

CONFIDENTIAL



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Treasury Chambers, Parliament Street, SW1P 3AG

Di Hurd

The Rt Hon Douglas Hurd CBE MP
 Secretary of State for Foreign Affairs
 Foreign & Commonwealth Office
 King Charles Street
 London
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17/1

17 January 1990

Dear Secretary of State,

KNOW-HOW FUND FOR EASTERN EUROPE

Thank you for your minute of 12 January.

2. I accept your view that we are likely to face fresh expectations of bilateral support as further East European countries embark on reforms. In the circumstances, I welcome your suggestion that we should extend the application of the Know-How Fund to East European countries other than Poland and Hungary, once they are firmly committed to political and economic reform, and that we should discuss in the Survey a global sum for this purpose, but without specifying, except for internal purposes, allocations for individual countries other than those announced for Poland and Hungary.

3. I note your suggestion for a Fund of £150 million, implying an increase of £75 million in the sum presently agreed. I shall be ready to discuss a proposal from you in the Survey when, as my officials have indicated, I shall want to look at the scope for offsetting savings within the Diplomatic and Aid programmes towards the cost of the various initiatives which you propose, or in which we are already involved, in Eastern Europe, and other initiatives including proposed programme aid for Zambia which we held over from the last Survey.

4. We shall need to ensure that the countries concerned are committed to reform before they receive assistance from the Fund. I should be grateful therefore if you would consult the Treasury before the first commitment is made to any country other than Poland or Hungary. I should be content for the scheme to be used, as you suggest, to provide occasional modest technical assistance to the USSR, but agree with you that economic assistance to the USSR is a major question for separate consideration as and when the time comes.

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 18.01.91 10:00 AM

5. I welcome your suggestion that our discussion in the Survey should be informed by a fresh strategic look at the various initiatives for Eastern Europe. I shall be happy for my officials to collaborate with yours in preparing this.

6. For present purposes, I should be content for you to make the announcement proposed in paragraph 9 of your minute. I must accept your judgement that it would be useful to do this at the Foreign Affairs Committee on 20 January or before. I should be grateful if your officials would discuss with mine the precise terms of an announcement in the House or in the Committee. I hope you will bear in mind in any meeting or debate on Eastern Europe the importance of taking full credit for the most substantial support, bilateral and multilateral, including debt relief which we are already providing or committed to provide.

7. I am grateful to know your thinking on the shape of an extended Know-How Fund. I welcome your suggestion to drop the 5-year time limit on disbursements from the Fund. I am concerned that Fund resources should be carefully targeted on promoting the development of a market economy and political reform in the most cost effective way. I agree that the removal of the 5-year limit should help your officials to pursue this aim.

8. I should be content for the Fund to be used, as you suggest, for modest expenditure on related equipment and supplies, e.g. for the health sector in Romania, and to encourage British private investment in Eastern Europe provided that, on the latter, expenditure from the Fund is limited to contributions of up to 50 per cent towards the cost of feasibility studies of investments such as joint ventures and privatisation schemes, once the company has made the initial running. The resulting investments per se could be the subject of lending by the EIB or EBRD. We must recognise, however, that promoting such investment may increase pressure on the ECGD to renew or increase its cover for investment in Eastern Europe and for exports. Both activities seem likely to remain risky for some time.

9. You propose Estimates provision for 1990-91 of £15 million for an extended Fund, implying an extra £10 million from the Reserve to add to the £5 million agreed for the initial fund for Poland. I agree to your proposal.

10. Finally, you seek my agreement in principle to additional running costs provision for the administration of the Fund and for overseas representation. I am by no means convinced that an additional running cost requirement of £0.5 million is needed, but am content that our officials should examine the detailed case.

11. I am copying this letter to the Prime Minister, Geoffrey Howe, John Major, Nicholas Ridley, Tom King, Chris Patten and Sir Robin Butler.

Yours sincerely
 Aileen Campbell

pp NORMAN LAMONT

Approved by the Chief Secretary and signed in his absence

[This may help Lady Cox]



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The Rt Hon Norman Lamont MP
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My ref

Your ref

30 January 1990

CD 307i

Norman

KNOW-HOW FUND FOR EASTERN EUROPE

clap

Douglas Hurd wrote to you on 12 January about this.

You will be aware that there are very serious environmental problems in Eastern Europe. It seems likely that Know-How Fund expenditure there will prove very good value in helping to clean up our common European supplies of air and water. How much it would be sensible for us to spend, and over what time scale, will only begin to come clear when the first UK members of the G24 fact-finding mission return from Poland and Hungary at the end of the month. Initial soundings suggest that problems in the other Eastern Europe states may be at least as severe.

Studies in pollution measurement and control are likely to offer very good value for money and to deliver political credit. Implementing major reductions in pollution will be expensive by any standard. Good measurement will be essential if we and the East Europeans are to get results from that investment. We should press G24 to give priority to measurement work. However our UK experience suggests that setting up adequate measurements could take us into the £ (single) millions of spending in each country.

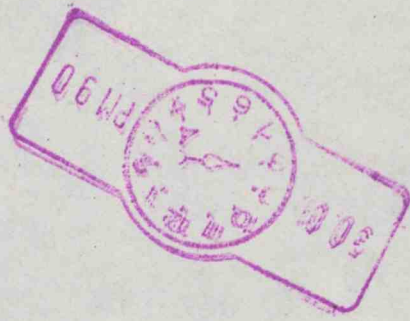
I therefore welcome Douglas Hurd's minute and also your reply of 17 January; and I would also point out that in my field it is too early to be excluding what might turn out to be very good value for money arguments for spending rather more at the margin, even in 1990/91.

I am copying this to the Prime Minister, Geoffrey Howe, Douglas Hurd, John Major, Nicholas Ridley, Tom King and to Sir Robin Butler.

Chris Patten

CHRIS PATTEN

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the department for Enterprise

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Sean Douglas

EASTERN EUROPE: OFFICIAL SUPPORT FOR EXPORT CREDIT AND INVESTMENT

Asap

I have seen your minute of 12 January to Norman Lamont about the Know-How Fund. I welcome the proposal in your paragraph 10 that the enlarged fund should be available to cover expenditure on encouragement to British private investment in Eastern Europe. I have the funding of feasibility studies particularly in mind. In this letter I also wish to make further proposals designed to encourage such investment through the use of ECGD Investment Insurance cover.

In my letter of 13 December I said I had asked for an urgent review of the position on ECGD cover for Eastern Europe, particularly on Investment Insurance. My letter contained details of existing arrangements for export credit cover for Eastern Europe. I see no immediate need to consider new arrangements. However, I think we need to do something quickly on Investment Insurance particularly for Poland and Hungary.

I think it is clear that Poland's current need is for investment rather than new credit. John Redwood has very recently visited Hungary and he believes that there are important opportunities there for British firms to invest. ECGD Investment Insurance cover could have a useful role to play both in Poland and Hungary in making this possible.





the department for Enterprise

Investment Insurance

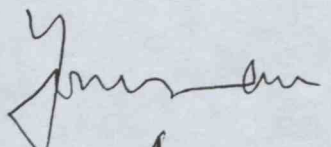
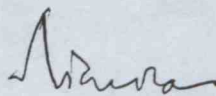
ECGD have reviewed the cover available for new investments in Poland and Hungary and are currently clearing their proposals at official level. While it will I hope be possible to make firm arrangements for Hungary to enable ECGD to offer its full range of investment insurance within a prudent review point, I understand that the Polish authorities are considering various changes to their investment insurance and exchange control regulations. Until these have formally entered into Polish legislation, the form of ECGD support for the transfer risk that would be appropriate cannot be determined because the changes will apparently affect the amount of any profits/dividends which may be transferred. Nevertheless, I am hopeful that ways can be found for giving a sufficient measure of support to meet UK investors' legitimate needs.

Export Credit

I do not at present see a need for exceptional arrangements on export credit for any of the East European markets. Poland clearly needs aid and investment rather than new export credit which would merely add to the present insupportable debt burden. Those of our overseas competitors who have resumed export credit support for Poland probably do not seriously expect to be paid, and may regard their support as akin to aid. We have participated very actively in the international aid effort for Poland, and I think we should continue to give our support to Poland and any other comparable East European market in this form until such time as the economic situation makes practicable the resumption of ECGD support.

Any changes in the present arrangements for official support for export credit for Eastern Europe would be considered in the normal way in the Export Guarantees Committee with reference as appropriate to Ministers. They should ensure that full consideration is given by Departments to any proposals for change.

I am copying this letter to the Prime Minister, Geoffrey Howe, John Major, Tom King, Chris Patten, John Wakeham, Norman Lamont and to Sir Robin Butler.



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