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10 DOWNING STREET

From the Private Secretary

27 November, 1984

Dear Steve,

Guangdong Nuclear Project

The Prime Minister has noted Mr. Channon's minute of 20 November and the Chief Secretary's supporting comment in his minute of 22 November.

She agrees to raise the matter with President Mitterrand and emphasise the importance of resisting Chinese demands on financing.

I am copying this letter to Private Secretaries to the members of EX, to the Private Secretary to the Secretary of State for Energy and to Richard Hatfield (Cabinet Office).

Yours sincerely

Charles Powell

C. D. POWELL

Steve Nicklen, Esq.,
Department of Trade and Industry

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CHIEF SECRETARY TO THE TREASURY

FROM: CHIEF SECRETARY
DATE: 22 November 1984

PRIME MINISTER

GUANGDONG NUCLEAR PROJECT

With CDP?

I have seen Paul Channon's minute of 20 November in which he proposes that we should use the forthcoming Anglo-French Summit to re-emphasise to the French the importance of standing together in the face of Chinese demands on financing terms for the Guangdong Project.

2 I entirely agree. If we are unsuccessful in this and the French continue to make concessions, the cost to us of pursuing this business will be very high indeed. The first issue to come up with the French is the interest rate to be charged if agreement with the Chinese is not reached by 15 January. I reluctantly agreed in September to match the French and hold until January the interest rate of 9.5 per cent despite the increase in interest rates in general and the Consensus rate (now 10.7 per cent) in particular. If the contract were signed on the basis of an interest rate of 9.5 per cent it would involve a subsidy equal to 36 per cent of the value of the UK exports, well outside the 25 per cent ceiling agreed by EX. At the time, the French said that they would increase the rate charged in line with the Consensus if agreement had not been reached with the Chinese by January. We must hold them to this. It will only be by increasing the interest rate charged that there will be any prospect of bringing the subsidy cost of this project back within the agreed ceiling. Even if this is settled satisfactorily, there still remains the question of how we respond to the reduction in the French premium which will give rise to considerable difficulties of principle as well as cost.

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3 The French are our partners but could do the whole project themselves. They have said that while they will co-ordinate negotiating strategy with us, they will not in the end risk losing the project by rejecting Chinese demands. But that should not mean adopting a supine attitude towards them. GEC's tender has favourably impressed the Chinese. There is no other competitor for this project and the Chinese are unlikely to walk away from it if their demands are not all met. They will not get such favourable terms for any alternative nuclear power station because of the recent nuclear sector agreement. And for them to cancel the Guangdong project would imply a lack of confidence in the future economic growth of Hong Kong.

4 Neither is it in the French interest to push the financing terms beyond our reach to secure the turbine order for themselves. Equally favourable and costly terms will also have to apply to the larger nuclear island at Guangdong and probably for the whole of the other planned Chinese nuclear power station that is also excluded from the terms of the nuclear sector agreement. The marginal cost to the French of securing the extra work on the Guangdong turbines by pricing us out of the market will therefore be enormous. We should therefore take a robust line with the French on financing terms for Guangdong.

5 I am sending copies of this minute to Paul Channon, other colleagues on EX, Peter Walker and to Sir Robert Armstrong.

PR

PETER REES