

PRIME MINISTER

MEETING WITH THE JAPANESE PRIME MINISTER

Mr Kaifu has asked for a bilateral with you in Houston before the Economic Summit. He is coming to your hotel suite at 3 pm on the Sunday afternoon.

Since you last met him he has won an election and his standing in Japan is remarkably high. Although some older rivals would very much like to get him out, they dare not do so. Meanwhile the economy is racing ahead, with five per cent GNP growth this year. Kaifu recently pulled off a successful conclusion to the Structural Impediments Initiative talks with the United States.

You will want to start by congratulating Mr Kaifu on his election victory and the success of his policies, and say how very much we welcome the continuing flow of Japanese investment to the United Kingdom. The Trade and Industry Secretary has been battling away valiantly in the European Community to ensure access for Japanese cars manufactured in the United Kingdom. We remain Japan's main champion on this. We hope that this investment will continue and the Japanese will not allow themselves to be put off by ludicrously exaggerated press reports that there is a risk of Britain leaving the European Community, or being marginalised within it. The whole thrust of our efforts is to ensure a European Community that is open to trade and investment with countries like Japan, and you are absolutely determined to win on that one.

You might go on to deal with some of the subjects on the Summit agenda, in particular assistance to the Soviet Union, relations with China, and the Uruguay Round. The Japanese are sceptical on aid to the Soviet Union and are likely to be resistant to any commitment in Houston. They are closest to us in wanting to open up relations with China, and we might together press for relaxation of restrictions on World Bank lending. The Japanese will probably try to lie low on the Uruguay Round and

agriculture. You will have to bring home to him that we shall only get a successful outcome if every country plays a part, and that means the Japanese will have to make concessions on rice. The consequences of failure of the Round would be very damaging indeed, perhaps most of all to Japan.

You might also raise South Africa on which the Japanese have been very cautious. But our self interest on the trade side is to see Japan maintain the sanctions as long as possible.

On the bilateral front, there are no real outstanding problems. The air services issue has been resolved. Our trade is doing well, although there is still a very large deficit on our side (£5 billion). The Princess Royal is going to Japan in September, the Prince and Princess of Wales will attend the Enthronement of the Emperor in November. There are a large number of ministerial visits planned.

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Sean Charles,

Bilateral with Prime Minister Kaifu at Houston

The Prime Minister will have a bilateral meeting with Mr Kaifu at Houston on 8 July. This will be their third meeting since the Prime Minister's visit to Japan in September 1989: their last meeting was on 12 January, during Mr Kaifu's tour of Europe. Despite speculation that Mr Kaifu's political base is insufficient to keep him long in office, his standing in the opinion polls remains high. None of his rivals dares mount a challenge at present: the continued period of uninterrupted economic growth (43 months, the second longest since the war), 5% GNP growth in 1989/90, and the successful conclusion of the Structural Impediments Initiative (SII) talks with the US are all likely to enhance his popularity further.

The Japanese have asked to exchange views on two of their major concerns at the Summit, aid to the Soviet Union and China. It is also an opportunity to talk to them on the Uruguay Round and South Africa. Mr Kaifu is also likely to enquire about EC integration. Our main objectives are to:-

- Explain our views on the way forward on aid to the Soviet Union, and stress the need for coordination with the Japanese;
- Confirm that we share Japanese views on the need to adopt a more forward-looking policy towards China, while continuing to look for an improvement in human rights performance;
- Remind the Japanese that a successful Uruguay Round settlement will involve concessions on rice;
- Stress that the UK continues to play an influential role in the EC, and continues to welcome Japanese investment.

Assistance to the Soviet Union

The Japanese have asked to discuss this subject. They are much more sceptical than most Western countries about how much has been achieved under President Gorbachev, and think that the Pacific Rim perspective on security policy is inadequately acknowledged by the Western Alliance. They have made clear that they are not willing to consider financial assistance to the USSR until the Northern Territories issue has been resolved satisfactorily. There has been no progress

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on this recently, although the forthcoming visits to Japan of Shevardnadze (in September 1990) and Gorbachev (in 1991) may help to move things forward.

The Prime Minister might give Mr Kaifu our views on how the West might help the process of economic reform. It would be helpful if she could brief him on the decisions taken at the Dublin European Council and explain our thinking on the way forward (above all the need to bring in non-EC countries with the aim of setting up an exercise similar to the G24 for Eastern Europe). She could draw on the following:

- Money is not the Soviet Union's problem. Essentially a rich, not a poor country. Needs expertise and must learn how to mobilise its own resources. Without necessary skills, other help will inevitably be wasted.
- Question of wider help discussed by Dublin European Council. Commissioned preliminary analysis of the problems faced by the Soviet economy. We can only decide possible remedy when we know precisely what the patient is suffering from.
- If help is to make sense it must be preceded by Soviet commitment to major structural reform. As aid begins to flow, reforms must be implemented, and if reforms stop, so must aid.
- Reform must also include lasting switch of Soviet expenditure from military programmes.
- Important that this should not be treated simply as an EC exercise. Essential both that it is coordinated more widely, above all with Japan and North America, and that Commission work hand-in-hand with those with real expertise (IFIs - in particular IMF/IBRD).
- Wrong to prejudge conclusions of preliminary EC analysis. Quite likely that best way forward is not through eg new loan facilities for Soviet Union but through increased training and know-how programmes.

China

The Japanese have circulated a paper to G7 partners calling for a full exchange of views on policy towards China at Houston. This stresses the need not to isolate China and the importance of stability in China as reasons for the West to relax its stance. The Japanese concern also reflects their wish to go ahead with the third Yen development loan (Yen 810bn, roughly US\$5.4 bn) stalled because of last June's events. They have put partners on notice that they intend to go ahead with the loan following Houston. The Japanese are keen to avoid any declaration at Houston that further restricts Western countries' dealings with China.

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We have taken a similar line within the EC, recommending a further relaxation of the Madrid Declaration measures against China (in particular of the suspension of Ministerial and high level contacts and of concessional finance for development projects). We have not sought relaxation of the suspension of arms sales and high level military contacts. There has, however, been no consensus among the Twelve for a relaxation. France has taken a lead in arguing that there has been insufficient progress in the human rights situation in China to justify such a relaxation.

In speaking to Mr Kaifu the Prime Minister may like to say:

- we agree with the general Japanese approach that the West should adopt a more forward looking policy towards China.
- we have been arguing within the Twelve for a similar approach; but there has been no consensus among European partners for a significant relaxation of the EC's measures because of continuing concern about China's human rights record.
- we share Japanese hope that the Summit will not make any declaration that would further restrict Western countries' dealing with China.
- nonetheless, there remains concern about China's human rights record: while we wish to see a return to a more normal relationship it is important to emphasise that the West is looking for further progress by the Chinese on reform and on their human rights performance. It is important that the political declaration and/or press statement should reflect this.
- we are grateful for the Japanese Government's continuing encouragement of Japanese investment in Hong Kong and we hope that Japan will do all it can to maintain the confidence of Hong Kong people in the future.

GATT Uruguay Round

The GATT Uruguay Round will be a key issue at Houston. EC/US differences over the nature of the commitments to be made on agriculture will need to be resolved. Japan's main concern is to continue her high level of support and protection for rice, aimed at maintaining self sufficiency. This issue has a very high political profile in Japan. The Japanese are therefore happy for the limelight at Houston to be taken by the EC/US dispute. Nevertheless, for the draft communiqué Japan has proposed a reference to "taking account of food security" which the US have not yet agreed. We can accept the Japanese wording on the basis that it does not excuse Japan from the reductions in her support and protection

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for rice, which will be necessary if we are to get a good outcome on agriculture in the Round.

We hope that Heads of Government at Houston will agree on the need for stronger rules for dispute settlement. In return we want the US to abandon use of unilateral measures and we expect a commitment to this effect to be included in the communiqué: Japan, as a main target of US measures, stands to gain from such an outcome, but has yet to give public support to the need for stronger dispute settlement rules.

The Prime Minister might draw on the following:

- GATT Uruguay Round rightly a high priority for Summit. Believe EC and US will resolve differences over the form of commitment we should make on agriculture.
- Recognise Japanese concerns on rice. Not really addressed so far. But we must all be ready to make commitments to reduce support and protection if we are to produce a credible result, in line with the commitments we made at the start of the Round. There can be no special cases.
- Welcome US willingness to confirm their commitment to use only multilateral routes for dispute settlement if GATT rules are strengthened. We must now work for a dispute settlement agreement in the Round strong enough to hold the US to this commitment. Japan, as a target of US unilateral action, stands to gain. Hope Japanese will continue to support strong dispute settlement as an aim of the Round.

South Africa

The Japanese acknowledge change is taking place in South Africa but are being cautious in their response. They will make no move to relax sanctions until the US does. They have inched their contacts with the SAG up to senior official level. Although they are negotiating with the ANC for a visit by Mr Mandela in the autumn, they are not yet prepared to invite President de Klerk. In view of their considerable trade with South Africa the Japanese want to ensure that any future South African Government will follow sensible economic policies, but they are unsure how to help achieve this. Against this background the Prime Minister may wish to brief Mr Kaifu on her talks with Mr Mandela. She may also wish to say:

- Profound and irreversible changes de Klerk has accomplished deserve international response. This will help reduce risk of right-wing backlash.
- UK, Italy, Netherlands, Spain, Denmark have already relaxed national measures. US Administration would probably have done so were it not constrained by legislation. EC has

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accepted principle of relaxation in response to change. Japan should be prepared to act too.

- South Africa will need growth and external finance to tackle successfully underlying socio-economic problems. Failure to do so could undermine political settlement. Main source will be private sector. We should encourage international financial institutions to help.

EC Integration

Kaifu is likely to ask about developments towards EC integration. There have been some recent signs that Japanese concern over UK attitudes towards the Community is discouraging inward investment (a report on NEC's strategy in Europe is being submitted separately). The Prime Minister may wish to say that:

- The UK continues to play an influential role in the Community: the UK has led the way on 1992, which remains the core of the current agenda.
- Our ideas have also been instrumental in making the debate on political union more practical, focussing on the balance between Community and national institutions.
- We shall be pursuing vigorously our recent proposals on EMU, which are widely recognised as a positive and serious contribution to the IGC preparations.
- UK remains the best location within the EC for Japanese investment. Japanese companies already here have been very successful. We would welcome more.

UK-Japanese Relations

The Japanese have asked to discuss our bilateral relations. These remain excellent with no significant problems outstanding, with the effective resolution of the argument over air services (on which the Prime Minister wrote to Mr Kaifu on 9 April) in the May talks. The Japanese have agreed to accommodate the additional services requested: it is for discussion between the airlines how those services may be accommodated within existing slots.

Bilateral contacts have strengthened since the adoption in 1987 of a strategy towards Japan that sought to establish a relationship encouraging political links to offset the emphasis on economic and trade issues. The reduction of the rate of increase in the trade deficit from 20% between 1987 and 1988 to 1.3% between 1988 and 1989 contributed, although the deficit for 1989 still stood at £4.8 billion. A large number of high-level visits to Japan are proposed for the remainder of 1990. The Princess Royal will visit Japan in

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September for an IOC meeting and to attend the UK90 Cultural Festival. The Prince and Princess of Wales will attend the Enthronement of the Emperor on 12 November. The Duke of Edinburgh will visit from 16-18 November privately but is expected to call on the Emperor. In addition to the Foreign Secretary's proposed visit to Japan in September, and a visit by Lord Brabazon (dates yet to be confirmed), several other Ministerial visits to Japan are planned including Mrs Chalker (July), Mr Howard (September), Mr Luce (September/October) and Mr Hunt (November). The Governor of the Bank of England will be visiting Japan in October. Mr Muto, Japanese Minister of International Trade and Industry, will be visiting the UK in August/September. Mr Ozawa, Secretary-General of the ruling Liberal Democratic Party, will be visiting in mid-July.

Japan's Bid for Permanent Membership of the UN Security Council

The Prime Minister will wish to be aware of the background to this issue. The Japanese have aired their aspirations for permanent membership of the Security Council. While leaving no doubt about the importance they attach to the issue they were content for discussions to continue on a confidential basis. They are not proposing action in the next UN General Assembly.

Any move to open the question of Council membership would awaken claims by India, Brazil and other regional powers to permanent seats, and claims by the Third World to a greater share of non-permanent seats. The Germans have recently indicated that they are not interested in pursuing permanent membership, but that may well change. Our interest is to avoid any threat to our position as a permanent member. Any change in the membership of the Security Council would be subject to the veto. So we are hearing the Japanese out but giving them no encouragement.

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