEARER. LATE ON THURSDAY 1 SEPTEMBER THE MINISTER FOR ECONOMY AND FINANCE, ROBLES FREYRE, FELT OBLIGED TO RESIGN IN THE FACE OF CABINET OPPOSITION TO HIS PROPOSED PACKAGE OF ECONOMIC MEASURES WHICH SOME COLLEAGUES CONSIDERED INSUFFICIENTLY HARSH. AS IS CUSTOMARY THE ENTIRE CABINET THEN PLACED THEIR PORTFOLIOS AT THE PRESIDENT'S DISPOSAL.

2. DURING THE COURSE OF FRIDAY 2 SEPTEMBER, GARCIA TOOK THIS OPPORTUNITY TO MAKE FIVE CHANGES IN ALL WITH THREE NEW FACES AND TWO MINISTERS RESHUFFLED. ALONG WITH ROBLES FREYRE, OUT WENT ARTEGA AT INDUSTRY AND MAUROY AT TRANSPORT AND COMMUNICATIONS. ABEL SALINAS IZAGUIRRE WAS MOVED SIDEWAYS FROM ENERGY AND MINES TO TAKE OVER ECONOMY AND FINANCE AND WAS REPLACED BY JOSE CARLOS CORRASCO TAVARA, THE APRA DEPUTY FOR PIURA. TRANSPORT AND COMMUNICATIONS WENT TO CAMILO CARRILLO, THE JUSTICE MINISTER, WHO WAS REPLACED BY CESAR AUGUSTO DELGADO BARRETTO, A CHRISTIAN DEMOCRAT. FINALLY ARTEGA'S JOB AT INDUSTRY WAS TAKEN BY IVAN GARCIA CABREJOS, CHAIRMAN OF THE GOVERNMENT STEEL CORPORATION, SIDERPERU.

3. IT IS NO SURPRISE THAT GARCIA TOOK THE OPPORTUNITY TO REMOVE ARTEGA WHO HAD BECOME A BIT OF AN EMBARRASSMENT WITH HIS HABIT OF SOUNDING OFF UNILATERALLY. MAUROY WAS ANONYMOUS AND HAD MADE LITTLE IMPACT AT TRANSPORT AND COMMUNICATIONS.

4. PERSONALITY NOTES FOR LPRS FOLLOW ON THE NEWCOMERS BY NEXT BAG.

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AND TO ROUTINE GUATEMALA CITY, PANAMA CITY
INFO SAVING CARACAS, BOGOTA, LIMA, LISBON, BRASILIA, MONTEVIDEO,
INFO SAVING HAVANA

COSTA RICA: GOVERNMENT CHANGES
SUMMARY

1. LIMITED MINISTERIAL RESHUFFLE BY PRESIDENT ARIAS, PRINCIPALLY IN
ECONOMIC SECTOR, REINFORCES ORTHODOX MONETARIST FACTION. CHANGES
RECEIVE GENERAL APPROVAL.

DETAIL:

2. THE FOLLOWING MINISTERIAL APPOINTMENTS WERE ANNOUNCED
ON 2 SEPTEMBER:-

INTERIOR AND POLICE: ANTONIO ALVAREZ DESANTI (FROM AGRICULTURE)

FOREIGN TRADE: LUIS DIEGO ESCALANTE (FROM COMMERCE AND INDUSTRY)

ECONOMY: ANTONIO BURGUES TERAN (PROMOTION FROM VICE-MINISTER)

PLANNING: JORGE MONGE AGUERO (FORMER ADVISER TO THE PRESIDENCY)

AGRICULTURE: JOSE MARIA FIGUERES (FROM FOREIGN TRADE)

THE FOLLOWING OTHER CHANGES WERE MADE:-

VICE-MINISTER OF ECONOMY: SANDRA PISZK (FROM PLANNING)

VICE-MINISTER OF PLANNING: FERNANDO HERRERA ACOSTA

VICE-MINISTER OF NATURAL RESOURCES, ENERGY AND MINES:
JORGE RODRIGUEZ QUIROS

(BOTH FORMER SENIOR OFFICIALS IN THEIR RESPECTIVE MINISTRIES)

VICE-MINISTER OF FOREIGN TRADE: EDGAR BRENES ANDE (FORMER PRESIDENT
OF STATE HOLDING COMPANY, CODESA)

OTHER APPOINTMENTS:-

PRESIDENT OF THE COSTA RICAN ELECTRICITY INSTITUTE (ICE):
TEOFILO DE LA TORRE (FORMER VICE-MINISTER OF NATIONAL RESOURCES)

PRESIDENT OF CODESA: JOSE MANUEL SALAZAR XIRINACH

DIRECTOR-GENERAL OF TELECOMMUNICATIONS OF ICE : ANTONIO CANAS MORA

MINISTERS WHO HAVE BEEN REPLACED:-

OTTON SOLIS FALLAS OF PLANNING

ROLANDO RAMIREZ PANIAGUA OF INTERIOR AND POLICE (RECENTLY ELECTED
PRESIDENT OF THE CENTRAL AMERICAN BANK FOR ECONOMIC
INTEGRATION) (BCIE)

VICE-MINISTER OF COMMERCE: EDUARDO ALONSO

VICE-MINISTER OF INTERIOR AND POLICE: PABLO RODRIGUEZ OCONTRILLO

COMMENT

2. A NEW APPOINTMENT TO INTERIOR AND POLICE WAS INEVITABLE FOLLOWING RAMIREZ'S MOVE TO THE PRESIDENCY OF BCIE, AND IT WAS NOT UNUSUAL FOR HIS VICE-MINISTER TO OFFER HIS RESIGNATION AT THE SAME TIME. HIS SUCCESSOR, ALVAREZ DESANTI, IS VERY YOUNG AND HAS NO EXPERIENCE IN THE PORTFOLIO SEMI COLON HIS MOVE FROM AGRICULTURE IS A REFLECTION OF THE PROBLEMS WITH PEASANT FARMERS WHICH DESANTI HAS FAILED TO RESOLVE. HIS REPLACEMENT, JORGE MONGE, IS PROBABLY CLOSER TO THE PRESIDENT. DIEGO ESCALANTE TAKES WITH HIM HIS FORMER RESPONSIBILITIES FOR TOURISM AND COFFEE SEMI COLON PRESERVING CONTINUITY IN THE LATTER IS USEFUL FOR ICA NEGOTIATIONS. THE DEPARTURE OF OTTON SOLIS IS SEEN AS A VICTORY FOR THE ORTHODOX MONETARISTS, THE MINISTER OF FINANCE AND THE PRESIDENT OF THE CENTRAL BANK, IN THEIR DIFFERENCES OVER THE HANDLING OF THE ECONOMY AND THE REFORM OF THE BANKING LAWS SEMI COLON SOLIS WAS OPPOSED TO PROVISIONS OF THESE WHICH PROMOTED PRIVATE BANKS UNDER CERTAIN CONDITIONS TO ACCEPT DEPOSITS. HOWEVER, PRIVATISATION GENERALLY MAY LOSE A STRONG ADVOCATE WITH HIS DEPARTURE (HE WANTS TO RESUME HIS STUDIES IN THE UK THOUGH NOT, AS THE PRESS HAS SUGGESTED, COMBINE THIS WITH BEING AMBASSADOR).

3. THE CHANGES HAVE GENERALLY BEEN ACCORDED A CAUTIOUS WELCOME AS GIVING MORE COHESION TO THE GOVERNMENT'S ECONOMIC POLICIES.

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ENTHUSIASM FOR THE APPOINTMENTS BY THE CHAMBER OF INDUSTRIES
CONTRASTS WITH STRONG RESERVATIONS FROM SOME UNIONS. FURTHER
COMMENTS AND LPRS WILL FOLLOW BY BAG.

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FROM: A C S ALLAN
DATE: 7 September 1988

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MRS S THOMSON

cc PS/Economic Secretary
Sir G Littler
Mr Lankester
Mr Mountfield
Mr Bottrill
Mr Walsh
Ms Life

ARGENTINA: BRIDGING FINANCE

Further to Miss Wallis' minute of 24 August, the Chancellor raised this point at lunch with the Governor yesterday: the Governor said he had already given notice that he would be raising this at Basle, and would more generally be pressing for criteria for bridging loans to be established.

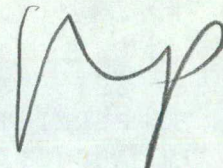
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(CULL)

PERU : THE BELT TIGHTENS

SUMMARY

1. ON 6 SEPTEMBER SALINAS, NEW MINISTER OF ECONOMY ANNOUNCED PACKAGE OF MEASURES AIMED AT CURBING INFLATION, REDUCING FISCAL DEFICIT AND STIMULATING EXPORTS. MEASURES INCLUDE SUBSTANTIAL PRICE RISES (SEMI COLON) INCREASES IN INDIRECT TAXATION (SEMI COLON) PUBLIC SPENDING CUTS (SEMI COLON) A SINGLE EXCHANGE RATE (SEMI COLON) 150 PERCENT RISE IN MINIMUM WAGE AND A PRICE FREEZE FOR 120 DAYS.

DETAIL

2. THE ANNOUNCEMENT ON 6 SEPTEMBER OF A SERIES OF STIFF ADJUSTMENT MEASURES PUT AN END TO WEEKS OF UNCERTAINTY DURING WHICH THE MERITS OF GRADUALIST OR SHOCK TACTICS FOR DEALING WITH THE ECONOMIC CRISIS WERE DEBATED AND HOARDING BY TRADERS LED TO PROGRESSIVE SHORTAGES, IN PARTICULAR OF ESSENTIAL FOODSTUFFS. THE MEASURES, AIMED AT COMBATTING INFLATION ARE FOCUSED ON PRICES, THE FISCAL DEFICIT AND THE EXCHANGE RATE.

PRICES

3. THE PRICES OF A RANGE OF PRICE CONTROLLED GOODS (FOOD, CEMENT, PETROL) HAVE BEEN INCREASED BY BETWEEN 100 PERCENT AND 270 PERCENT (PETROL) WITH IMMEDIATE EFFECT. UTILITIES, MANUFACTURERS AND RETAILERS HAVE BEEN GIVEN 10 DAYS TO NOTIFY INCREASES IN PRICES FOR ALL OTHER GOODS AND SERVICES SUBJECT TO PRICE CONTROL : THE NEW PRICES TO BE HELD FOR 120 DAYS.

EXCHANGE RATE

4. A SINGLE EXCHANGE RATE OF INTIS/250 TO 1 US DOLLAR

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HAS BEEN SET, TO BE HELD FOR 120 DAYS. BUT TRANSACTIONS WILL STILL BE PERMITTED AT THE FREE MARKET RATE, CURRENTLY AT A LITTLE ABOVE INTIS/300 TO THE US DOLLAR, FOR NON ESSENTIAL IMPORTS/EXPORTS.

FISCAL DEFICIT

5. GENERAL SALES TAX HAS BEEN INCREASED (AGAIN) FROM 30 PERCENT TO 40 PERCENT, CONSUMPTION TAX BY 10 PERCENT AND A 4 PERCENT TAX WILL BE LEVIED ON THE FOB VALUE OF ALL EXPORTS. IN ADDITION, A LARGE NUMBER OF TAX EXEMPTIONS ARE TO BE ABOLISHED. OTHER MEASURES TO REDUCE GOVERNMENT EXPENDITURE - FREEZE ON RECRUITMENT, CLOSING EMBASSIES AND CONSULATES, RECALLING OTHER GOVERNMENT SERVANTS ABROAD AND SALE OF GOVERNMENT VEHICLES HAVE ALSO BEEN ANNOUNCED. THE UNIFICATION OF THE EXISTING EXCHANGE RATE WILL ABOLISH THE SUBSIDY FOR IMPORTED FOOD STUFFS AND PHARMACEUTICALS.

WAGES

6. TO MITIGATE THE SEVERITY OF THESE MEASURES, THE MINIMUM WAGE (AFFECTING 2 MILLION PERUVIANS) IS TO BE RAISED BY 150 PERCENT ANPD HELD, LIKE THE OTHER MEASURES, FOR 120 DAYS. THE EMERGENCY EMPLOYMENT PLAN (PAIT) IS ALSO TO BE REACTIVATED TO PROVIDE 200,000 JOBS - MOSTLY IN PUBLIC WORKS.

FOREIGN CREDIT

7. DURING HIS ANNOUNCEMENT, SALINAS SAID PERU WOULD INTENSIFY HER RELATIONS WITH THE INTERNATIONAL INSTITUTIONS MENTIONING SPECIFICALLY THE WORLD BANK, THE INTERAMERICAN BANK AND THE ANDEAN RESERVE FUND. HE ALSO SAID THAT PERU WOULD SEEK 'MUCH MORE SUPPORT FROM THE COUNTRIES OF WESTERN EUROPE AND FROM CANADA'. FOREIGN INVESTMENT WOULD BE SOUGHT FOR THE MINING, PETROLEUM (SIC) AND FISHING SECTORS.

REACTIONS

8. WHILE NO-ONE CONTESTS THE NEED FOR DECISIVE ACTION TO CONFRONT THE ECONOMIC CRISIS NOR THE NEED FOR PERU TO TIGHTEN HER BELT, THE TIMING, CONTENT, SCOPE, IMPACT AND PRESENTATION OF THE GOVERNMENT'S PACKAGE HAVE ALL, PREDICTABLY, ATTRACTED CRITICISM FROM ACROSS THE POLITICAL SPECTRUM. LEFT WING SPOKESMEN HAVE POINTED TO THE HARDSHIP THAT THE POOR WILL HAVE TO BEAR WHILE CENTRIST AND RIGHT WING SPOKESMEN HAVE CAST DOUBTS ON WHETHER THE MEASURES WILL SUCCEED IN GETTING THE CRISIS UNDER CONTROL. THE UNIONS ARE EXPECTED TO MOUNT A NATIONAL STRIKE.

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COMMENT

9. GARCIA HAS AT LAST BOWED TO THE INEVITABLE. IT HAS TAKEN NINE MONTHS OF DRIFT AND MUDDLE DURING WHICH HIS GOVERNMENT'S CREDIBILITY HAVE SUFFERED GREAT DAMAGE. BUT WHEREAS ON JULY 28 HE HIMSELF PROCLAIMED THE GOVERNMENT'S COMMITMENT TO DEALING WITH TERRORISM, THE GOVERNMENT SPOKESMAN ON THE ECONOMIC CRISIS ON 6 SEPTEMBER, WAS NOT THE PRESIDENT, NOR THE PRIME MINISTER BUT THE ECONOMICS MINISTER WHO HAS BEEN IN OFFICE A WEEK.

10. BEFORE SALINAS SPOKE, INSPIRED LEAKS TO THE MEDIA HINTED AT A PLAN ZERO IE ZERO INFLATION. IN FACT, DURING HIS ADDRESSSS HE ESCHEWED ANY MENTION OF SPECIFIC TARGETS. THIS MAY REFLECT THE STRUGGLE THAT CONTINUED RIGHT UP TO HIS SEVERAL TIMES POSTPONED BROADCAST BETWEEN THE HARDLINERS AND THE ADVOCATES OF THE GRADUALIST APPROACH. THE SEVERITY AND COHESION OF THE ORIGINAL PLAN WAS DILUTED.

11. AS THEY STAND THE MEASURES REFLECT THE CONTRADICTIONS THAT REMAIN AT THE HEART OF THE GOVERNMENT'S APPROACH TO ECONOMIC POLICY. THE NINE MONTH'S DELAY IN ADOPTING MEASURES TO STABILISE THE ECONOMY AROSE FROM GARCIA'S FEARS ABOUT POPULAR REACTIONS TO AUSTERITY AND HIS REFUSAL TO RESILE FROM HIS DEFIANCE OF THE IFIS BOTH OF WHICH ARE STILL EVIDENT IN THE NEW MEASURES. THE ACTIVITIES OF THE PAIT EMPLOYMENT PROGRAMME WILL MAKE INROADS INTO THE EFFORT TO TRIM PUBLIC EXPENDITURE, WHILE THE REFERENCES TO RESUMING RELATIONS WITH THE INTERNATIONAL COMMUNITY ARE AT BEST HALF HEARTED. THE TIME LIMITS ON PRICES, WAGES AND THE EXCHANGE RATE MAY BE REGARDED AS WEAKNESSES IN SO FAR AS THEY UNDERLINE THE PROVISIONAL NATURE OF THESE NEW LEVELS AND THUS WEAKEN CONFIDENCE AND ENCOURAGE SPECULATION. NEVERTHELESS, FOR ALL ITS EVIDENT SHORTCOMINGS, THE NEW APPROACH IS A WELCOME AND COURAGEOUS ATTEMPT TO CONFRONT REALITY. WE MUST HOPE THAT IT WILL HAVE SOME SUCCESS AND THAT ENCOURAGED BY THAT THE GOVERNMENT WILL TAKE FURTHER SUPPORTIVE MEASURES. THE BRUTAL NATURE OF THE ADJUSTMENTS PARTICULARLY FOR THE POOR, THE MAJORITY, AND THE CONSEQUENTLY RISKY COURSE THE GOVERNMENT HAS EMBARKED UPON CAN BE GAUGED BY NOTING THE GOVERNMENT'S TWICE REPEATED WARNING THAT LIMA AND CERTAIN OTHER DEPARTMENTS (OR PROVINCES) ARE FORMALLY UNDER A STATE OF EMERGENCY AND THAT APPROPRIATE INSTRUCTIONS HAVE BEEN GIVEN TO THE MILITARY IN RELATION TO THE PRESERVATION OF PUBLIC ORDER.

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8 September 1988

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ACTION	Mr BOTTRILL
COPIES TO	EST. Sir P. MIDDLETON Sir G. LITTLER Sir T. BURNS Mr LAWKES Mr MOUNTFIELD Mr H.P. EVANS.

1/8/88

Dear Charles

Possible Meeting with the Argentine Foreign Minister at the UN General Assembly

There is strong possibility that Senor Caputo, the Argentine Foreign Minister, may be elected President of the UN General Assembly on 20 September. The Foreign Secretary will as usual be visiting the Assembly, from 25 to 30 September. In the normal course of events he would automatically pay a courtesy call on the President. This year, if Senor Caputo is elected, the case for such a call is naturally not automatic.

The easiest option would appear to be not to bother about a courtesy call at all. But this is not a cost free option. It would certainly be noticed in New York, and regarded as both a slight on the office of President and as an indication of an unconstructive approach towards Argentina. The Argentines (and others) could be relied upon to play up these points, if only to strengthen their own hand for the ritual Falklands debate which is likely to be in November.

In contrast, offering to pay such a call would provide us with some presentational opportunities. If Senor Caputo refuses, as he might, we would automatically have the advantage, and could play it up accordingly if we wanted to. If he accepts, it will enable us to demonstrate that it is perfectly possible to have normal and sensible contacts on matters of mutual interest with Argentina, provided sovereignty over the Falklands is kept off the table. Even if Senor Caputo were to raise the Falklands, the Foreign Secretary could make our position quite clear (yes to more normal relations; no to discussion of Falklands sovereignty) without entering into substantive discussion. We could say publicly that this was what had happened, if need be (for example if it led to public or media speculation of a "breakthrough" over the Falklands). We could also use such an occasion to advantage with the Americans, as further proof of our constructive intentions toward Argentina.

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The Foreign Secretary accordingly proposes to offer to pay a brief courtesy call on Senor Caputo, in his capacity as President of the UNGA. He will instruct the Governor in Port Stanley to reassure Falkland Island Councillors of the formal nature of any meeting before it takes place. He will, of course, give careful thought to the press handling of the call.

I am copying this letter to the Private Secretaries of OD members and to Trevor Woolley.

Yours ever

Boiler

(R N Peirce)
Private Secretary

C D Powell Esq
10 Downing Street

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INFO IMMEDIATE WEST BERLIN, WASHINGTON, BANK OF ENGLAND

MY TELNO 300: ARGENTINA: NEW ECONOMIC MEASURES

SUMMARY

1. THE ECONOMIC PLAN MAY SURVIVE LONGER THAN EXPECTED, CONCEIVABLY INTO NEXT YEAR. 12 PERCENT RETAIL PRICE INFLATION IS FORECAST FOR SEPTEMBER & OCTOBER INFLATION SHOULD BE LOWER. FOR MOST OF AUGUST AND SEPTEMBER THE FINANCIAL DOLLAR EXCHANGE RATE HAS REMAINED AT OR BELOW THE GOVERNMENT CEILING OF AUSTRALES 14.40. BUT THERE ARE MANY PITFALLS. AND THE LONG-TERM STRUCTURAL PROBLEMS REMAIN.

DETAIL

2. THE GOVERNMENT'S ECONOMIC PLAN LOOKS LIKE HOLDING UP LONGER THAN ORIGINALLY FORECAST BY MOST PEOPLE. MANY OBSERVERS ARE NOW PREPARED TO GIVE THE PLAN UNTIL THE END OF THE YEAR. SOME EVEN BELIEVE THE GOVERNMENT CAN KEEP INFLATION UNDER REASONABLE CONTROL UNTIL THE ELECTIONS NEXT MAY. THIS SHIFT IN PERCEPTION OF THE PLAN'S LIKELY SURVIVAL HAS IN TURN CONTRIBUTED TO ITS PROSPECTS OF LONGEVITY. BUT THERE ARE PLENTY OF POTENTIAL PITFALLS WHICH COULD RENDER THESE FORECASTS EXCESSIVELY OPTIMISTIC. AND SOONER OR LATER THE UNDERLYING STRUCTURAL DISTORSIONS WILL RE-EMERGE.

INFLATION

3. GOVERNMENT GUIDELINES ANNOUNCED AT THE PLAN'S INCEPTION HAVE GENERALLY HELD FIRM DURING SEPTEMBER. SEPTEMBER RETAIL PRICE INFLATION IS EXPECTED TO BE 12 PERCENT. THIS IS HIGHER THAN THE 8 PERCENT PREDICTED BY PRESIDENT ALFONSIN IN MID-MONTH AND IS LARGELY BECAUSE OF AGRICULTURAL PRICE INCREASES. BUT IT IS A SUBSTANTIAL REDUCTION ON THE 26.6 PERCENT IN AUGUST. AND THE INDICATORS SUGGEST A FURTHER FALL IN OCTOBER. VOLUNTARY RESTRAINT IS STILL BEING OBSERVED BY THE PRIVATE SECTOR, WHO HAVE AGREED TO MAINTAIN PRICES AT CURRENT LEVELS DURING OCTOBER. PUBLIC SECTOR TARIFFS AND WAGES ARE TO BE ALLOWED TO RISE 4 PERCENT IN OCTOBER AFTER BEING HELD STEADY IN SEPTEMBER.

ECONOMIC LIBERALIZATION

4. THE GOVERNMENT ARE PRESSING AHEAD WITH MEASURES TO OPEN THE

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ECONOMY. ON 21 SEPTEMBER 2100 PRODUCTS WERE ELIMINATED FROM THE ANNEX II LIST OF ITEMS REQUIRING IMPORT PERMITS. IMPORT TARIFF REFORMS WILL BE INTRODUCED IN OCTOBER, PROBABLY INVOLVING A 40 PERCENT TARIFF CEILING.

5. THESE MEASURES HAVE BEEN STRENOUSLY OPPOSED BY PRIVATE SECTOR MANUFACTURERS ALREADY IN THE GRIP OF RECESSION. INDUSTRIAL PRODUCTION CONTINUES TO DECLINE AND SUPERMARKETS REPORT A 40 PERCENT FALL IN DEMAND IN THE FIRST HALF OF SEPTEMBER.

6. THE GOVERNMENT'S HAND APPEARS TO HAVE BEEN FORCED BY THE NEED TO COMPLY WITH THE CONDITIONS NECESSARY TO OBTAIN WORLD BANK APPROVAL FOR THE TRADE POLICY LOAN. THIS PLUS APPROVAL FOR THE OTHER LOANS JUST ANNOUNCED IN BERLIN (ASSUMING BOARD APPROVAL) CLEARS THE WAY FOR DISBURSEMENT OF THE US TREASURY BRIDGING LOAN AND WILL STRENGTHEN ARGENTINA'S HAND IN TALKS WITH THE IMF AND PRIVATE CREDITOR BANKS.

EXTERNAL SECTOR

7. THE FOREIGN BANKS HAVE BEEN INCREASINGLY IRRITATED BY ARGENTINA'S FAILURE TO KEEP UP WITH DEBT INTEREST PAYMENTS. ARREARS ARE ESTIMATED AT AROUND US 1 BILLION DOLLARS. COMBINED WITH STRONG EXPORT EARNINGS THIS POLICY OF NON-PAYMENT HAS PERMITTED ARGENTINA TO BUILD UP SUFFICIENT RESERVES (CURRENTLY UNOFFICIALLY ESTIMATED AT US DOLLARS 3 BILLION) TO DEFEND THE FINANCIAL EXCHANGE RATE IN THE SHORT TERM.

8. THE GOVERNMENT'S EVIDENT ABILITY UNTIL NOW TO DEFEND A FINANCIAL RATE OF AUSTRALES 14.40 = 1 US DOLLAR HAS BEEN AN IMPORTANT FACTOR IN BOOSTING CONFIDENCE AND IN PRACTICE SO FAR INTERVENTION HAS BEEN RARELY NECESSARY. WITH A FIRM EXCHANGE RATE IT HAS BEEN RELATIVELY VERY PROFITABLE TO HOLD FUNDS IN AUSTRALES RATHER THAN DOLLARS. THIS WEEK HAS SEEN RENEWED DEMAND FOR DOLLARS AS INVESTORS TAKE PROFITS IN ADVANCE OF THE ANNOUNCED 3 PERCENT DEVALUATION DURING OCTOBER. BUT THE GOVERNMENT APPEAR CONFIDENT THEY STILL HAVE THINGS UNDER CONTROL.

POTENTIAL PITFALLS

9. DESPITE THE BETTER-THAN-EXPECTED SUCCESS OF THE GOVERNMENT'S INGENIOUS CIRCLE-SQUARING RECIPE THERE ARE PROBLEMS WHICH COULD UPSET THINGS SOONER RATHER THAN LATER:-

A. WAGE CLAIMS POSE CONSIDERABLE UNCERTAINTY. THE MINIMUM SALARY HAS JUST BEEN AGREED AS AUSTRALES 1310 FOR OCTOBER.

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EMPLOYERS CLAIM THEY HAVE NOW VIRTUALLY EXHAUSTED THEIR CUSHION. AND POWERFUL UNIONS, EG THE METALWORKERS, CONTINUE TO PRESS FOR LARGE INCREASES.

B. THE PUBLIC SECTOR COMPANIES DO NOT ENJOY THE SAME PRICE CUSHION AS THE PRIVATE COMPANIES. THEIR FINANCIAL PROBLEMS, APART FROM PUTTING PRESSURE ON THE CREDIT MARKET, THREATEN THE GOVERNMENT'S AMBITION TO REDUCE THE FISCAL DEFICIT AND MUST ULTIMATELY BREAK THROUGH IN PRICE INCREASES.

C. A 20 PERCENT INCREASE IN MEAT PRICES THIS WEEK AND POSSIBLE INCREASES IN PRICES OF OTHER FOOD PRODUCTS OUTSIDE THE PRICE GUIDELINES ARE ALREADY POSING A THREAT.

D. THE FINANCES OF THE PROVINCES AND OF THE PROVINCIAL BANKS ARE IN SERIOUS DIFFICULTIES.

E. PUBLIC EXPENDITURE REMAINS WITHOUT SERIOUS CONTROL AND CURRENT TAX RECEIPTS ARE LOWER THAN HOPED FOR.

CONCLUSION

10. THE GOVERNMENT HAVE CLEARLY SWITCHED THEIR PRIORITIES IN FAVOUR OF DOMESTIC TARGETS (PRINCIPALLY INFLATION) OVER THE EXTERNAL SECTOR IN THE RUN-UP TO THE ELECTIONS. SO FAR THIS HAS BEEN SUCCESSFUL BUT THERE IS A CLEAR CONFLICT WITH THE LONGER TERM OBJECTIVE OF HIGHER EXPORT GROWTH. EVEN IN THE SHORT RUN THIS POLICY MAY CAUSE DIFFICULTIES IN DEBT NEGOTIATIONS WITH THE CREDITOR BANKS AND THE IMF.

11. THE GOVERNMENT SEEM CONFIDENT THEY CAN TALK DOWN INFLATION OVER THE NEXT COUPLE OF MONTHS. THE FUNDAMENTAL FLAW OF THE ECONOMIC PLAN REMAINS THEIR INABILITY TO TACKLE THE CENTRAL ISSUE OF PUBLIC EXPENDITURE. WHETHER THE PLAN LASTS TO THE END OF THE YEAR OF EVEN UNTIL NEXT MAY THERE MUST EVENTUALLY COME A MAJOR READJUSTMENT IN PRICES AND IN THE EXCHANGE RATE TO COMPENSATE FOR THE CURRENTLY SUPPRESSED IMBALANCES. NO-ONE OUTSIDE THE GOVERNMENT SERIOUSLY DOUBTS THIS. THE SPECULATION CONSISTS ESSENTIALLY OF HOW LONG THEY CAN SPIN THINGS OUT.

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