



DEPARTMENT OF TRADE AND INDUSTRY
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Handwritten initials and circled number 2

PS/
 Secretary of State for Trade and Industry

6 December 1984

Charles Powell Esq
 Private Secretary to the
 Prime Minister
 10 Downing Street
 London SW1

Handwritten initials 'MS'

Prime Minister
You enquired
about this. It
seems that
agreement is near.
I shall ask for
you to be kept
informed.
CDP 6/xii

Dear Charles

SALE OF AIRBUS TO TURKEY

You enquired this morning about the problem over the sale of Airbus aircraft to Turkish Airlines in view of the concern expressed by M. Fabius to the Prime Minister over the inability of BAe to support this business. The award of this contract to Airbus Industrie was announced in October and contracts were due to be signed this month. At a late stage, however, BAe instructed Airbus not to sign the contract because they were dissatisfied with the official support they were getting through ECGD.

ECGD cover for this sale - as with all other project business in Turkey - has been offered throughout on a risk sharing basis under which ECGD would take 60% of the risk on the proposed 10 year loan for 85% of the contract price, with the other 40% of the risk on the loan being carried by the private sector. This degree of support was maintained even though the final negotiations involved seven aircraft as against the three aircraft originally agreed inter-departmentally. For reasons which are not altogether clear - though we suspect a degree of brinkmanship by Sir Ray Lygo - BAe are unwilling themselves to carry any share of the exposure relating to the Airbus, and their bankers have still not decided whether they will carry on their own account the risk on the £36 million loan amount not covered by ECGD.

Mr Channon will be considering the position with officials on his return from the United States on Monday and will consider what should be done in the event that the banks refuse to accept their share of the risk. Our latest information suggests that there is a

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A good chance that this problem will be overcome within the next few days, but Mr Channon will consult colleagues if he considers that further support by ECGD should be given to prevent the loss of the business. We will keep you informed of developments.

Yours ever

Callum

M C McCARTHY
Private Secretary

JH5AMZ



PS/

Secretary of State for Trade and Industry

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CCPC
CCNO

20 December 1984

Charles Powell Esq
Private Secretary to the
Prime Minister
10 Downing Street
London SW1

NAM

Dear Charles,

SALE OF AIRBUS TO TURKEY

Following concern on the above issue expressed by M Fabius to the Prime Minister at the recent EC Summit, I wrote to you on 6 December giving some of the background and saying that Mr Channon was considering the issues involved. You replied on 10 December passing on the Prime Minister's wish to be kept informed.

2 As you have no doubt read in the Press, Mr Channon, after consulting the Chief Secretary, authorised ECGD to give full cover for the UK element of the seven Airbus aircraft sold to the Turkish airlines within the agreed credit ceiling for this market. As a result very little of this ceiling now remains to cater for other business in prospect for Turkey.

Yours ever

McCarthy

M C McCARTHY
Private Secretary

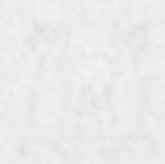
JH3BHF

Defence: Sales Pt 4



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 1) AT
 2) NBM

Treasury Chambers, Parliament Street, SW1P 3AG

CDD

12/12

Rt Hon Paul Channon MP
 Minister for Trade
 Department of Trade and Industry
 1 - 19 Victoria Street
 London
 SW1E 6RB

11 December 1984

Dear Minister

AIRBUS FOR TURKEY

Thank you for your letter of 11 December in which you sought my agreement to increase the amount of support to be provided for the sale of 7 Airbus aircraft to Turkey with an increase in the permitted ceiling on ECGD's exposure so that the amount of cover available for other business remains broadly as it was.

This is a very difficult case and I am reluctant to agree to either proposition and neither do I accept the implication of your argument that a market limit should be increased to accommodate a project that is turning out to be larger than originally expected. It is inherent in fixing a limit that choices may have to be made about what business can be covered by that limit. It is necessary in these circumstances to choose where one's priorities lie.

There is no justification for increased ECGD exposure on Turkey. ECGD have paid very large claims on Turkey in the past and limited cover has only recently been restored and this with some trepidation. Moreover, ECGD's financial position is such that they are in no position to take on unnecessary risks. As was acknowledged in the refusal to cover the proposed Tornado sale, the Turkish economy is in a poor state. The current account deficit is widening at a time when debt service obligations under earlier rescheduling agreements reach a peak. Unless the Current Account deficit is reduced substantially in the short term, creditor confidence in Turkey will evaporate to an extent where a rescheduling in late 1985 or 1986 may prove unavoidable. This is just the time when repayments on these aircraft begin.

It is not at all clear why the risk sharing arrangement envisaged for this sale cannot be delivered especially since BAe themselves said only last month that they could provide considerably more than this in support of the proposed Tornado sale. While BAe may be bluffing, one possible explanation is that the private sector's assessment of Turkey has worsened

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worsened considerably over this period so that they no longer are able to take on the risk. If this is so this would be no reason for ECGD to take on more risk. Indeed, there would be a case for cutting back on what cover is available.

It is normal practice to require risk sharing for business with Turkey and a risk sharing arrangement was a condition of the offer of any ECGD cover for this sale. There are no reasons for exceptional treatment in this case. Furthermore, there are other projects in prospect which would be squeezed out if increased cover for this Airbus sale were agreed. Because of the risk sharing arrangements on offer for those cases, more UK exports would be supported by the amount of ECGD cover available than would be with the 7 Airbus. Finally, as in the case of all Airbus business currently supported, subsidies are considerably higher than for other business. The guidelines on Subsidies and Risks said that when the acceptance of both a high risk and a high subsidy was required to secure a contract, the contract was probably not worth securing.

The amount of subsidy payable on all Airbus business is currently considerably higher than for other UK exports. Hopefully, the current discussions in Paris on a OECD Sector Agreement for Aircraft will reduce considerably the amount of support sales of these aircraft will require. If these negotiations are not successful we will need to review the scale of the support we give to the sales of Airbus in future cases.

Having said that, I recognise the strong pressures on us not to frustrate a large Airbus sale at this juncture. If you judge it essential, I will acquiesce in the provision of cover for the UK share of 7 aircraft on the terms you propose: 85 per cent, and without risksharing if you are satisfied that is not negotiable.

But I must insist that this is accommodated within the present Market Limit for Turkey, of £143 million (plus some £57 million set aside against risks on cash contracts). A review of the prospects of the Turkish economy is in progress and will be reported to Ministers in the New Year. I understand that the present draft does not indicate any improvement which would justify increasing the limit, though I shall of course be ready to reconsider that judgement when the review is complete. Meanwhile you will recognise that if the present limit is maintained, there will be no room within it for the Bosphorus Bridge project, even though nearly £20 million would be left for smaller-scale business. I am sorry about that: but judgements have to be made about priorities, and you clearly believe that Airbus comes first.

I am sending copies of this letter to the Prime Minister and to the Foreign Secretary.

Yours sincerely



for PETER REES

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[Approved by the Chief Secretary]



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From the Minister for Trade

The Rt Hon Peter Rees QC MP
Chief Secretary
HM Treasury
Treasury Chambers
Parliament Street
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SW1P 3AG

1) AT
2) NBPY
OAM 12/12

11 December 1984

Peter Rees

ECGD COVER FOR SALE OF AIRBUS TO TURKEY

As you will know, we have come under strong pressure to provide ECGD support for the full 85% of the UK share of the sale of seven Airbus to Turkey.

Up to now ECGD has offered support on a 60/40 risk sharing basis, giving a DML of £55 million. The contract has in fact been signed, subject to finance. Airbus Industrie are now saying that unless the British finance can be quickly confirmed, the order may still be lost to Boeing. The French and German governments have agreed to cover the full 85% of their shares (which comprise 40 per cent of the total order in each case), and the French Minister of Transport has just written to Geoffrey Pattie pressing for a quick and favourable decision. We can expect a similar approach from the Germans who have expended considerable political capital in Turkey in pursuing this order. The Turkish government is also insisting that ECGD support 85% of the UK share, as they do not wish a risk sharing arrangement to interfere with the capacity of the market to take up the loan they will shortly be seeking; Boeing are able to offer full Exim Bank support for their bid.

I am reluctant to provide cover in breach of the risk sharing principle we have established for large orders in Turkey, and I am concerned about the amount of cover which would be required for this one contract. On the other hand for us not to agree to extend ECGD cover could have a substantial adverse effect on BAe's future role in the Airbus consortium and cause considerable resentment on the part of the French and German governments. The Airbuses will also earn foreign exchange to the benefit of the Turkish economy. In all the circumstances, I consider that we should agree to the request for 85% cover.

I am, however, concerned about the implications for other business in Turkey, and in particular the second Bosphorus Bridge project. Cleveland Bridge, who built the first bridge, are facing strong international competition for this contract, particularly from the Japanese who are offering a soft finance package. We consider this



to be a very important contract, and that Cleveland Bridge will require ATP if they are to head off the Japanese. ECGD cover involving a DML of up to £40 million will be required. To date, your officials have been unable to agree the SCAT case, and I may need to write to you separately about this shortly.

The provision of 85% cover for the Airbuses would increase ECGD's exposure on this contract to £91 million, which would leave under £20 million of the total £200 million cover available under Section 2. In order to accommodate the likely maximum exposure on Bosphorus Bridge (on the risk sharing basis) and to leave some marginal flexibility I propose that the overall cover available should be increased by £30 million. I recognise that the economic outlook in Turkey remains a cause for concern; nevertheless ECGD considers that in view of the importance of the business involved this modest degree of additional risk can be accommodated.

An urgent decision is needed. Apart from the commercial pressures for a decision on Airbus, I shall be appearing before the House of Commons Select Committee on Trade and Industry tomorrow. You will have seen the publicity this case has received. I am bound to be questioned about it, and I think it is important that I should be able to say that the cover has been agreed. It would be particularly unfortunate if I were to be pressed on the difficulties, and on possible differences between us, and shortly thereafter announce that the cover would be given.

If therefore I do not hear from you in the course of today, I will take it that you are content for us to proceed on the basis I have proposed.

I am copying this letter to the Prime Minister and to the Foreign Secretary.

cc PS/Secretary of State
PS/Mr Pattie
PS/Lord Lucas
PS/Sir Brian Hayes
PS/Sir Anthony Rawlinson
Mr Croft, Dep Sec
Mr Roberts, Dep Sec
Mr Gill, ECGD
Mr Michell, Air
Mr Benjamin, PEP
Mr Bowder, Air
Miss Harding, ECGD
Mr Henley, ECGD
Miss Neville-Rolfe, PEP
(a/o)

Paul
Paul
PAUL CHANNON

112 DEC 1984

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