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Treasury Chambers, Parliament Street, SW1P 3AG
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Charles Powell Esq
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Dear Charles

EUROPEAN COUNCIL: MIXED CREDITS

The Chancellor thinks that it would be very helpful if the Prime Minister could find an opportunity to raise the question of mixed credits with President Mitterand in the margins of the European Council next week. In his view it is very much in the UK interest that progress should be made in the negotiations with the Americans and others at the OECD Consensus meeting from 10-12 December. At the moment, however, French intransigence is blocking agreement on even a limited EC negotiating position; and the risk of damaging US entry into the mixed credits field is a real one.

The Chancellor proposes to raise the matter first in his talks with M. Beregovoy during the Anglo-French Summit later this week. We will, of course, let you know of any relevant developments at that meeting. In the meantime I attach a brief for the Prime Minister' use.

I am copying this letter to Len Appleyard (FCO) and Richard Hatfield (Cabinet Office).

Yours ever
David

D L C PERETZ
Principal Private Secretary

MIXED CREDITS

POINTS TO MAKE

1. Important to agree on Commission's mandate for OECD meeting on 10-12 December.

2. Not a question of bowing to US pressure. Commission's proposals desirable in themselves.

3. Proposals deal with "transparency" only. They will make unfair competition from others, eg Japanese, more difficult. They involve no restriction on individual countries' freedom of action.

4. If it would help, could clarify Commission's mandate further, eg bymaking it clear tht face-to-face consultations would not override an individual country's position if it did not agree to a common approach.

BACKGROUND

Mixed credits are a method of financing exports of capital goods by combining aid funds (a 25 per cent grant is typical) with commercial credits. The UK favours the multilateral phasing out of mixed credits because they are a distortion of trade and their use is provoking an escalating competition in export subsidies.

The OECD Ministerial in May agreed that prompt action should be taken to strengthen transparency and discipline in their use. Since then the French (with Italian support) have blocked proposals to this end in Community discussions. This has irritated the Americans, who cancelled the last OECD consensus meeting.

The Commission has now drafted a proposed negotiating mandate for use at the OECD meeting fided for 10-12 Deecember. This would:-

(1) Widen the definition of mixed credits to include all forms of soft financing, including for example the device used by the Japanese, Swedes and Austrians of 'preblending' aid with commercial loans to produce subsidised interest rates.

(2) Increase the period and threshold for the prior-notification of mixed credits to competitors. At present only offers of a grant element between 20 per cent (the minimum permissible) and 25 per cent are notified in advance and the period of notice is only 10 days.

(3) Introduce meetings between country representatives to discuss specific projects ('face-to-face consultations') with a view to agreeing a common approach.

With the exception of the French, all EC countries (now including Italy) have accepted these proposals. The French so far are only prepared to agree to item (1).

The last chance of agreeing an EC negotiating mandate on these lines is at ECOFIN on 10 December. The Commission's proposals are limited in scope: they deal only with "transparency" and do not involve <u>restricting</u> mixed credits (as the Americans, and we, would like) at all. Nevertheless they would at least allow negotiations in OECD to start. If there is no progress the Americans are threatening to use mixed credits on a scale which would seriously damage EC exports of capital goods. They have already started offering mixed credits in one or two cases.