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M PEKING 241830Z SEP 82

TO IMMEDIATE F C O

TELEGRAM NUMBER 596 OF 24 SEP 82

AND TO IMMEDIATE HONG KONG (PERSONAL FOR ACTING GOVERNOR)

TO PS TO SECRETARY OF STATE

FROM PS TO PRIME MINISTER

PRIME MINISTER'S TALKS WITH DENG XIAOPING: HONG KONG

1. THE PRIME MINISTER MET DENG XIAOPING ON FRIDAY 24 SEPTEMBER. DENG IMMEDIATELY RAISED THE QUESTION OF THE FUTURE OF HONG KONG AND ASKED THE PRIME MINISTER TO SPEAK FIRST.

2. THE PRIME MINISTER REPEATED MUCH OF WHAT SHE HAD SAID TO ZHAO, STRESSING THE FOLLOWING POINTS:

- A) THE TWO SIDES HAD THE COMMON OBJECTIVE OF MAINTAINING THE STABILITY AND PROSPERITY OF HONG KONG.
- B) THAT WHAT WAS SAID OR DONE NOW (UNDERLINED) WOULD HAVE AN IMMEDIATE IMPACT ON CONFIDENCE IN HONG KONG ITSELF AND INTERNATIONALLY:
- C) SHE KNEW HOW IMPORTANT SOVEREIGNTY WAS TO CHINA BUT IT WAS ALSO A DIFFICULT ISSUE FOR HER. HOWEVER, IF THE TWO GOVERNMENTS COULD AGREE DEFINITE ARRANGEMENTS ABOUT THE FUTURE ADMINISTRATION AND CONTROL OF HONG KONG AND IF SHE WERE SATISFIED THAT THEY COULD WORK AND COMMAND CONFIDENCE, AND IF SHE COULD JUSTIFY THEM TO THE BRITISH PARLIAMENT AND IF THEY WERE ACCEPTABLE TO THE PEOPLE OF HONG KONG, THEN SHE COULD CONSIDER THE QUESTION OF SOVEREIGNTY. WITHOUT SUCH AGREEMENT SHE COULD NO MAKE RECOMMENDATIONS TO HER GOVERNMENT ON SOVEREIGNTY.
- D) THE IMMEDIATE ISSUE WAS NOT WHAT WOULD HAPPEN IN 1997 BUT WHAT PEOPLE NOW (UNDERLINED) THOUGHT WOULD HAPPEN IN 1997.
- E) THERE WAS NOT ENOUGH TIME DURING HER VISIT TO RECONCILE THE DIFFERENCES BETWEEN THE TWO SIDES BUT SHE BELIEVED THOSE DIFFERENCES COULD BE RECONCILED THROUGH TALKS AND AND IT WAS ESSENTIAL TO MAINTAIN CONFIDENCE MEANWHILE

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- E) THERE WAS NOT ENOUGH TIME DURING HER VISIT TO RECONCILE THE DIFFERENCES BETWEEN THE TWO SIDES BUT SHE BELIEVED THOSE DIFFERENCES COULD BE RECONCILED THROUGH TALKS AND AND IT WAS ESSENTIAL TO MAINTAIN CONFIDENCE MEANWHILE.

THE PRIME MINISTER PROPOSED THAT THE TWO SIDES SHOULD ANNOUNCE BEFORE SHE LEFT PEKING THAT SHE SHOULD HAVE FURTHER TALKS, TO BE PURSUED URGENTLY, AND THAT THE COMMON OBJECTIVE OF THOSE TALKS SHOULD BE THE MAINTENANCE OF PROSPERITY AND STABILITY IN HONG KONG.

3. CHAIRMAN DENG XIAOPING SAID THAT ZHAO HAD ALREADY CLEARLY ENUNCIATED CHINA'S BASIC POSITION ON HONG KONG. THERE WERE THREE QUESTIONS - SOVEREIGNTY SEMICOLON THE CONTINUED PROSPERITY OF HONG KONG SEMICOLON AND DISCUSSIONS BETWEEN THE CHINESE AND BRITISH GOVERNMENTS ON HOW TO AVOID TURBULENCE IN HONG KONG IN THE PERIOD BETWEEN NOW AND 1997 AND HOW TO MAINTAIN HONG KONG'S PROSPERITY THEREAFTER.

4. DENG REITERATED THAT CHINA HAD NO LEEWAY ON THE SOVEREIGNTY QUESTION. IT SHOULD BE CLEAR TODAY THAT CHINA WOULD CERTAINLY RECOVER SOVEREIGNTY OVER HONG KONG IN 1997. ON THIS PRECONDITION CHINA AND BRITAIN WOULD HOLD TALKS ON FORMULAE FOR THE FUTURE OF HONG KONG AND ON POLICIES FOR MAINTAINING HONG KONG'S PROSPERITY. IN NO MORE THAN ONE OR TWO YEARS TIME THE CHINESE GOVERNMENT WOULD FORMALLY ANNOUNCE ITS DECISION TO RECOVER HONG KONG. THEY WOULD WAIT ONE OR TWO YEARS IN ORDER THAT THE TWO GOVERNMENTS COULD CONDUCT FRIENDLY CONSULTATIONS SO THAT MAJOR DISTURBANCES SHOULD BE PREVENTED AND SO THAT THE PROSPERITY OF HONG KONG WOULD BE MAINTAINED. TIME WAS NEEDED TO SETTLE THE FUTURE OF HONG KONG. BUT AN ANNOUNCEMENT COULD NOT BE PUT OFF FOR MORE THAN ONE OR TWO YEARS. HE THEN SUGGESTED THAT THE CHINESE RESUMPTION OF SOVEREIGNTY OVER HONG KONG WOULD BENEFIT BRITAIN BY BRINGING TO AN END THE PERIOD OF COLONIALISM.

5. THE PRIME MINISTER REPLIED THAT BRITAIN WAS NOT COLONIALIST SEMICOLON WE SIMPLY WANTED TO CARRY OUT OUR MORAL DUTY TO HONG KONG. WE KNEW THAT IN 1997 SOVEREIGNTY OVER 92 PERCENT OF HONG KONG WOULD PASS TO CHINA. THE BRITISH GOVERNMENT KEPT TO ITS TREATIES AND WAS NOT CONTESTING THE TERMINATION OF THE LEASE. SHE STRESSED AGAIN THE NEED TO BOLSTER INVESTOR CONFIDENCE NOW (UNDERLINED). SHE SUGGESTED THAT WE SHOULD BEGIN TALKS IMMEDIATELY IN ORDER TO OBTAIN AN AGREEMENT ACCEPTABLE TO CHINA, HONG KONG, AND THE BRITISH PARLIAMENT AND WHICH WOULD PRESERVE PROSPERITY, FOR IF WE DESTROYED PROSPERITY IT WOULD NEVER RETURN. SHE RECOGNISED THAT CHINESE HAD ITS OWN POSITION ON SOVEREIGNTY. WE

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IN ORDER TO OBTAIN AN AGREEMENT ACCEPTABLE TO CHINA, HONG KONG, AND THE BRITISH PARLIAMENT AND WHICH WOULD PRESERVE PROSPERITY, FOR IF WE DESTROYED PROSPERITY IT WOULD NEVER RETURN. SHE RECOGNISED THAT CHINESE HAD ITS OWN POSITION ON SOVEREIGNTY. WE TOO HAD OUR POSITION. BUT THESE POSITIONS WERE RECONCILABLE AND IN THAT SPIRIT WE COULD ENTER TALKS.

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6. DENG REPLIED THAT HE HOPED WE WOULD UNDERSTAND THAT CHINA WOULD RECOVER SOVEREIGNTY OVER THE WHOLE OF HONG KONG BY 1997. HE DID NOT THINK HONG KONG'S PROSPERITY COULD ONLY BE MAINTAINED UNDER BRITISH ADMINISTRATION. THE MAINTENANCE OF PROSPERITY WOULD DEPEND FUNDAMENTALLY ON THE POLICY PURSUED BY CHINA TOWARDS HONG KONG AFTER IT HAD RECOVERED SOVEREIGNTY AND WHEN HONG KONG WAS ADMINISTERED BY CHINA. SOME CHANGES WOULD BE MADE BUT HONG KONG WOULD REMAIN A CAPITALIST SOCIETY.

7. DENG CONTINUED THAT IT WAS UNAVOIDABLE THAT THERE WOULD BE SOME QUOTE FLUCTUATIONS UNQUOTE AFTER CHINA ANNOUNCED THAT IT WOULD RECOVER SOVEREIGNTY. CHINA WOULD TRY TO AVOID MAJOR FLUCTUATIONS AND, WITH COOPERATION, THIS COULD BE DONE. MANY PEOPLE SAID THAT IF PROSPERITY IN HONG KONG COULD NOT BE MAINTAINED THIS WOULD EFFECT CHINA'S MODERNISATION DRIVE. THERE WOULD BE SOME EFFECT BUT IT WOULD NOT BE GREAT. WITH REGARD TO THE FLIGHT OF INVESTMENTS FROM HONG KONG, PROVIDED CHINA PURSUED APPROPRIATE POLICIES FOREIGN INVESTMENTS WHICH HAD LEFT WOULD RETURN. WHEN CHINA ANNOUNCED ITS INTENTION TO RESUME SOVEREIGNTY, IT WOULD AT THE SAME TIME ANNOUNCE THE POLICIES AND MEASURES TO BE ADOPTED. IF THERE WERE VERY LARGE AND SERIOUS DISTURBANCES IN THE NEXT FIFTEEN YEARS THE CHINESE GOVERNMENT WOULD BE FORCED TO CONSIDER THE TIME AND FORMULA FOR THE RECOVERY OF ITS SOVEREIGNTY. NOT ONLY SHOULD THE TWO GOVERNMENTS NOT DO ANYTHING TO THE DETRIMENT OF PROSPERITY, BUT THEY SHOULD PREVENT BUSINESSMEN FROM DOING THINGS DETRIMENTAL TO THE PROSPERITY AND STABILITY OF HONG KONG. HE PROPOSED THAT THE TWO SIDES SHOULD AGREE TO START DISCUSSIONS THROUGH DIPLOMATIC CHANNELS ON THE PRECONDITION THAT IN 1997 CHINA WOULD RECOVER SOVEREIGNTY OVER HONG KONG. ON THIS PRECONDITION THEY WOULD DISCUSS HOW TO ENSURE A GOOD TRANSITIONAL PERIOD AND WHAT WOULD BE DONE THEREAFTER.

8. THE PRIME MINISTER REPLIED THAT SHE WAS WORRIED BY DENG'S REFERENCE TO DISTURBANCES. SHE WAS NOT CONTEMPLATING DISTURBANCES SEMICOLON SHE WOULD DO EVERYTHING TO PREVENT THEM. SHE ALSO WANTED TO PREVENT FINANCIAL COLLAPSE. SHE URGED DENG NOT TO MAKE THE KIND OF STATEMENT HE HAD SUGGESTED AND ASKED HIM TO AGREE THAT THE TWO SIDES SHOULD SAY THAT THEY HAD HAD TALKS, THAT THIS HAD BEEN THE FIRST EXCHANGE, IT HAD NOT BEEN POSSIBLE TO SOLVE ALL

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9. THE PRIME MINISTER AND DENG THEN AGREED THE STATEMENT IN MY TELNO 591 OF 24 SEPTEMBER.

10. THE PRIME MINISTER WISHED THE CONTENT OF THIS REPORT TO BE VERY CLOSELY GUARDED. IT SHOULD THEREFORE BE GIVEN EXTREMELY RESTRICTED CIRCULATION.

11. PLEASE COPY TO NO. 10 DOWNING STREET.

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