



10 DOWNING STREET

From the Private Secretary

5 August 1982

The Prime Minister recalls with pleasure your generous hospitality on 12 July. She much enjoyed the occasion, both as a prelude to her forthcoming visit to China and as an opportunity to talk with you.

As the Prime Minister explained, she is greatly looking forward to an exchange of views with your Government on current international and bilateral matters. She hopes, in particular, that her programme will be so arranged as to allow serious discussion at the appropriate level on the subject of the future of Hong Kong.

You asked about the possibility of a soft loan which Sir Y.K. Pao and others have raised with the British Government. The Government would very much like to increase the British contribution to China's modernisation programmes, but a soft loan poses problems for us at present. Export credits, supported by the Export Credits Guarantee Department, are already offered at concessionary rates of interest in accordance with the OECD consensus. Where particular projects are concerned we can consider matching such lower interest rates as may be offered by our competitors. But it would be difficult for us to envisage the major new commitment in China, not linked in the first instance to specific projects, which has been discussed.

We do of course make a major contribution to the aid programmes pursued in China by multilateral agencies such as the World Bank and UNIDO and we very much welcome their activity. We are also prepared to consider ways of strengthening our bilateral technical and other exchanges.

You also enquired about a Government tax in connection with negotiations for the Luda destroyer refit. It is our practice, where the costs of research and development of equipment have been borne by public funds, to require some payment in respect of these costs when that equipment is sold. This naturally results in a

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higher price. But while negotiations on price must remain a matter between your Government and British industry, the British Government are prepared to consider constructively how, in the special circumstances of this project, the levy might be reduced or waived in the interests of securing a settlement satisfactory to both parties.

The Prime Minister is aware of the importance of this contract, not only commercially, but as a milestone in the relations between our two countries in the defence field. She very much hopes that it will soon be successfully concluded.

Thank you again for a memorable evening.

JOHN COLES

His Excellency Mr. Ke Hua