10/9/2

Falklands box.

RECORD OF MINISTER OF STATE'S OFFICE MEETING TO CONSIDER ECONOMIC POLICY TOWARDS THE FALKLANDS: 30 AUGUST, 1979.

Present

Mr Nicholas Ridley MP
Mr G Hall AUS
Mr Duggan SAmD
Mr Cowling "
Mr Osborne "
Mr Yapp, PS/Mr Ridley

Mr Baxter (ODA)
Mr Sparkhall (ODA)
Mr Hall (Economists)

1. Mr Ridley said he wanted to discuss in a general way the economic potential of the Falklands. Economic progress was bound up with the political problem of relations with Argentina: but if negotiations were to fail (and on balance this seemed rather more likely), we should need more ideas to develop the Islands in a hostile climate.

2. The Islands had considerable potential; how were we to unlock it. It was not a question of aid. The Islanders were a developed people; the soil and climate were advantageous. Obviously there were problems; distance, isolation, communications difficulties, lack of people. The Islanders' attitudes were a drawback; they had no entrepreneurial instincts; their approach to currency matters was naive, they saved their money instead of investing and borrowing for development. They were reserved towards outsiders. It was not surprising that people had not been prepared to invest in the Islands. The Islands' tax regime might well be inimical to investment. The absence of banking facilities inhibited development. The Falkland Islands Company stultified development.

3. We needed to change the economic atmosphere to encourage an influx of capital and people. There were a number of areas worth considering:

a) Falkland Islands Company (FIC)

The Department had submitted a paper on buying out the FIC. There were obvious difficulties in nationalisation. But interest could be stimulated in private banking circles: a bank might be persuaded to pay the going price for the company, put in the right sort of bright and active manager and sell

/off

off its assets. Any unsold could be transferred to the FIG. Some of the services provided by the company (eg island shipping) might more properly become an FIG responsibility. The whole operation might require a Government guarantee but it would be better to keep out. In many ways, the acquisition of the Falkland Islands Company could be regarded as a land reform measure. It would also break up a harmful monopoly.

b) <u>Currency</u>

The £ Falkland was tied to sterling. There might be advantages in breaking the link and floating, enabling the FIG to operate in the international market. This would require more sophisticated local financial advice and institutions.

c) <u>Commercial Banking Facilities</u>

Private capital on a large scale was needed. This would be facilitated by the establishment of local commercial banking operations: to provide competition more than one bank would be better; and money might be used to provide initial incentive. An overseas bank with major interests in Argentina would obviously be inhibited. But the Nova Scotia Bank of Canada, amongst others, might be interested. The difficulty was the tiny population.

d) <u>Tax Regime</u>

Income tax rates should be looked at; they could be higher than in the UK. Potential investors would be discouraged by too high Company tax rates.

e) <u>Government Infrastructure</u>

The present infrastructure was probably not capable of introducing and managing radical economic reforms. Institutional changes might be needed; attitudes would also have to change. An energetic go-ahead chief development officer/ financial secretary would be required.

/3.

3. Mr Hall said that development of the Islands' economic potential could only take place in the context of a settlement with Argentina. A total breakdown in the negotiations would put us in an impossible position: the Argentines would cut communications. We would have to provide services at great cost. But if we secured a settlement much could be done on the lines set out by the Minister.

4. Mr Hall said no approaches had been made to banks about their acquiring the FIC themselves; we had spoken only in terms of the advisory services which the banks might provide if someone else (eg FIG) were to acquire the company. Foreign and Colonial Investment Trust had an interest in Latin America and more specifically in the area around the Falklands. Rothschilds could also be approached. ECGD investment guarantees against political risks might also be reconsidered.

5. Mr Baxter said that the assumption in the ODA was that the land could not be improved. Mr Ridley said that more research was needed; the GTU were doing a good job. Many farmers he had spoken to believed the land could be improved and he had seen what was being done at North Arm and in the vegetable gardens in Stanley. But it would be expensive. The Falklands Company estimated that it cost £30 per acre to improve the land. They had made a start on 3,000 acres.

6. Mr Hall said the taxation position would need to be handled carefully as FIG finances could suffer, especially before increased investment flows began. The FIG might have to seek more aid for a time. Mr Ridley agreed. But the overriding need was to create more economic activity and hence more income.

7. Mr Duggan proposed that we should consult the Governor on

/these

these points; he would no doubt wish to seek the advice of his fiscal adviser. We would want to draw also on the expertise of ODA's Advisers. In the light of these responses, we could subsequently seek wider input, eg by contacting banks.
Mr Ridley agreed; he suggested a further meeting in some three months time.

South America Department
September 1979

Circulation

PS/Mr Ridley ✓
SAmD
ODA (Mr Baxter)
Economists
Governor, Port Stanley
Chancery, Buenos Aires