

SECRET

FM PEKING 300835Z DEC 82

TO IMMEDIATE FCO

TELEGRAM NUMBER 874 OF 30/12/82

REPEATED FOR INFO TO PRIORITY HONG KONG

HONG KONG TEL NO ^[sic] 1510

FUTURE OF HONG KONG .

1. TUR ASKS WHETHER THE CHINESE HAVE THOUGHT THROUGH THE IMPLICATIONS OF THE GUANGDONG NUCLEAR PROJECT. THE ANSWER MUST BE THAT THEY HAVE CERTAINLY THOUGHT ABOUT IT IN THE CONTEXT OF THE FUTURE. THEY HAVE ALL ALONG SOUGHT TO PROLONG THE PERIOD OF REPAYMENT OF THE LOANS, AND POSTPONE THE START OF REPAYMENT. WE KNOW THAT ZHAO ZIYANG HAS BEEN PERSONALLY INVOLVED IN DECISIONS ON THE PROJECT, AND HE IS CERTAINLY INVOLVED IN DISCUSSION OF THE FUTURE. WHETHER THE CONCLUSIONS THEY HAVE REACHED ON THE BASIS OF THIS CONSIDERATION ARE SOUND IS ANOTHER MATTER.

2. GIVEN OTHER DEMANDS ON THEIR LIMITED RESERVES OF CAPITAL AND FOREIGN EXCHANGE, THE POSSIBILITY OF FINANCING THIS PROJECT BY SALES OF ELECTRICITY TO HONG KONG IS A KEY FACTOR. THE VIABILITY OF THE PROJECT FROM THE CHINESE POINT OF VIEW THEREFORE DEPENDS ON THE HONG KONG ECONOMY GROWING AT A RATE WHICH WILL PROVIDE A DEMAND FOR ELECTRICITY CONSISTENT WITH THE PROJECTIONS WHICH MAKE THE PLAN POSSIBLE. IT WILL ALSO DEPEND, THOUGH TO A LESSER EXTENT, ON THE VALUE OF THE HONG KONG DOLLAR. THE CHINESE BELIEVE THAT THEY CAN MAINTAIN THE PRESENT FINANCIAL AND SOCIAL SYSTEM IN HONG KONG AFTER THEY REGAIN SOVERIGNTY. WE ARE, AT THE VERY LEAST, DOUBTFUL ABOUT THIS.

3. HOWEVER, IF THE CHINESE CALCULATION IS WRONG, THE CONSEQUENCES ARE SERIOUS FOR THEM RATHER THAN FOR US. IF THE BANK OF CHINA HAS GUARANTEED LOANS AMOUNTING TO SEVERAL BILLION DOLLARS WHICH ARE TO BE FINANCED OUT OF RECEIPTS IN HONG KONG CURRENCY, THERE WILL BE A POWERFUL EXTRA INCENTIVE FOR THE CHINESE GOVERNMENT TO PRESERVE THE PROSPERITY OF HONG KONG BOTH IN THE IMMEDIATE FUTURE AND

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AFTER 1997. UNLESS THE BANK OF CHINA WERE TO RENEGE ON ITS GU-
ARANTEES, THE CONSEQUENCES OF CHINESE MISCALCULATION WOULD BE VERY
MUCH LESS SERIOUS FOR THE HONG KONG GOVERNMENT OR CLP.

TO THIS EXTENT THERE WILL THEREFORE BE ADDED
PRESSURE ON THE CHINESE TO COME TO A REASONABLE SETTLEMENT ON HONG
KONG. THIS IS TO OUR ADVANTAGE AND TO HONG KONG'S.

4. THE COMMITMENT HOWEVER WILL DEMAND A (NEXT THREE WORDS
UNDERLINED) QUID PRO QUO. THE CHINESE WILL EXPECT THE HONG KONG
GOVERNMENT TO GIVE WHOLEHEARTED SUPPORT TO THE OFF-TAKE
AGREEMENT AND PERHAPS TO COME TO CLP'S RESCUE ON THE EQUITY
QUESTION. THEY WANT CLP TO HAVE A REAL AS OPPOSED TO NOMINAL
EQUITY HOLDING IN THE JOINT VENTURE AS A MEANS OF ENSURING THAT
CLP WILL NOT RAT ON THE PROJECT EITHER DURING THE CONSTRUCTION
STAGE, OR LATER AS A CUSTOMER. THE BANK OF
CHINA'S REPORTED PRESENT WILLINGNESS TO GIVE A
90% GUARANTEE, COMPARED WITH ITS EARLIER REFUSAL TO GO
BEYOND THE PROJECTED 60% GUANGDONG POWER COMPANY'S
EQUITY STAKE IS A MEASURE OF CHINESE ANXIETY ON THIS POINT.

5. THE REVERSE OF THIS COIN IS THAT IF THE HONG KONG
GOVERNMENT DOES NOT RESPOND APPROPRIATELY, THE
PROJECT WILL PROBABLY NO LONGER BE VIABLE IN CHINESE EYES
AND WILL GO OFF THE BOIL AGAIN. THE CHINESE
WILL CONCLUDE IN THE WIDER CONTEXT THAT THE PROSPECTS OF
CLOSE CO-OPERATION WITH THE HONG KONG GOVERNMENT ARE NOT GOOD.
THEIR WILLINGNESS TO INVEST IN THIS PROJECT IS IN A SENSE
AN ACT OF FAITH IN THE FUTURE PROSPERITY OF HONG KONG.
IF THE HONG KONG GOVERNMENT APPEARS TO BE UNWILLING TO MAKE
A SIMILAR ACT OF FAITH, THIS WILL BE A PRETTY DAMAGING PROP-
AGANDA POINT WHICH WE SHALL BE GIVING TO THE CHINESE TO USE WITH
THE HONG KONG PEOPLE. I IMAGINE THAT IT WOULD ALSO BE DAMAGING
FOR CONFIDENCE IN HONG KONG GENERALLY. ON THE OTHER HAND,
A WILLINGNESS TO MAKE A SIMILAR ACT OF FAITH WOULD
BE A BOLD STROKE INDICATING CONSIDERABLE CONFIDENCE IN THE FUTURE.
IT COULD HELP TO RESTORE COMMERCIAL CONFIDENCE IN HONG KONG,
AND INCIDENTALLY TO ENCOURAGE WESTERN BANKS TO PARTICIPATE IN THE
LOANS. AT PRESENT THERE ARE NO OBVIOUS SIGNS OF EAGERNESS ON
THEIR PART.

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6. ON BALANCE I CONSIDER THAT THE ADVANTAGES IN THE PROJECT GOING AHEAD ARE MUCH GREATER FOR THE UK AND HONG KONG THAN THEY ARE FOR THE CHINESE GOVERNMENT IN THE CONTEXT OF THE NEGOTIATIONS ON THE FUTURE OF HONG KONG. THE CHINESE GOVERNMENT HAVE PROBABLY NOT FULLY REALISED THIS.

CRADOCK

FUTURE OF HONG KONG

LIMITED

HD/HKGD

HD/FED

HD/PLANNING STAFF

HD/PUSD

PS

PS/LORD BELSTEAD

PS/PUS

MR GIFFARD

MR DONALD

SIR J BULLARD

MR GILLMORE

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SIR I SINCLAIR LEGAL ADVISER

MR ROBERTS NEWS DEPT

MR COLES NO 10 DOWNING ST

MR MARTIN ASSGS. STAFF

MR HANLIE CABINET OFFICE

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MR COLES

HONG KONG

When Sir Frank Cooper paid his farewell visit on the Prime Minister, he said how worried he was about the prospects for Hong Kong. He thought that there was no prospect that the Chinese would agree to anything less than full sovereignty and control, but this would be very prejudicial to the interest of a large number of Hong Kong residents, many of whom had originally been refugees from the Chinese. However, Sir Frank Cooper said - and the Prime Minister agreed - that there was no realistic prospect of defending Hong Kong from the Chinese if they were determined to take it over.

In the course of a brief discussion, Sir Frank Cooper said that contingency plans were being made for the maintenance of internal order in Hong Kong. But he suggested that it would be wise for the Prime Minister to ask the Chiefs of Staff to let her have their professional assessment of the scope for reinforcing and defending Hong Kong in the event of external aggression. Sir Frank Cooper suggested that it would be a defence for the Prime Minister to say that she had obtained this assessment.

The Prime Minister agreed and asked me to arrange to obtain an assessment of this sort. Since this is not immediately urgent, I have not acted on it because I thought that it might be easier for you to frame such a request in the context of the rest of policy towards Hong Kong without raising the alarms which such a request, coming out of the blue, might cause.

F.R.B.

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24 December 1982