10 DOWNING STREET

Prime Minister

I think that you will find this interesting. It is written by a distinguished British consultant engineer who was retained by the Turkish Government as their consultant on the Bosporus Bridge project. It shows that by most criteria the Japanese / Italian offer was lower: though it says nothing about how the Japanese offer was financed.

CDP 10/5.

NEIL THORNE
DR W. BROWN
consultant to the Turkish Govt;
(Freeman Fox).

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Bosporus II Bidding
Background to Project

Whilst the Turkish contract is referred to as the second Bosporus Bridge, in fact the bridge itself is a relatively small part of the total contract - around 20%; the rest is for some 200 km of urban and rural motorways.

Plans for motorways in Turkey have been under discussion for the last 20 years, but progress has been slow, a mere 40 km being completed during that period.

When the present Turkish Government was elected in November 1983 they determined to make progress in many areas of infrastructure development, including power stations, dams, roads, etc, and to harness private enterprise to assist. Power station projects etc. were offered on a finance, construct and collect concept. It was therefore in keeping with this policy that in June 1984 the Minister of Public Works (a businessman prior to joining the new Government) should be receptive to suggestions that the sections of motorway as were reasonably defined or already designed should be linked to the Second Bridge project, then under active design (FF&P were commissioned as Engineers in December 1983) and the whole made the subject of a finance, construct, toll concession undertaking.

Two Turco-American Management Finance groups made such tentative suggestions.

There was a degree of scepticism within the Highways Department but the Minister became quite enthusiastic, pressing at least the concept of finance and construct while retaining the option for repayments through toll collection, should such an offer be made.

It thus became common knowledge in August 1984 that the Turks were pushing for the whole scheme - Bridge plus 200 km - and what is more, contractors were showing genuine interest.

The Minister realised that his trump card was the Bridge, and for two main reasons:

(a) the prestige value to the contractor concerned

(b) that its British design would be most advanced and would add to the experience of the contractor.

The Japanese industry in particular was well aware of this and had been following the project closely for many years. As long ago as 1978, when work on a second bridge nearly went ahead, the Japanese expressed willingness to fund it.

Thus it was clear that while the roads alone would, where credit was concerned, provide limited international interest, link it to the Bridge and insist, as far as possible, that the two were inseparable, then there was a chance that acceptable foreign credit would be forthcoming.

From the Turkish point of view it was not an unreasonable gamble. They see the provision of good motorway communications as essential to their economic growth.

Nevertheless, they did waver somewhat in that the overall contract was eventually divided into 4 sections, largely for internal administrative reasons. Section 2 included the Bridge and about 40 km of urban roads (see later).

The Turks informally encouraged interested contracting groups to make presentations and to discuss possibilities with them last September/October, and of course many did. The Cleveland Bridge Co. actually held a press conference at the Ritz in London before moving on to Ankara, and spoke of at least £200M credit being available via the American Express Bank.

Just before Christmas, documents clearly outlining the scheme were issued to practically all the groups who had expressed any interest, for them to develop their ideas of consortia etc, and also something more definitive about the provision of credit.

The project was still divided into 4 sections, and consortia were invited to apply for prequalification for any or all, but with the clear preference for groups requesting prequalification for all. Replies were required by end January '85.

By this time, it was common knowledge that the Japanese Government were prepared to provide a soft loan for at least $150M.

Not unnaturally many groups applied for all sections but in the event only 4 were prequalified on technical grounds and 3 of these included at least one Japanese and one Italian company, the latter inclusion clearly indicating a strong interest from that country.

The CBE consortium included US, German, as well as Turco-British involvement. It could easily have included Italian, Spanish, French etc, or even Japanese. The composition represented the contractors' own assessment of their best chance of success, both on cost and credit.

It was clear to me, however, as it must have been to others, that credit for the road sections would have to come from "export credit" facilities, largely non-convertible into Turkish Lira. This meant that, contrary to previous concepts, the project should deliberately emphasise imported items rather than locally made products, i.e. imported steel beams for small motorway bridges, rather than reinforced concrete, and also lavish provision of modern earthmoving and roadmaking plant at the expense of local labour. Turkey has so little plant of this type. The Turks were aware of this aspect. I indicated these possibilities to CBE and when the definitive tender documents were prepared and issued in February to the prequalified groups I introduced a clause which permitted such changes to be made at the contractor's desire.

The tender documents, although still dividing the project into 4 sections, made it absolutely clear that the project would be let as one single contract and if necessary would be so negotiated.

It was also stated that as part of the evaluation, the various tender sums, including repayment terms, would be reduced to a present value.

Additionally, offers of credit had to be backed by genuine statements from Government or other financial institutions.

Tenders

The Tenders were returned on April 16th and there were only two serious offers, summarised below.

	(Italian/Japanese/ Turkish)	(British/German) US/Turkish)
	$ Millions	$ Millions
Section 1	93	114
Section 2	270	312
Section 3	76	101
Section 4	112	149
Total	551	676

Thus there is a large difference in price but of course credit terms could influence the award. The Italian/Japanese contractor is lower on all sections.

The credit offers from the Japanese/Italian group were straightforward and from best memory were as follows:

Soft Loans

$200M 5% @ 25 yrs 7 yr grace - Japan
$30M 2½% @ 15 yrs " " " - Italy

Export Credit

$140M - standard terms from Italy - 12 yrs

Commercial Loans

$70M fixed interest from Japanese banks - 10% - 7 yrs
£110M Euroloan. To be arranged in London by Chase Manhattan.

The credit proposals from CBE group were less well defined but included a generous UK government straight grant of $12M coupled with $48M export credit, export credit from Germany - $40-50M, Ex Im bank credit of possible $255M from US, together with possible export credits from Brazil and Yugoslavia of $50M & $100M. Additionally a Euroloan of perhaps $300M was suggested for it was recognised that the export credit was only available for a proportion of the exports (only 65% in case of Ex Im - 85% elsewhere) and that in any case had to be related to export of real hardware or services, all of which may not have been possible from all the sources.

Nevertheless in evlauating present values the maximum use was made of Export Credit.

There was some debate in Ankara about the discount rate to be applied, and I failed to persuade their Treasury and planning officials to use a different rate for Yen, $ and £.

With a single rate, the disparity between the two tenders moved from 1.23 to over 2.

However, on closer examination of part only of Section 2 (the section including the Bridge), the situation becomes less adverse. Certain figures, as presented, might be interpreted to indicate the cost of the bridge alone, notwithstanding that some of the tenderers, including the Italian/Japanese, clearly stated that they should not be isolated from the rest. It is well understood within the industry that contractors often move overhead allowances and balancing items to different sections of the project for various reasons, including cash flow. Thus costs may be moved from late to early start items, in this case from bridge approach roads which have a late start to bridge supply items, etc.

If one were to ignore this and hence produce a hypothetical situation, at first sight, for the Bridge only such figures are:

CBE	Italian/Japanese		Others	
111.1	122.7	less % reduction forming integral part of offer	114.4	119
-	1.4			
111.1	121.3			

Thus it might be thought the UK bid for the bridge alone was lower. All this is theoretical and in any case as a minimum the bridge needs some 15 km of road to be effective. With this added the basic figures move to 194-180 in favour of the Japs.

Unfortunately, when it came to a detailed evaluation, it transpired that the CBE offer was incomplete and one item was only provisional. Strict adherence to the rules would have meant rejection. The Japanese offer had an obvious heavy balancing item for the whole of section 2, and which they had been at pains to point out in their submission.

On the best possible bias to UK therefore the comparative figures are:

CBE	Italian/Japanese
112.5-113	111-112

A slight lead to the Japs, but really nothing to choose between them. Only if one were to deduct the UK grant is there a lead.

However, when such credit terms (including increased UK grant) were included and the two evaluated with a 5% difference in discount rate against the Yen (something which I insisted upon, but which the Turks would never accept), the CBE offer became some 16% higher.

The idea of just separating the Bridge structure is of course quite unreal as it is to say the Japanese cannot build the bridge. (They have completed, or have under construction, many suspension bridges in Japan.) Whilst one would have some preference to UK experience, I simply could not press this as far as CBE wanted and will no doubt continue to say I should have.

It was clear that the best way to achieve UK contractor involvement was by joining the Japs.

To my mind vital time was lost while CBE/Trafalgar House pontificated about what I should tell the Turks to do while at the same time trying to pull political strings in Ankara.

The Japanese loan is good for Turkey, so is the Italian support and I fail to see how anyone in Ankara could do anything else than accept it. To remove the bridge from the Japs would obviously undermine the credit offer.

What I did, however, was to bring the Japanese and UK representatives together and point out to the Turks that there were real possibilities of reducing the Euroloan content if more export credit worthy items were to be incorporated in the whole project, indicating in general terms how this might be achieved by certain design changes, particularly on the road structures. This was accepted and the Italian/Japanese team asked to try to do so.

Thus, although the prestige value of the project may have gone elsewhere, all need not be lost to UK manufacturing, if the export credit remains* and prices are reasonable.

* possibly without

Certainly the Japanese and Turks are unhappy at recent Ministerial comment and publicity, but they may well overcome that resentment if the commercial terms are right.

On the other hand, the Italian steel fabricators are eager to pick up more and there is nothing to indicate that they have reached their ceiling on export credit to Turkey.

Of note is that the Italian member of the group IMPREGILO includes as its leader IMPRESIT. This company is a branch of the FIAT organisation who not only make trucks etc but through their associate company Allis-Fiat roadmaking equipment.

WCB/MB
9.5.85

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File KB

(original attachment to CDP)

10 DOWNING STREET

From the Private Secretary

9 May 1985

BOSPHORUS BRIDGE

I enclose a copy of a note on the Bosphorus Bridge contract prepared by Dr. Brown of Freeman Fox. It has been given in confidence to Michael Alison by Neil Thorne: and we should not admit to having it, at least until we get it from some other source. I found it a valuable account and propose to show it to the Prime Minister over the weekend. Some of the information in it might be useful in working up a reply to Mr. Nakasone.

I am copying this letter and enclosure to Colin Budd (Foreign and Commonwealth Office).

CHARLES POWELL

John Mogg, Esq.,
Department of Trade and Industry.

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Secretary of State for Trade and Industry

PS/

20 May 1985

NBPM
CDP
20/5.

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

Dear Charles,

BOSPHORUS BRIDGE

Thank you for your letter of 9 May enclosing a confidential note by Freeman Fox on the background to the bidding for the Second Bosphorus Bridge. I have drawn this to the attention of my Secretary of State.

2 The Freeman Fox analysis gives an interesting insight into the cut and thrust of competition for an international project of this magnitude. While some of the opinions expressed, particularly on Cleveland's tactics might be open to question, the note confirms the main conclusions that we had drawn from the case, namely:

(i) the Japanese were prepared to put up a very large subsidy, (four times the amount of ours) to buy the business;

(ii) the Japanese did not, however, break the international rules on concessional finance;

(iii) given the Turks' desire to include connecting motorways in the project, the Japanese could have virtually won the contract on price alone.

(iv) The reference to the price evaluation is also of interest: it confirms that the UK were certainly fully competitive, and if there is a marginal difference in the Freeman account this could well be simply a consequence of the different assumptions used. I should add that key officials have discussed the situation informally

with the London IHI (the leading Japanese company) representative, who has not contested the assertion that Cleveland were the most competitive on the bridge itself. But this further illustrates the problems of getting to the heart of such complex cases.

3 We have taken Freeman Fox's views into account in preparing a reply for Mr Nakasone, particularly their judgement that there was still an opportunity for the UK to secure some of the work.

4 I am copying this letter to Colin Budd (FCO).

Yours sincerely,

Maureen Dodsworth.

MAUREEN DODSWORTH
Private Secretary

TRADE: Non-Tariff Barriers:
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