

PREM 19/1734

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Confidential Filing

Visit of Mr. Khalil, Prime Minister of Egypt.

AND DR ALI LUTFI

EGYPT

OCTOBER 1979

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10 DOWNING STREET
LONDON SW1A 2AA

THE PRIME MINISTER

16 September 1986

Dear Prime Minister,

I was very pleased to be able to have such a good talk with you last week, and delighted that your prediction of a solution to the Taba arbitration problem and an Egyptian/Israeli summit was subsequently borne out. I send you and President Mubarak warm congratulations on this.

Thank you very much for the very pretty mirror. It was a most kind thought which I very much appreciated.

With best wishes,

Yours sincerely
Margaret Thatcher

His Excellency Dr. Ali Loutfi

ALo



EMBASSY
OF THE ARAB REPUBLIC OF
EGYPT

26, SOUTH STREET, LONDON, W.1.
TELEPHONE: 01-499 2401

The Rt. Hon. Margaret Thatcher, M.P.,
Prime Minister of the United Kingdom

I would like to express my appreciation for the friendly reception you offered me. Our talks reflected a genuine desire to strengthen the friendly relations and fruitful co-operation between our two countries.

On behalf of the Egyptian Government and myself, I would like to extend my deepest thanks to you and to the members of your Cabinet for your very warm hospitality.

A handwritten signature in blue ink, appearing to read 'A. Loutfi', with a long horizontal stroke extending to the right.

Dr. Ali Loutfi
Prime Minister.

London
10th September 1986



SUBJECT cc MASTER

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MJ

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10 DOWNING STREET

LONDON SW1A 2AA

10 September 1986

*From the Private Secretary**Dear Robert,*

PRIME MINISTER'S MEETING WITH THE PRIME MINISTER OF EGYPT
ON 10 SEPTEMBER AT 1200

The Prime Minister received the Egyptian Prime Minister this morning. Dr Lutfi was accompanied by the Egyptian Ambassador and a notetaker. The Chancellor of the Exchequer and HM Ambassador in Cairo were also present.

Egypt and the IMF

The Prime Minister recalled that President Mubarak had briefed her in July on Egypt's economic problems and the state of negotiations with the IMF. She invited Dr Lutfi to bring her up to date.

Dr Lutfi said that it would not be accurate to speak of an economic crisis in Egypt. There was a difficult economic situation. The main reason was the collapse of oil prices. The most pressing problem was a lack of foreign currency. The Egyptian Government had prepared and was beginning to implement a serious economic reform programme. This was designed to increase agricultural and industrial production, to deal with the budget and balance of payments deficits and to curb high population growth. Particular measures were aimed at reducing Government spending, diminishing tax evasion, reducing energy consumption, encouraging exports, and - most important - reducing and eliminating domestic subsidies.

Dr Lutfi continued that an IMF technical mission had been in Cairo and had approved the Egyptian Government's programme, leaving only one major contentious issue to be resolved. This concerned the exchange rate. The IMF wanted the Egyptian Government to unify the Central Bank and free market rates in one year. This was politically impossible for the Egyptian Government since it would mean a 50 per cent increase in prices. They had therefore told the IMF that they would agree to unify the rates within three (or perhaps two and a half) years. The Egyptian Government fully recognised the importance of reaching agreement with the IMF as a precondition for receiving further

international assistance. He hoped that the British Government would encourage the IMF to show understanding for Egypt's political problems.

The Prime Minister said that the United Kingdom recognised that Egypt's situation was critical to the free world. We were very understanding of the Egyptian Government's problems. It was essential to the solution of these problems that there should be agreement with the IMF. The IMF would undoubtedly impose tough conditions but not so tough as to bring about political collapse. The IMF would need to be convinced not only that Egypt's reform programme was on the right lines but that it would be implemented in practice.

The Chancellor of the Exchequer said that it was a tremendous step forward that Egypt was negotiating seriously with the IMF. IMF approval of the Government's reform programme would unlock other doors to help. As regards unification of the exchange rates, no proposal had yet been made to the IMF Executive Board and the United Kingdom had not therefore been required to take a position. But a realistic exchange rate was an essential element in a reform programme and the sooner it was achieved the better. He acknowledged the political difficulties of a rapid move to unify the two rates. But there were political drawbacks also to drawing out the agony over a period of two or three years. Moreover, the IMF would lack confidence that a gradual narrowing of the gap between the two rates over an extended period would be definitely carried through to a conclusion.

Dr Lutfi agreed that it was important to have a realistic exchange rate, but stressed again the difficulties of getting there in one bound. He noted that Mexico had recently signed an agreement with the IMF after a certain amount of political pressure had been exerted on the Fund by the United States and others. Egypt was seeking similar help. The Chancellor pointed out that Mexico had been following tough IMF programmes for the best part of four years. He would be visiting Washington shortly for the IMF/IBRD meeting and would see the IMF Managing Director. He would do what he could to be helpful. But Egypt must be prepared to reach an agreement within the Fund's guidelines. The Prime Minister suggested that it might be easier to solve the exchange rate problem if Egypt were prepared to take a very substantial step towards unifying the rates in the first year.

Taba

Dr Lutfi said that he had spoken to President Mubarak this morning and had learnt that there was a good prospect that the negotiations on Taba would be concluded later today. In that event President Mubarak would meet Mr Peres tomorrow and Egypt's Ambassador to Israel would return to his post shortly thereafter.

Arab/Israel

Dr Lutfi said that Egypt was still trying to bridge the gap between King Hussein and Arafat. Egypt was in a unique position to help advance the Middle East peace process as the only country which enjoyed good relations with all the parties. The Prime Minister said that it was important to inject some momentum into that process, and make the fullest use of Mr. Peres' remaining time in office.

Terrorism

Dr Lutfi referred to President Mubarak's proposal for an international conference on terrorism and urged closer practical co-operation between Britain and Egypt. The Prime Minister stressed the need to bring the full weight of the law to bear on those engaged in terrorism.

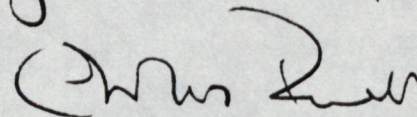
GATT

The Prime Minister referred to the importance of including services fully in the GATT negotiations. Services constituted a steadily increasing proportion of world trade. Dr Lutfi made no comment.

Bilateral Relations

Dr Lutfi characterised relations as good and paid a tribute to the work of Sir Alan Urwick and Mr Sharara. He referred to the very fruitful and productive meetings which he had held with the Lord President, Mr Renton and Mr Raison.

I am copying this letter to the Private Secretaries to the Chancellor of the Exchequer, Secretary of State for Trade and Industry, the Defence Secretary and Sir Robert Armstrong.

Yours sincerely


Charles Powell

Robert Culshaw Esq
Foreign and Commonwealth Office.



With the compliments of

**NEAR EAST AND NORTH AFRICA
DEPARTMENT**

**FOREIGN AND COMMONWEALTH OFFICE
LONDON, SW1A 2AH**

Immediate
cc Mr Powell, m 10
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SAVING BEIRUT, TEHRAN, BAGHDAD

MR RENTON'S CALL ON EGYPTIAN PRIME MINISTER

1. MR RENTON PAID A HALF HOUR CALL THIS AFTERNOON ON THE EGYPTIAN PRIME MINISTER, WHO SAID HE LOOKED FORWARD TO SEEING HIM IN CAIRO LATER THIS MONTH. ON SUBSTANCE, A SUPERFICIAL RUN-THROUGH OF CURRENT INTERNATIONAL PROBLEMS, TOUCHING ONLY BRIEFLY ON EGYPT'S ECONOMIC DIFFICULTIES.

PEACE PROCESS

2. LUTFI DENIED TODAY'S AGENCY REPORTS THAT THE LATEST ROUND OF NEGOTIATIONS ON TABA HAD ENDED IN FAILURE. THERE WOULD BE A FURTHER SESSION THIS EVENING, WHICH HE EXPECTED TO LEAD TO AGREEMENT IN THE NEXT DAY OR TWO ON THE NAMES OF ARBITRATORS AND BORDER MARKERS. THE WAY WOULD THEN BE CLEAR FOR A PERES/MUBARAK SUMMIT, THE RETURN OF AMBASSADORS, AND, AT A LATER STAGE, AN INTERNATIONAL CONFERENCE. MR RENTON UNDERLINED THE IMPORTANCE OF MAKING PROGRESS BEFORE ROTATION IN ISRAEL, AND REMINDED LUTFI OF THE NEED FOR THE TERMS OF REFERENCE OF ANY

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INTERNATIONAL CONFERENCE TO BE CLEARLY DRAWN. BIG CONFERENCES WERE NOT NECESSARILY THE ANSWER TO BIG PROBLEMS.

IRAN/IRAQ

3. LUTFI SAID THAT THE GULF CONFLICT THREATENED THE STABILITY OF THE ENTIRE REGION. THE POSSIBILITY OF AN IRANIAN VICTORY WAS WORRYING FOR THE ARAB WORLD, BOTH MILITARILY AND ON ACCOUNT OF THE DAMAGE WHICH COULD BE DONE IF KHOMEINI'S IDEAS WERE TO GAIN WIDER SUPPORT. IRAN HAD CONSISTENTLY REJECTED IRAQI PEACE OVERTURES. THE INTERNATIONAL COMMUNITY, PARTICULARLY THE GREAT POWERS, SHOULD HELP FIND A SOLUTION. MR RENTON SYMPATHISED. THE PROBLEM WAS HOW TO HELP THE UN SECRETARY GENERAL'S EFFORTS TO BROKER A SOLUTION.

LIBYA

4. EGYPT HAD NO QUARREL WITH THE LIBYAN PEOPLE, LUTFI SAID, BUT FOUND IT IMPOSSIBLE TO DO BUSINESS WITH QADHAFI, WHO WAS MAD. MR RENTON ASKED WHETHER THE EGYPTIAN GOVERNMENT HAD AN ALTERNATIVE LEADER IN MIND. THE PRIME MINISTER SAID HE HAD NOT, BUT BELIEVED THAT IT WOULD BE POSSIBLE, IN COOPERATION WITH THE US, TO SELECT AND PREPARE A CANDIDATE. CONCERTED ACTION SHOULD NOT, HOWEVER, INCLUDE FURTHER MILITARY STRIKES AGAINST LIBYA, WHICH PLACED MODERATE ARAB STATES IN A DIFFICULT POSITION. MR RENTON COMMENTED THAT THE US MILITARY ACTION IN APRIL HAD WEAKENED QADHAFI'S POSITION AND CONTRIBUTED TO A LULL IN TERRORIST ACTIVITY.

SUDAN

5. LUTFI DREW ATTENTION TO THE ENORMITY OF SUDAN'S DIFFICULTIES, NOTABLY IN THE SOUTH. IT WAS IMPORTANT NOT TO DESERT SADIQ EL MAHDI AND FORCE HIM TO TURN TO QADHAFI.

LEBANON

6. HERE TOO, LUTFI ARGUED, THE STABILITY OF THE REGION WAS THREATENED. FULL ISRAELI WITHDRAWAL WOULD HELP. SO TOO WOULD A BRITISH TROOP CONTRIBUTION TO UNIFIL. MR RENTON DREW ATTENTION TO THE CURRENT LEVEL OF OUR SUPPORT FOR UNIFIL. INTERNALLY, THE BEST HOPE FOR PROGRESS LAY IN REVIVING THE SYRIAN-SPONSORED TRIPARTITE AGREEMENT.

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EGYPTIAN ECONOMY

7. LUTFI SAID HE PLANNED TO DISCUSS EGYPTIAN ECONOMIC NEEDS IN DETAIL WITH MR RAISON AND THE PRIME MINISTER. MR RENTON STRESSED THE IMPORTANCE OF REACHING AGREEMENT WITH THE IMF. BRITAIN WAS READY TO SUPPORT EGYPT IN MAKING THE NECESSARY ECONOMIC ADJUSTMENTS. LUTFI SAID THAT EGYPT WAS READY TO SIGN, IF ONLY THE IMF WOULD ALLOW A TWO OR THREE YEAR ADJUSTMENT PERIOD RATHER THAN THE ONE YEAR CURRENTLY PROPOSED. THE SPECIAL TERMS RECENTLY AGREED WITH MEXICO PROVIDED A POSSIBLE MODEL.

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PS
SIR D MIERS

MR E FERGUSSON

PS/PUS

PS/MR RENTON

PS/MR RAISON



OVERSEAS DEVELOPMENT ADMINISTRATION
ELAND HOUSE
STAG PLACE LONDON SW1E 5DH
Telephone 01-213 5409

②

CC PC
BUP

Time Raison
relevant to your
meeting tomorrow.
CDP 9/9

9 September 1986

From the Minister

Charles Powell Esq
10 Downing Street
Whitehall
LONDON SW1

Dear Charles

CALL BY MR RAISON ON PRIME MINISTER OF EGYPT, DR LUTFI

Dr Lutfi, who is seeing the Prime Minister tomorrow, had a meeting with Mr Raison this afternoon.

Dr Lutfi's main concern was that Britain should support Egypt in its negotiations with the IMF. He said that the Leader of the IMF Mission now in Cairo is fully satisfied with the economic actions taken by the Government but the difference in Egypt's two exchange rates remained the key problem. The IMF wanted them to be unified in a year's time. Dr Lutfi said this was impossible; 2-3 years were needed or there would be a 30 per cent increase in prices which would be politically unacceptable. He hoped that a little political pressure could be applied to the IMF to help secure an agreement with Egypt. He believed that an IMF agreement with Mexico had been secured in this way. He hoped Britain would be able to help. Mr Raison said he well understood the political difficulties of meeting the requirements of an IMF agreement. But he stressed the importance of an agreement being reached and he hoped that the Egyptian Government would feel able to come to an accommodation with the Fund. Since the negotiations involved bilateral discussions between Egypt and the Fund he did not see that Britain had a particular role to play at this stage. But Mr Raison undertook to report the strength of Dr Lutfi's feeling to his Treasury colleagues.

Dr Lutfi asked for more aid funds to be made available for potential professors to come to Britain to take their PhDs. He argued that training of this sort made a particularly valuable contribution to cultural relations and better understanding between the two countries. Mr Raison agreed about the value of this training. He pointed out that the FCO had recently increased the allocation for training awards but he said that the Prime Minister's request would certainly be given further consideration.

The Egyptian Ambassador raised the question of the second phase of the Cairo Wastewater project. He said - and the Prime Minister confirmed - that the Egyptians were ready to go ahead with the second phase. Mr Raison took note but commented that it was unlikely that Britain would be able to make available funds on the scale that it had provided to Phase I. A British contribution from the Aid and Trade Provision, linked with ECGD credit, would be a possibility to be considered. The Prime Minister took note of this.

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I am copying this letter to Robert Culshaw (Foreign Secretary's Office), Alex Allan (Chancellor of the Exchequer's Office) and Peter Westmacott (Mr Renton's Office).

Yours sincerely
M J Dinham

(M J Dinham)
Private Secretary

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PRIME MINISTER

MEETING WITH THE EGYPTIAN PRIME MINISTER

You are seeing Dr. Lutfi for 45 minutes before lunch tomorrow. He will be accompanied by the Egyptian Ambassador and an adviser. The Chancellor of the Exchequer and our Ambassador (Sir Alan Urwick) will also attend.

You might begin by enquiring after his back. He was in hospital in London for treatment in January/February, but left before you were able to see him. He is having it checked up this time.

The main purpose of his call is to brief you on the Egyptian economy and negotiations with the IMF. You will recall that you discussed this with President Mubarak in July (a note on the meeting is at the back of the folder). He complained that the conditions which the IMF were trying to set on cuts in subsidies, increases in interest rates and unifying exchange rates were too tough and would cause instability in Egypt. He also alleged that the UK Director was discouraging the IMF from showing flexibility. You can deal firmly with this latter point: like other donors, we are waiting for proposals from the IMF before taking up a firm position. But you will want to leave him in no doubt that agreement with the IMF is an essential step if Egypt is to receive Paris Club rescheduling and additional aid. As you told President Mubarak, it is important to set tough targets.

You might also take the opportunity to mention the forthcoming GATT negotiations. The Egyptians have thrown in their lot with India and Brazil in opposing the inclusion of services in the new GATT round. This is ridiculous, because services now amount to 20 per cent of world trade. A GATT round without services would drastically diminish the attraction for us (and would affect our ability to earn the income which enables us to give aid). The Americans might well pull out altogether.

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As you will recall, Lutfi is not well briefed on Arab/Israel
and Iran/Iraq, but you may like to refer to both issues
briefly, at the end. You are seeing King Hussein on
20 September.

CDP

C.D. POWELL

9 September 1986

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Foreign and Commonwealth Office

London SW1A 2AH

9 September 1986

EDP
9/9.

Dear Charles

Visit of Egyptian Prime Minister

/ Following Caroline Ryder's letter of 20 August, I enclose a brief, agreed with DTI and HM Treasury, for the Prime Minister when she sees Dr Lutfi at 12 noon on 10 September. We understand that Dr Lutfi will be accompanied by the Egyptian Ambassador and Mr Farghal, a Counsellor to Dr Lutfi. On our side the Chancellor and Sir Alan Urwick will be present.

I am copying this letter and its enclosure to Tony Kuczys (HM Treasury), Tim Walker (DTI) and Michael Stark (Cabinet Office).

Yours ever

(R N Culshaw)
Private Secretary

C D Powell Esq
PS/10 Downing Street

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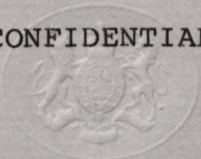
MEETING BETWEEN THE PRIME MINISTER AND THE EGYPTIAN PRIME MINISTER,
10 SEPTEMBER 1986

OUR OBJECTIVES

- To ascertain Egyptian government's intentions regarding the economy; to urge Egypt to come to terms with IMF, assuring him of UK's continued support for economic adjustment, but without raising hopes of new capital aid.
- To get Egypt to play a constructive role at the GATT Ministerial.
- To underline HMG's concern to help promote constructive initiatives on Arab/Israel and seek Egyptian views, particularly on Taba and the prospects for success of current US diplomacy.
- To express concern at course of the Iran/Iraq conflict; to avoid raising hopes of active EC mediation during UK Presidency; to reiterate our strict policy on arms supplies to each side.

ARGUMENTS TO USE

- Exactly one year since we met in Cairo. Delighted to meet again, especially in view of EC Presidency. Valuable recent meetings with President Mubarak, Field Marshal Abu Ghazala and Dr Al-Baz. Mr Renton to visit Egypt this month.
- Welcome your commitment to economic reform and measures already taken. Prospects for a strategy agreed with IMF? Convinced this is essential first step towards recovery. Would increase prospects for longer-term prosperity, give vital boost to international confidence and unlock door to new resources.
- Recognise importance to West of Egypt's stability and prosperity. Assure you of UK's continued support (in EC, IMF and bilaterally).
- GATT Ministerial next week in Uruguay crucial for future of world trading system. Hope Egypt will use her influence to secure launch



of new GATT round.

- Deep concern at lack of progress on Arab/Israel before Israeli rotation. No sign of PLO adopting more constructive approach. Note moves towards agreement over Taba. What are the prospects? Is a Peres/Mubarak summit now on the cards? Know that Americans have been trying to promote Egypt/Jordan joint approach: welcome briefing and your perspective of progress made.

- Actively looking with European partners for ways to help the parties to move forward. Will continue this effort. In close touch with US also. Working bilaterally and through EC to improve conditions in Occupied Territories, as move towards, not substitute for, Israeli withdrawal.

- Increased activity and tension in Iran/Iraq conflict worrying. UN Secretary General reiterated on 13 August his readiness to work with the two governments. His efforts represent best chance of progress when chance for mediation opens up.

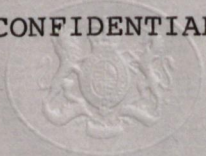
TACTICAL ARGUMENTS

- West cannot rescue Egypt from economic crisis. But can continue to provide support for action by Egyptian government.

- Fine balance between need for economic reform and threat to stability. But need to set tough targets. Long-term benefits of bold measures will outweigh short-term political risks.

- See no realistic alternative to Paris Club rescheduling. [If necessary] To ensure equality of treatment for creditors, not our policy to agree bilateral rescheduling outside Paris Club framework. Orderly rescheduling in best interests of all.

- Will aim to maintain an effective bilateral aid programme into the future, especially in field of technical cooperation. Will do best to promote bilateral trade (Trade balance has been in Egypt's favour this year). But concerned that progress on Cairo Wastewater project (which I inaugurated in September) threatened by failure to budget



for local cost contributions: hope for detailed progress at Joint Commission this month.

- Our bilateral food aid limited. Priority used for emergencies. 1986 programme already fully committed.
- Will remain major contributor to multilateral aid, especially through EC. [If discussed in detail] Recognise Egypt's continuing need for EC food aid to support progress towards self-reliance: but essential Egyptian Government does more to encourage local food production. UK supported early discussion of proposal to increase allocation agreed recently to 170,000 tons of food aid cereals.
- New Mediterranean Financial Protocols still under discussion within Community. Budgetary constraints are severe but want to see benefits of new protocols directed to poorer countries, including Egypt. Hard to see STABEX-type arrangements applying to Egypt.
- Policy on ECGD cover similar to other Western insurers: will continue to hold exposure within prudent limits. Hope defence tranche will be used.
- We sell more defence equipment to Iraq than to Iran.

HIS OBJECTIVES

- To explain Egypt's latest attitude towards negotiations with the IMF on an economic adjustment package; to seek UK help in ensuring IMF pay due regard to Egypt's difficulties and risk of provoking political disorder.
- Perhaps to express reservations about inclusion of trade in services in new GATT round.
- Perhaps to reiterate long-standing Egyptian call for a European initiative on Arab/Israel
- To express concern at cause of Iran/Iraq conflict and (perhaps) to urge EC involvement in mediation during UK Presidency.



OUR RESPONSE

- Sympathy with Egypt's economic difficulties. But IMF package, essential first step to allow Egypt towards economic recovery and obtaining necessary additional foreign assistance. Cannot intervene in detailed negotiations between Fund and authorities.

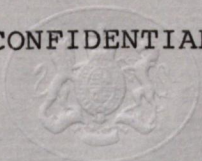
- Services must clearly be an integral part of new GATT round. Over 20% of world trade.

- Determined to work to help the parties to the Arab/Israel dispute to solve their differences. But role of outsiders limited. What positive trends in relationship between the parties do you identify which we could seek to strengthen?

- Iran/Iraq conflict is costly to both sides and to stability of whole region. All mediation efforts except UN Secretary General's have failed. Only he has confidence of both sides; 8 point proposals still on the table. EC should not muddy the water.

PRESS LINE

1. Dr Lutfi visiting London privately (5-11 September). In his call on the Prime Minister on 10 September he gave her an account of the latest state of negotiations with the IMF over a package of economic adjustment measures for Egypt. The Prime Minister assured him of Britain's continued support, both through Britain's bilateral trade and aid relations with Egypt and in the context of Egypt's relations with the European Community and international financial institutions. The Arab/Israel dispute and the Iran/Iraq war were also discussed: the Prime Minister reaffirmed the willingness of Britain and the Twelve to support realistic initiatives to promote peaceful solutions.



BACKGROUND

1. Dr Lutfi is coming to London from France, partly to consult his doctor about his back (for which he received hospital treatment here in January/February). He has asked to see the Prime Minister to follow up President Mubarak's tour of European countries in July to explain his government's intentions regarding the economy. A record of the Prime Minister's meeting with Mubarak is attached, together with a personality note on Dr Lutfi and a report from Cairo on the latest IMF mission to Cairo last month.

2. Though not the poorest of countries, Egypt suffers from longstanding economic mismanagement. With a \$40 billion external debt, a \$3.5 billion external current account deficit, 3% annual population growth and recent reductions in Egypt's foreign exchange earnings from oil, remittances from overseas workers, Suez Canal dues and tourism, the Egyptian government faces the dilemma of whether to opt now for IMF adjustment measures (including cuts in consumer subsidies, exchange rate unification/devaluation) which might endanger internal stability, or to go on deferring difficult and unpopular decisions and thus allow situation to exacerbate. Dr Lutfi appears to be cool towards opting for the IMF route.

3. The IMF's seal of good housekeeping, however, is an essential precondition for Paris Club rescheduling and significant new aid inputs. US aid (\$1 billion civil and \$1.3 billion military in FY87) is static, although some relief on military debt repayments may be possible. Prospects for new European aid are also slim. Since Mubarak's tour, only Italy has argued that the West should influence the IMF to adopt a softer line towards Egypt. We and other donors await Fund proposals before taking a firm position. Nevertheless, the Prime Minister will want to dispel firmly any misconception on Lutfi's part that the UK is less disposed than its partners to see Egypt benefit from assistance through the IMF or EC.

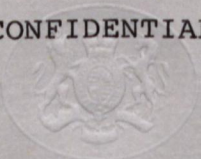
4. Because of competing claims elsewhere and the high level of US aid, UK bilateral capital aid to Egypt is set to fall over the next few years, though substantial technical cooperation will remain. The Prime Minister might raise with Lutfi the Egyptian failure to

budget adequately local cost contributions towards Cairo Waste Water, our biggest development project in Egypt. ECGD cover is very tight, despite eleventh-hour agreement on cover for defence sales reached during Field Marshal Abu Ghazala's visit in June. ECGD's current and contingent exposure amounts to \$1.7 billion, equal to that of the FRG but less than that of France (\$6.1 billion).

5. New GATT round. Egypt has hitherto tagged along with the hardliners in Geneva (Brazil and India), in opposing a new round including trade in services. But there are signs that they are prepared to take a more flexible line at the Uruguay Ministerial, in the interests of achieving consensus.

6. Food Aid. Egypt's grain import requirements this year are likely to be some 7 million tonnes. Most of this will be provided by the US, either as food aid or commercially. The EC has agreed to provide 170,000 tonnes of grain as food aid. The Egyptians are looking to other donors to finance food aid shipments in order to minimise the amount they have to purchase commercially. The UK bilateral programme of some 110,000 tonnes of cereals is fully committed for 1986. We give priority to emergency needs and this year will be arranging shipments to Ethiopia and Mozambique. The balance will go to the World Food Aid programme. For some years the European Community has provided Egypt with substantial quantities of food aid. The latest EC food aid offer is linked to pressure from the Commission on the Egyptians to make major policy changes for encouraging local production of food.

7. Arab/Israel. Egyptian policy has been to promote the re-establishment of cooperation between Jordan and the PLO (broken off by King Hussein on 19 February). This has looked increasingly unrealistic. They have also urged Arafat to accept SCR 242 and called for closer European involvement in the peace process, but it is not at all clear what this could realistically be expected to achieve. Agreement has been reached with Israel on the terms of arbitration on Taba, but choice of arbitrators is outstanding and maps must be selected as a basis for their work. It appears that these remain serious obstacles to signature of the agreement, which could open the way for a Peres/Mubarak summit. Mubarak is under



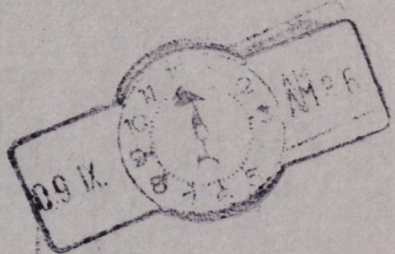
some pressure to agree to a summit to ease congressional approval of debt rescheduling. The US have been trying to promote a joint Jordan/Egypt/Israel statement on the principles for moving to a negotiated Arab/Israel settlement, but Hussein is understandably cautious.

8. The European Commission has announced proposals for improved aid to the Occupied Territories and access for produce. It is strongly in our political interests to urge the Commission to press ahead with them as a practical demonstration of our concern for Palestinians at a time of virtual stalemate in the peace process. Urgent consultations of the proposals is underway in Whitehall.

9. Iran/Iraq. The last month has seen increased attacks by both sides on targets in civilian areas and a further escalation of attacks on shipping in the Gulf. A major Iranian offensive is expected this autumn. Both sides are suffering economically because of the oil price decline. Egypt has maintained her firm support for Iraq.

NEAR EAST AND NORTH AFRICA DEPARTMENT

September 1986



cc Subject

CONFIDENTIAL

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Subject Filed on
EGYPT: Visits by
President Mubarak. Pt 2



cc PC

10 DOWNING STREET

LONDON SW1A 2AA

From the Private Secretary

17 July 1986

Dear Robert,

PRIME MINISTER'S MEETING WITH THE EGYPTIAN PRESIDENT

The Prime Minister saw President Mubarak for an hour and a quarter this evening. Only note-takers were present.

The Prime Minister recalled her meetings with Field Marshal Abu Ghazala and Mr. Al-Baz, both of which she had found useful and constructive.

Egyptian Economy

The Prime Minister said that she understood that the Egyptian Government had approached the IMF for help. She had considerable sympathy with Egypt's difficulties. A number of misfortunes had struck simultaneously: the decline in oil prices, a falling off of tourism and a drop in revenue from the Suez Canal.

President Mubarak confirmed that the Egyptian economy faced serious problems. Moreover, Egypt's loans were not well phased and repayments would be at a peak over the next three years. Egypt had therefore been in discussion with the IMF and had reached satisfactory conclusions on most points. However, there were two outstanding difficulties. The first was the IMF's demand that interest rates should be increased from 11 per cent to 20 per cent. This would stop investment in industry and would drive up prices. Secondly, the IMF wanted Egypt's various exchange rates to be unified in the course of a single year. This too would lead to a very steep rise in prices. Were the Egyptian Government to accept the IMF's prescription on these two points, there would be a grave risk of instability. They were prepared to move as fast as politically feasible to implement the IMF's recommendations. But to accept them as they stood would lead to a repeat of the 1977 riots. Egypt would be thrown into turmoil and the whole area would be affected. Economic reform had to be tackled sensitively. Timing was very important. For instance he planned to increase electricity prices next April when the university students would be busy with exams and the chances of disorder thus diminished. He was therefore seeking the help of Egypt's friends to

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persuade the IMF to negotiate more reasonably on these two points. He understood that the British and German Executive Directors were offering the strongest resistance to flexibility on the IMF's part. He well understood that the IMF's recommendations were in Egypt's interests. He wanted to implement them as rapidly as possible. But the people had to eat, and he simply could not move as fast as the IMF wanted.

The Prime Minister said that agreement with the IMF was an essential step in restoring Egypt to economic health. Once such agreement was reached, it would unlock the door to further assistance. She could understand the political constraints facing President Mubarak. But the IMF would need to be convinced that he really had gone to the limits of what was feasible. This was something which had to be negotiated between Egypt and the IMF. It was important to establish tough targets. We recognised the scale of the difficulties which Egypt faced and acknowledged Egypt's strategic importance. She would look again at the instructions which had been given to the UK Executive Director but could not ask him to do anything basically unreasonable.

Taba

The Prime Minister asked about progress in the negotiations over Taba. President Mubarak said that the real problem lay with political manoeuvring in Israel. Likud wanted to create political problems for Mr. Peres and were seeking wording which would make it possible to reopen the whole Israel/Egypt border. But he was optimistic that agreement would be reached.

Arab/Israel

The Prime Minister gave President Mubarak a brief account of her visit to Israel and subsequent discussions with King Hussein. She had reached the conclusion that Mr. Peres' proposals for dealing with Gaza first were unlikely to lead anywhere. King Hussein was clearly not prepared to accept them. She was worried about the current hiatus in the peace process. But there was no prospect of any fresh initiative from the United States until after the Congressional elections.

President Mubarak said that he had undertaken not to enter discussions on Gaza except in agreement with King Hussein. Meanwhile he was pressing Arafat to take the step of accepting UN Security Council Resolutions 242 and 338. People in Egypt were fed up with the PLO and he had made clear to Arafat that the organisation was losing support. The Prime Minister said that the PLO must be brought to realise that unless they accepted 242 and 338 they would find themselves excluded from any negotiations.

President Mubarak railed against President Asad who had recently again tried to persuade Egypt to drop the Camp David Agreements and the Peace Treaty with Israel. He had

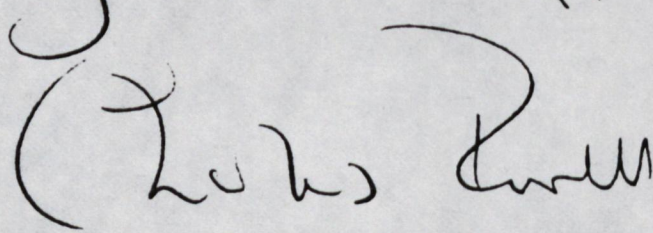
told Asad that Egypt respected its commitments and could not, like Lebanon, be bullied out of its agreements. President Asad and indeed the whole Syrian leadership were sly and corrupt.

Iran/Iraq

The Prime Minister said that she was concerned by indications that the Iranians might be gaining an upper hand in the conflict with Iraq. President Mubarak doubted whether either side was winning. Iraq's military performance was far from inspiring. They had totally failed to spot Iranian preparations for the invasion of Fao, even though these involved assembling some 5,000-6,000 small boats. He did not foresee any early end to the war. It was essential to maintaining Khomeini in power, although he believed that the regime would eventually be overthrown by the Armed Forces.

The Prime Minister told President Mubarak as he left that she would "see what she could do" about the IMF negotiations. She would therefore be grateful if the Chancellor could inform her in more detail of the precise position we are taking on the remaining points of difficulty. She thinks that the political constraints on President Mubarak must be given some weight although they cannot of course in themselves determine our position.

I am copying this letter to Rachel Lomax (HM Treasury), John Mogg (Department of Trade and Industry) and Michael Stark (Cabinet Office).

Yours sincerely,


Charles Powell

R. N. Culshaw, Esq.,
Foreign and Commonwealth Office.

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DR.

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FM CAIRO

TO DESKBY 290900Z FCO

TELNO 531

OF 281305Z AUGUST 86

INFO ROUTINE DTI, ODA, ECGD, BANK OF ENGLAND, UKDEL IMF/IBRD

INFO ROUTINE UKREP BRUSSELS, WASHINGTON

INFO SAVING HMC G ALEXANDRIA - ACTIONED

MY TELNO 527: EGYPTIAN ECONOMY;
NEGOTIATIONS WITH THE IMF

SUMMARY

1. EC REPRESENTATIVES BRIEFED ON EGYPT'S ECONOMIC STABILISATION AND STRUCTURAL REFORM PROGRAMME. EGYPTIAN HOPE FOR EC SUPPORT IN NEGOTIATIONS WITH IMF AND WORLD BANK REITERATED.

DETAIL

2. EC REPRESENTATIVES WERE SUMMONED TO THE MFA ON 28 AUGUST TO BE BRIEFED ON THE GOVERNMENT'S 'ECONOMIC STABILISATION AND STRUCTURAL REFORM PROGRAMME'. WE WERE TOLD THAT THE BRIEFING WAS TO BE GIVEN BY THE MINISTERS OF FOREIGN AFFAIRS, FINANCE AND CABINET AFFAIRS. IN THE EVENT, THE THREE MINISTERS HAD AT THE LAST MOMENT TO GO TO ALEXANDRIA TO SEE THE PRESIDENT AND THE BRIEFING WAS THEREFORE GIVEN BY ASSISTANT FOREIGN MINISTER MAKHLOUF.

3. READING FROM A PREPARED TEXT (COPY TO NENAD BY TODAY'S BAG), MAKHLOUF RECOUNTED THE ORIGINS OF EGYPT'S ECONOMIC PROBLEMS IN FAMILIAR TERMS (FALL IN OIL PRICES, MIDDLE EAST TERRORISM AND DROP IN REMITTANCES) AND THE MEASURES TAKEN SO FAR TO DEAL WITH THEM. HE THEN WENT ON TO DESCRIBE IN VERY GENERAL TERMS THE FURTHER MEASURES TO BE TAKEN. THE AIM WOULD BE THE COMPLETE LIBERALISATION OF THE ECONOMY AND THE DIVERSIFICATION OF ITS EXPORT BASE WITHIN 6-10 YEARS. OVER THE NEXT DECADE, AGRICULTURAL AND INDUSTRIAL PRODUCER PRICES WOULD BE FULLY LIBERALISED AND ALL PRODUCTION SUBSIDIES ELIMINATED. BEFORE THE END OF THE CURRENT FINANCIAL YEAR, SUBSIDIES WOULD BE MOVED TO THE DISTRIBUTION LEVEL, TO ELIMINATE THEIR DISTORTIONARY IMPACT ON DOMESTIC PRODUCTION. ENERGY PRICES WERE EXPECTED TO REACH INTERNATIONAL LEVELS WITHIN 7 YEARS AND IT WAS AIMED TO HALVE THE RATE OF INCREASE OF DOMESTIC ENERGY CONSUMPTION OVER THE SAME PERIOD. A NUMBER OF PUBLIC SECTOR ACTIVITIES WERE TO BE PRIVATISED, TAX REVENUES INCREASED AND PUBLIC EXPENDITURE CUT IN ORDER TO ACHIEVE A REDUCTION OF THE PUBLIC SECTOR DEFICIT BY 2.5% OF GDP PA FOR THE NEXT 4 YEARS. MEASURES WERE ALSO PLANNED TO REDUCE THE EXTERNAL FINANCING GAP AND THE INTEREST RATE STRUCTURE WAS TO BE REFORMED. SUBSTANTIAL PROGRESS WAS PLANNED IN DEALING WITH POPULATION GROWTH AND PUBLIC EMPLOYMENT, WHICH REMAINED EGYPT'S 2 BASIC PROBLEMS.

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4. MAKHLOUF SAID THAT THE EGYPTIAN GOVERNMENT BELIEVED THAT THEY HAD TAKEN A NUMBER OF COURAGEOUS STEPS, WHICH WENT A LONG WAY TO ACHIEVING THE NECESSARY ECONOMIC REFORMS WHILE SAFEGUARDING THE STABILITY OF EGYPTIAN SOCIETY. EGYPT RELIED ON THE SUPPORT OF EC COUNTRIES AND GREATLY HOPED THAT WE WOULD ASSIST THEM IN THEIR NEGOTIATIONS WITH THE IMF AND THE WORLD BANK. SPEAKING ON BEHALF OF MY COLLEAGUES, I ASSURED MAHLOUF THAT WE WOULD REPORT FULLY WHAT HE HAD SAID: I WAS CONFIDENT THAT EGYPT'S DIFFICULTIES WOULD BE LOOKED AT SYMPATHETICALLY BY ALL OUR GOVERNMENTS.

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B. R.

CDP - free

Range of MEX's options
also confirmed.
CR
27/8

PRIME MINISTER

You are seeing the Egyptian Prime Minister for an hour on Wednesday 10 September. The Chancellor will also be arranging to see him, and the Treasury have suggested that it might be appropriate for you and the Chancellor to meet Dr. Lutfi together.

Would you like the Chancellor to join your meeting (or at least a portion of it); or prefer to see the Egyptian Prime Minister on your own?

MEA

↓
Yes
not

Mark Addison

22 August 1986

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EA

cc PC.

10 DOWNING STREET

LONDON SW1A 2AA

From the Private Secretary

20 August 1986

VISIT OF EGYPTIAN PRIME MINISTER

Thank you for your letter of 15 August. The Prime Minister is content to see Dr. Ali Lutfi at 1200 on Wednesday 10 September for an hour.

I would be grateful if you could provide briefing for this meeting by Tuesday 9 September.

I am copying this letter to Timothy Walker (Department of Trade and Industry), Tony Kuczys (H.M. Treasury) and Michael Stark (Cabinet Office).

(Mrs Caroline Ryder)

Colin Budd, Esq.,
Foreign and Commonwealth Office.

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CC/C



Foreign and Commonwealth Office

Prime Minister:

London SW1A 2AH

You are away for 6-8
 September. 9 September
 and possibly 10 September will be very busy with other matters. 15 August 1986
 But you ought to see Dr Lutfi.
 Agree to a slot as late as possible
 on 10 September when other business
 should be finished?
 Lea Tim
 JK 18/8
 Yes

VISIT OF EGYPTIAN PRIME MINISTER TO LONDON

The Egyptian Embassy have asked on instructions whether the Egyptian Prime Minister, Dr Ali Lutfi, may call on the Prime Minister during his private visit to London from 6 - 10 September for medical consultations. (He had hospital treatment here earlier this year for back trouble.) The Embassy have told us that Dr Lutfi hopes to follow up President Mubarak's talk with the Prime Minister last month (Charles Powell's letter to Robert Culshaw of 17 July) and that the main subject of discussion would again be the Egyptian economy. They emphasised the importance Egypt attaches to maintaining high-level contact with us on this subject, particularly in view of our current Presidency of the EC.

Lady Young believes that a talk with Dr Lutfi will be useful, and hopes that the Prime Minister can receive him. It will offer an excellent opportunity to obtain an authoritative Egyptian reaction to their talks with the IMF team which is to visit Cairo later this month, to reassure the Egyptians of our continued understanding and support, and to reiterate the advantages to Egypt of reaching agreement with the IMF on the basis of a rigorous and realistic economic programme. It is also desirable, given our inability to increase our bilateral aid to Egypt, that we avoid giving the Egyptians any grounds to complain again that we are being less helpful than our EC partners. Dr Lutfi is to visit Paris, where he is likely to be received at high level, before he comes to London.

The Prime Minister will recall that she met Dr Lutfi in Cairo in September 1985, shortly after his appointment as Prime Minister. Since then she has received President Mubarak;

/his

T Flesher Esq
 10 Downing Street

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his political adviser, Dr Osama Al Baz; and the Deputy Prime Minister and Minister of Defence, Field Marshal Abu Ghazala. Dr Lutfi is senior to both Al Baz and Abu Ghazala.

Dr Lutfi has been unwell and has had little success so far in tackling Egypt's economic problems or even in mobilising support in his cabinet for a coherent approach to them. But he was Mubarak's personal choice as Prime Minister and Mubarak is unlikely to want to replace him while he is still seeking to reach agreement with the IMF.

We are recommending that Sir Geoffrey Howe should also see Dr Lutfi. Mr Renton, who saw Dr Lutfi in February and who plans to visit Egypt in September, also hopes to call on him.

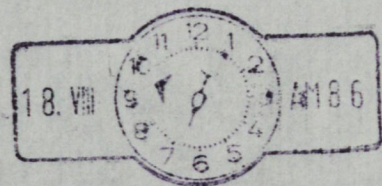
I am copying this letter to John Mogg (DTI), Michael Stark (Cabinet Office) and Tony Kuczys (HM Treasury).

Yours sincerely,

David Reddaway

David Reddaway
Private Secretary to
Baroness Young

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Egypt
JPA
JPA



10 DOWNING STREET

From the Private Secretary

26 October 1979

Dear George,

Visit by the Prime Minister of Egypt

As you know the Egyptian Prime Minister, Mr. Khalil, called on the Prime Minister yesterday evening. Enclosed is a report of their talk.

You will wish to be aware that in discussion after Mr. Khalil's departure, the Prime Minister said that we should do what we could to assist Mr. Khalil in bringing to fruition the plan described in the enclosed record.

Yours ever

Michael Alexander

SB

G.G.H. Walden, Esq.,
Foreign and Commonwealth Office.

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RECORD OF A CONVERSATION BETWEEN THE PRIME MINISTER AND THE
PRIME MINISTER OF EGYPT, MR. MUSTAFA KHALIL, AT 10 DOWNING STREET
ON 25 OCTOBER 1979 AT 1730

Present

Prime Minister	Mr. M. Khalil
Mr. M.S. Weir	H.E. Mr. M.S. Anwar
Mr. M.O'D.B. Alexander	

* * * * *

Autonomy Talks

The Prime Minister asked about progress in the autonomy talks. Mr. Khalil said that the talks were going very slowly. The view-points of the Israeli and Egyptian Governments were quite different, e.g. over the question of the responsibilities of a self-governing authority. In the Egyptians' view all civilian responsibilities should be transferred to the new authority. Only military responsibility should be retained by the Israeli Government. The Israelis on the other hand wanted the military authorities to retain extensive powers. Mr. Khalil quoted as an example the fact that the Israelis wanted to retain control of education in order to ensure that schoolbooks did not contain criticism of them. The Egyptians wanted the self-governing authority, which would be elected, to have legislative as well as judicial and administrative powers. The Israelis wished to limit the electoral process as far as possible: they had in mind a ^{directly elected} eleven-man council. The Egyptians wanted a contested election in constituencies. The Israelis claimed that this would mean party politics and would bring the PLO to power. When the Egyptians had attempted to resolve this last point by making it a condition for participation by any party in the election that that party should have to accept the existence of Israel, the Israelis had shelved the question. Indeed one of the problems of dealing with the Israelis was that their negotiators had no powers of decision; everything was referred back to Mr. Begin.

The Prime Minister asked whether Mr. Khalil had any specific objective for the following day. Mr. Khalil said that whole negotiations could be finished in six months ~~if~~ the principles

/could

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could be agreed. But since at present everything was disagreed, little progress could be made. Mr. Strauss was trying very hard to find a way through. Mr. Khalil said that he agreed with Mr. Strauss that this was not a time to try to put too much pressure on the Israelis. They would resist US pressure and in any case Mr. Carter was unlikely to be prepared to exert it in a pre-election period. In short, the talks on the following day were unlikely to get very far. The Israelis were said to have brought some new ideas with them but it was not easy to see what these might be.

Mr. Weir asked whether Mr. Khalil had a timetable in mind. Mr. Khalil said that he planned to escalate the pressure on Israel when Egyptian territory up to the El Arish/Ras Mohammed line had been returned, i.e. after January. It was an essential part of Egyptian thinking on this that the Israeli Defence Minister, Mr. Weizman, should not resign until the El Arish/Ras Mohammed line had been secured. Mr. Weizman, whom Mr. Khalil claimed as a good friend, had an excellent understanding with the Egyptian Defence Minister. If he were to go, and still more if Mr. Begin's Government was to fall, there might well be a prolonged period of paralysis. The situation would be ^{still more} unfavourable if Mr. Weizman was succeeded by Mr. Sharon.

The Prime Minister asked about the compatibility of the Camp David process and of the ideas that King Hussein had been advocating. Mr. Khalil said that King Hussein's opinion was that the Camp David talks would get no further and that the Camp David procedure was itself wrong. Mr. Khalil's own view was that it would be better for the Camp David process to continue. He had an additional proposal to put forward which he believed would make it possible for King Hussein's ideas to be pursued in parallel and on a complementary basis with the Camp David process.

It was clear that the PLO could not advance their cause without accepting the right of Israel to exist. It was equally clear that the Palestinian National Council would not take this step/ ^{voluntarily} The Egyptian Government's proposal was that before the Arab Summit at the end of November, the leading Arab states should

/agree

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to the adopting of a suitable Security Council resolution on the basis that once it was passed, the PLO would make a statement accepting Israel's right to exist. The Security Council resolution would be a balanced one which would include references to the right of Israel to exist and to the right of the Palestinian people to self-determination but would contain no reference to a Palestinian state. It would of course be essential for the PLO to agree before the resolution was put to the Security Council that if it were passed they would accept it.

Mr. Khalil went on to argue that once the resolution had been passed and had been accepted by the PLO, terrorist activity, particularly along the Israel/Lebanon border, would cease. This in turn would make it possible for the PLO and Israel to withdraw from the disputed area in Southern Lebanon and for the PLO to be partly but not completely disarmed (they might for instance surrender their missiles while retaining small arms). If the Palestinians were then prepared to accept Lebanese sovereignty in the areas they at present controlled, the Syrians could pull back and a comprehensive settlement in the Lebanon might become possible. This would clear the way for the entry of the Palestinians into the autonomy talks and for an alignment of the positions of the PLO and of the Egyptian Government.

The Prime Minister asked how Mr. Khalil intended to pursue his idea and how much support he expected to gain for it. Mr. Khalil said that the next three or four weeks would be crucial. The Egyptian Government was not in direct touch with the other Arab Governments but Mr. Strauss, who was aware of and approved the plan, would convey it to President Carter. It would then be for the Americans to sell it to the other Arab Governments. Mr. Khalil himself had discussed the plan with Chancellor Kreisky, who was in favour, and with the PLO representative in Vienna, Mr. Sirtawi. Mr. Sirtawi had undertaken to convey the plan to Yasser Arafat. He was confident that Arafat would accept it. As regards the attitude of other Arab states, Mr. Khalil expected that only Iraq, Libya and South Yemen would reject it.

/Mr. Weir

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Mr Weir commented that Mr Khalil's plan was very similar to the abortive American initiative in August about which Egypt had had reservations. Mr. Khalil said that his plan was essentially the same. However, his Government had considered that the timing of the earlier initiative had been quite wrong. The plan had no chance of acceptance in the summer but the situation was now more favourable. The only result of pursuing the plan on the earlier timing would have been that the Israelis would have pulled out of the negotiations. Now everyone, including Israel, would accept the approach he was suggesting. The resolution might best be presented to the Security Council in January.

The Prime Minister said it would be essential to avoid another failure like that of the summer. If the idea was to be pursued then everything would have to be arranged before the resolution was put to the Security Council. Mr. Khalil repeated that he was confident that his plan would be accepted. He referred to a list of 14 questions which King Hussein had put to President Carter immediately after the Camp David talks and to which President Carter had given written answers. Those answers had covered every point on which Egypt was now seeking satisfaction. Mr. Khalil said that his Government asked for nothing more. As regards the PLO, if they did not accept the present opening they would lose their chance of involvement in the peace process for a considerable time. He did not underestimate the difficulties with the PLO. Chancellor Kreisky had come close to resignation earlier this year after he had been let down by his PLO contacts. He had wanted to present a peace prize jointly to a distinguished Israeli and to Mr. Sirtawi, the PLO representative in Austria. Yasser Arafat had agreed that Mr. Sirtawi might accept the peace prize and then, after knowledge of Chancellor Kreisky's plan had become public, Yasser Arafat under pressure from the Palestinian National Council had changed his mind. It was only the willingness of Mr. Sirtawi to defy Yasser Arafat and accept the award (at possible risk to his own life) that had saved the situation. This episode, according to

/Mr. Khalil

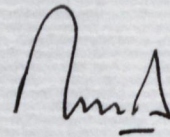
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- 5 -

Mr. Khalil, showed the difficulties of dealing with the PLO and of getting the Palestinian National Council to take a responsible line on the recognition of Israel's right to exist. However, Yasser Arafat would have to shoulder his responsibilities. Mr. Khalil was confident that if the other Arab states brought sufficient pressure to bear in the period between now and 25 November, he could be brought to do so.

The discussion ended at 1815.



26 October 1979

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Foreign and Commonwealth Office

London SW1A 2AH

24 October 1979

Dear Michael,

Call on the Prime Minister by the Egyptian Prime Minister

Mr Khalil is calling on the Prime Minister at 5.30 pm on 25 October. I enclose a brief for the Prime Minister's use, including a personality note on Mr Khalil. He is likely to concentrate on Arab/Israel issues, in particular the autonomy negotiations, but may raise the possibility of more aid for Egypt. It would also be helpful if the Prime Minister could raise with Mr Khalil the problems caused for British companies by the winding up earlier this year of the Arab Organisation for Industry (AOI). This is covered in the brief.

Michael Weir, our Ambassador in Cairo, will attend the meeting.

Yours ever

Paul

(P Lever)
Private Secretary

M O'D B Alexander Esq
10 Downing Street
LONDON

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CALL ON THE PRIME MINISTER BY THE EGYPTIAN PRIME MINISTER MR MUSTAFA
KHALIL, 5.30 pm, 25 OCTOBER 1979

Points to make

Arab/Israel

1. We support the autonomy negotiations. A successful result could be a further useful step towards a comprehensive settlement. But, while we understand the difficulties we are concerned at slow progress. The issues cannot be ducked indefinitely. What is President Sadat's strategy? Is agreement really possible?

2. We have made clear that we do not agree with restrictive Israeli views of autonomy. The self-governing authority should have legislative as well as administrative powers and a measure of real authority over public land and water resources. How can pressure be most effectively brought on Israel? What effect will Mr Dayan's resignation have on Israeli attitudes?

3. Concerned at continuing bad relations between Egypt and the rest of the Arab world. Countries such as Jordan and Saudi Arabia might be more receptive now to Egyptian overtures.

4. How do the Egyptians view the possibility of a new Security Council resolution on Palestinian rights? Could it provide a way of attracting the Palestinians into the negotiations?

Arab Organisation for Industrialisation (AOI)

5. Regret the decision by Saudi Arabia, Qatar and UAE to liquidate the AOI. Hope to see agreement on continued bilateral cooperation on the manufacture of arms, particularly the Lynx helicopters and Swingfire missiles. Hope that a delegation from Egypt will be able to visit the UK for discussions very soon.

Aid for Egypt (defensive)

6. Over last 18 months we have committed nearly £50 million in aid to Egypt. Disbursements in 1979/80 may total £21 million. Current review of all commitments means we are unable to take on any new projects for the time being.

Power generation (if raised)

7. UK companies are interested in doing business in Egyptian power field. Pleased to hear that officials are to discuss the possibility of coal fired power generation in Egypt. We shall be prepared to look at specific proposals for further assistance when the present review of overseas commitments is complete.



ESSENTIAL FACTS

Mr. Khalil's visit (not for use)

1. Mr Khalil is in London to take part in the one-day US/Egypt/Israel meeting on 26 October in the context of the autonomy talks. The meeting was arranged in London partly because Mr Khalil was going to be in Europe and partly to avoid an atmosphere of exaggerated expectations. Mr Khalil is coming to London from Vienna, where his primary object was to discuss Austrian participation in housing and telecommunications schemes for Egypt. He has said he does not intend to raise bilateral questions while in London, but he may ask about the possibility of increased aid.

Autonomy talks (not for use)

2. Under the provision of the Camp David agreement, a self-governing (autonomous) Palestinian authority is to be set up on the West Bank and Gaza Strip. The Administrative Council of the authority is to be elected by the inhabitants. The election will mark the beginning of a five-year transitional period at the end of which the final status of the areas will be determined in negotiations. The initial negotiations on the establishment of the self-governing authority were to have been between Egypt, Israel and Jordan and Palestinian representatives. However Jordan and the Palestinians have refused to take part. It was therefore agreed in a side-letter to the Egypt-Israel peace treaty that the US, Egypt and Israel should negotiate with the aim of finishing negotiations by May 1980.



3. Despite a considerable number of meetings at both political and working level, little substantive progress has been made so far. In the absence of agreement on the principles under which a self-governing authority would be established, it has been agreed not to seek results before the end of the year, but to allow a period for detailed discussion in the two main working groups, on the modalities of holding elections and the powers and responsibilities of the authority. Neither Israel nor Egypt seems anxious for quick progress or unduly concerned at the lack of results to show the other Arabs.

4. The current Egyptian priority is the successful completion of the interim Israeli withdrawal from Sinai. In the longer term Egyptian strategy and tactics are difficult to pin down. President Sadat's confidence in his relationship with Mr Begin and belief that changing Israeli attitudes will allow a satisfactory agreement to be reached with the help of US pressure are not shared by many of his advisers, including Mr Khalil. The latter said before leaving Cairo for Vienna that the meeting in London was to discuss the basic political differences between the parties, as a prelude to an eventual tripartite summit. He explained the Egyptian view by saying that autonomy must mean abolition of the Israeli military government and transfer of its powers to the autonomous authority. It was for the authority itself to lay down in detail what its responsibilities should be after it had been elected. There should be no attempt to define them in negotiations. Mr Khalil also said he intended to raise the issue of Israeli settlements during the talks.



5. We have heard in confidence from the Americans that Mr Strauss's main object at the meeting is in fact to persuade Mr Khalil to accept his proposal that a list should now be drawn up of the subjects to fall within the competence of the self-governing authority. This suits the Israelis, who see it as an opportunity to restrict the authority's powers, but Khalil may prove difficult to persuade. Egypt has made most of the concessions since the signing of the peace treaty and abandonment of their position of principle on this issue would further erode their credibility in Arab eyes.

6. The chances of agreement from the autonomy talks are poor, unless one side or the other makes major concessions. The negotiating objectives of the two sides are fundamentally different. The Egyptians want a form of full autonomy which will attract the Palestinians into the process and show the other Arabs that their professed attachment to the Palestinian cause is sincere. They see such autonomy as leading inevitably to Palestinian self-determination. The Israelis want to maintain ultimate control over the West Bank and above all to prevent any form of self-government which might be the first step down the road to an independent Palestinian state. They are therefore anxious to restrict the powers of the authority as far as possible and stick to the line that autonomy is for people not land. They have no intention of stopping the settlement of what they call Judea and Samaria.

7. The following are some of the questions which need to be resolved:-

(i) Which Palestinians should be able to take part in elections?



The Egyptians insist on the inclusion of East Jerusalem and some Palestinians living elsewhere. The Israelis reject any suggestion that East Jerusalem should be part of the autonomous area.

(ii) Should the elections be internationally supervised?
Egyptians for, Israelis against.

(iii) Should the self-governing authority have legislative powers, or only certain administrative (ie municipal) responsibilities, as the Israelis want?

(iv) Will the Israeli military government be withdrawn altogether?

(v) Will the authority have powers over public land (a key issue, related to the settlements question) and water resources (the West Bankers believe Israel is exploiting these to her advantage)?

8. The US view of the form of autonomy needed is much closer to the Egyptians than to the Israelis, as is our own. But the US have been handicapped by President Sadat's reluctance to upset Mr Begin by pressing too hard at this stage. They are nevertheless conscious that President Sadat will be looking to them to save both Egypt and the Camp David process by putting the squeeze on the Israelis. They are also aware of how limited their freedom of manoeuvre vis a vis Israel will be in an election year. Recently Mr Strauss has indicated his doubts over whether results are possible by May. Mr Dayan said on his resignation that he believed the autonomy talks could only be a show unless Israeli views changed.



9. Arab rejection of the autonomy talks remains firm. There is no possibility of either Jordanians or Palestinians joining in, although both are watching with interest. President Sadat has continued to abuse other Arab leaders, to the embarrassment of his colleagues and the Americans. The Arab opposition have no alternative strategy to offer. An Arab Summit is to be held in Tunis from 17 - 20 November. King Hussein is anxious to secure support at the Summit for a new Security Council resolution endorsing Palestinian rights. The Egyptians opposed the last attempt to produce a new resolution in August.

Arab Organisation for Industrialisation (AOI)

(may be drawn on)

10. The Arab Organisation for Industrialisation (AOI) was set up in 1975 as a partnership between Egypt, Qatar, Saudi Arabia and the UAE to create an indigenous Arab Defence industry. The two Gulf States and Saudi Arabia provided the greater part of the finance while Egypt supplied most of the technical expertise and manpower. The AOI's headquarters and many of its facilities were located in Egypt.

11. Joint venture companies were established with a number of Western firms. The British firms involved are:-

British Aerospace to manufacture 12,460 ^w Stingfire anti-tank missiles at a cost of £75 million and

Westland Helicopters and Rolls Royce to manufacture 250 Lynx helicopters at a cost of some £330 million.



12. Following the decision of Saudi Arabia, Qatar and UAE, in the context of sanctions against Egypt, to wind up the AOI, these three British companies stand to lose considerable business, and work for 2000 men. They hope for a satisfactory financial settlement and continuing arrangements to enable them to manufacture equipment for sale to Saudi Arabia and the Gulf States as well as through joint venture companies in Egypt. The Gulf States have made it clear that they expect to pay any compensation due from existing AOI funds held in Egypt or frozen in Western banks and that they will not consider direct purchases until the AOI has been finally wound up.

13. (Not for use) The Egyptians intend to continue with the AOI as a purely Egyptian venture. There is, however, no question of the rump Egyptian Organisation being able to maintain the joint venture agreements in their existing form, although they have been reluctant to accept this. British Aerospace are in the process of signing contracts for a more realistic revised production programme for 8000 Swingfire missiles, but the Egyptians despite agreeing in principle to send a delegation to London for talks, have declined to consider a revised programme of Lynx manufacture and have accused the two British companies of bad faith when they refused to continue work on the basis of the original AOI contracts. We have continued to press for discussions on joint venture production of Lynx. Prime Minister Khalil is a member of the AOI High Council. His visit to London provides a further opportunity to express our concern at a high level, and to press for an early visit by an AOI delegation to London.

Aid For Egypt

(May be drawn on generally)

14. President Sadat has talked of a Marshall Plan for Egypt and Secretary Vance has urged EEC governments to provide additional support for Egypt in the face of the Baghdad sanctions. But our own aid programme is already under pressure and it is clear that Britain will not be able to make any additional contribution in the near future.

15. The main thrust of our aid has been in the field of technical cooperation. The only British ongoing capital aid project is the Abu Zaabal fertilizer factory scheme. An adjunct to the factory is the West Sabaeya phosphate mining project which we had indicated our intention of supporting at a cost of £11.4 million. Following cuts in the aid budget, however, we have had to tell the Egyptians that we are unable to proceed with it.

16. Egypt has been a prime target under the Aid Trade Contingency Provision (ATCP). Since the Provision was set up £14.6 million of ATCP funds, in a total contract value of £38.5 million, have gone to Egypt. In addition a fourth contract with British Shipbuilders for 4 cargo ships worth £20 million of which the aid element will be £4 million has been accepted by the Egyptians but not yet signed. Further assistance under the ATCP, for Egypt as for other countries, will have to await the outcome of the current interdepartmental review of the workings of the provision, which is already heavily oversubscribed.

17. Total aid commitments to Egypt over the last eighteen months



have been £49.28m. (This excludes a pledged £50 million grant for Cairo sewerage). Disbursements in 1978-9 were £4.22 m and in 1979/80 will be about £21.5 m.

18. John Brown Engineering Ltd have heard that Prime Minister Khalil wishes to raise with Ministers the question of British aid to the power generation sector in Egypt during his visit. It is apparently a sector on which they would particularly like Western countries to concentrate. Our record in this field is already good. £12 million in UK aid under the ATCP is helping to finance the Egyptian purchase of four GEC 66 KV substations for Egypt's rural electrification scheme and the provision of Rolls Royce Gas Turbines. In addition the UK delegation to the UK/Egypt Joint Trade Commission meetings in June expressed a continuing interest in Egyptian power generation. It has been agreed that two officials from the Department of Industry should visit Egypt early in December to discuss coal fired power generation. Constraints on the aid programme rule out any more substantial assistance in the near future.

19. The Egyptian Prime Minister may suggest that, as a further contribution to the development of Egypt's electricity generating programme, HMG should finance the provision of a number of 25MW gas turbine generators (he may mention John Brown Engineering as the preferred supplier). We shall need to look closely at the project and to seek information from the British supplier and the Egyptian authorities concerned before we can consider any specific proposals of this kind.

KHALIL DR MUSTAFA

Prime Minister since 4 October 1978.

Appointed Foreign Minister 17 February 1979

Born 1920. Graduated from the Cairo Faculty of Engineering in 1941 and joined the Egyptian State Railways. From 1947 to 1951 he worked for the Chicago - St Louis Railway in the USA, studying at the University of Illinois, from which he obtained his doctorate in 1951. Returning to Egypt he became Professor of Railways and Engineering at Ain Shams University. From 1956 to 1964 he was Minister of Communications, from 1964 to 1965 Deputy Prime Minister for Communications and Transport, and from 1965 to 1966 Deputy Prime Minister for Industry, Electricity and Mineral Resources.

In 1970-71 he was Chairman of the Radio and Television system with the rank of Minister (appointed by Heikal then Minister of Information). In 1972 he was a signatory of the Baghdadi memorandum which called for a new Egyptian relationship with the USSR. Then a member of "Al Ahram" Strategic Studies Centre, he completed his book "The Energy Crisis in the USA" just before the October 1973 war. After the outbreak of the war he toured the oil producing states with Sayed Marei advocating the use of the "oil weapon", which Heikal in his "Road to Ramadan" virtually credits him with inventing.

In February 1974 he was appointed to the National Council for Production and Economic Affairs. In July 1975 he was "Industrial Adviser to the Chairman of the Arab International Bank". In June 1976 he was made Acting First Secretary to the ASU (though he retained his appointment at the Arab International Bank). He was appointed Prime Minister in a major Cabinet reshuffle in October 1978. Neat and dapper in appearance he is pleasant and interesting to talk to. He made no secret of the fact that his ASU appointment was temporary and of his wish to return to ministerial office. He visited the UK as an official visitor in June 1978 to study the workings of Parliament and the Press, and in December as Prime Minister to brief Mr Callaghan about the peace negotiations.

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Egypt

23 October 1979

You wrote to me on 22 October asking whether the Prime Minister would be able to see Prime Minister Khalil during his stay in London from 24-28 October. As I have told you on the telephone, the Prime Minister would be willing to see Mr. Khalil at 1730 on Thursday 25 October.

M O ' D B A

Paul Lever, Esq.,
Foreign and Commonwealth Office.

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Foreign and Commonwealth Office

London S.W.1

22 October 1979

Dear Michael,

US/Egypt/Israel Meeting in London

We have agreed to a US request to hold an informal meeting in the context of the autonomy negotiations in London on 26 October. The Americans say that they wanted a meeting in London to escape the glare of publicity and atmosphere of expectation generated by gathering in either Egypt or Israel. The Egyptian principal at the talks, Prime Minister Khalil was also due to be in Europe, principally visiting Austria. Apart from Mr Khalil, the meeting will be attended by Mr Robert Strauss, President Carter's Special Representative in the negotiations who is of Cabinet rank, and Dr Joseph Burg, Israeli Minister of the Interior.

Prime Minister Khalil has requested a meeting with the Prime Minister during his stay in London from 24-28 October. Lord Carrington recommends that the Prime Minister should agree to this. Mr Khalil, who is also Foreign Minister, is one of President Sadat's closest advisers. He is articulate, intelligent and much respected in Egypt. He may wish to discuss bilateral economic and commercial affairs as well as the peace talks, to which he is currently devoting most of his time. Lord Carrington believes that the Prime Minister would find a short meeting worthwhile. It would also be an important sign of our continuing support for Egyptian peace policies. If the Prime Minister agrees, what most suitable date would be Thursday 25 October, since 26 October is given over almost entirely to the trilateral autonomy talks.

Lord Carrington will see Mr Strauss and either he or the Lord Privy Seal will see Mr Burg while they are in London.

Yours ever

Paul

Paul Lever

M O'D B Alexander Esq
10 Downing Street

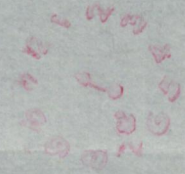
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Foreign and Commonwealth Office

London S.W.1



22 OCT 1979



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