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Foreign and Commonwealth Office

London SW1A 2AH

13 July 1990

Dear Charles,

Ankara Metro Project

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/ Thank you for your letter of 10 July. I enclose a note by the ODA with the background to this project, for which Hawker Siddeley are seeking ATP support.

Appraisal by the ODA suggests that this project makes little economic or financial sense. It offers an economic rate of return of between 4 and 6 per cent and would require an operating subsidy estimated at between \$20 million - \$40 million a year over the first 15 years of operation. Last year Ankara's total municipal budget was \$150 million.

/ In normal circumstances any proposition of this kind would almost certainly be ruled out for ATP support. However Mrs Chalker and Lord Trefgarne have agreed that, in view of the political importance to the Canadian Government of the French/Canadian angle, we should talk further to the Turkish Government about their general attitude to the project and to the scale of the operating subsidy necessary to implement it. I enclose a copy of the telelgram that has been sent today to Ankara.

Assuming that the Turks remain fully committed to the project (and its costs) both ODA and DTI would like to see the project opened up for re-appraisal involving the Turkish and Canadian Governments as well as ourselves. We have worked closely with the Canadians up to now and would certainly expect to continue to do so in reaching a final view on aid for this project.

I am copying this letter to Martin Stanley (DTI).

Yours ever,
Richard
(R H T Gozney)
Private Secretary

C D Powell Esq
10 Downing Street

TURKEY: ANKARA METRO PROJECT

Essential Facts

1. The project is to build and operate 14 kilometres of Metro from the centre of Ankara out to a new township in the North West. The main contractor is Canadian, Lavalin/UTDC, with UK, sub-contractors. The total project cost is estimated at £375.6m, of which £53.6m is UK content. Support of 35% of the UK content (i.e £18.76m) has been sought from the Aid and Trade Provision by Hawker Siddeley.

2. A 1987 appraisal by Canadian consultants gave an economic rate of return (ERR) of 9%. (We would normally expect ERR of at least 10% for acceptable projects in Turkey). We therefore arranged for our own economic/financial appraisal study to be carried about in Turkey by an ODA appraisal team and for consultants to carry out a desk study of the project structuring costs, geology and contractual arrangements. The economic appraisal resulted in an ERR in the range of 4-6%. The rate has declined because:

- i) the bids for the capital works are 60% higher than the consultants estimate;
- ii) operating costs are also forecast to be considerably higher;
- iii) the consultants' treatment of savings on bus investments was unrealistic and favourable to the Metro;
- v) there was no provision for civil works in the figures in the 1987 appraisal;
- iv) the consultants' estimate of patronage, which depends on completion of a satellite town, is optimistic in the early years by comparison with experience elsewhere.

3. A commercial consideration is that Hawker Siddeley hope to be associated with Lavalin on two potential Metro projects in Bangkok (£150m) and Toronto, both considerably larger in financial terms than Ankara. Hawker Siddeley, Lavalin

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and the Canadian High Commissioner have underlined that failure to obtain AT support in this case will jeopardise these projects and the prospects of any future co-operation between the two firms. This has been taken into consideration within ODA, but given the fundamentally uneconomic basis of the project the view is that this project should not be supported. Mrs Chalker has written to Lord Trefgarne who has asked that no final Whitehall decision be communicated to Hawker Siddeley or the Canadian Government until he has had the opportunity to respond on return from overseas in a week or so.

Canadian Government's Position

4. The Canadian High Commissioner has underlined the commitment to the project of his Government, the Ontario Provisional Government and the Export Development Corporation. EDC financing will take the form of a guarantee on non-concessional loans to the project company and a concessional interest-free loan to the Turkish Government for a total financing package representing 100% of the value of Canadian goods and services. But at present this does not count as aid money although, if the financial proposals are accepted, it can in future be so designated. The Canadian Government has not conducted any developmental appraisal of the Metro, and would not do so until after the project has started.

5. Our High Commission in Ottawa has reported that there is now rather more domestic political sensitivity about the project as the Federal Government are actively engaged in providing support for Quebec-based industry (following a particular failure) as part of their campaign to reassure the Province. But this consideration apart, there are no UK/Canada bilateral dimensions which the High Commission regard as having a major bearing on the decision on the ATP application.

West and North Africa and Mediterranean Department.
Overseas Development Administration

3rd July 1990

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DEFINITION

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FOR AMBASSADOR FROM IRETON

YOUR MODEV U/N OF 1JUNE ANKARA METRO

1. THE CANADIAN EXPORT DEVELOPMENT CORPORATION HAS ACCEPTED A SECURITY STRUCTURE FOR THIS PROJECT WHICH PROVIDES ULTIMATE TURKISH SOVEREIGN RISK. WE ARE TOLD THE STRUCTURE WAS DETERMINED IN CONJUNCTION WITH SENIOR OFFICIALS OF THE TURKISH TREASURY, WHO HAVE AGREED TO PROVIDE CERTAIN REPUBLIC OF TURKEY UNDERTAKINGS WHICH RECOGNISE THEIR ULTIMATE RESPONSIBILITY FOR REPAYMENT OF THE LOANS. EDC CONSIDERS THAT THE INVOLVEMENT OF TURKISH OFFICIALS IN DISCUSSIONS CONCERNING SECURITY AND LOAN PRICING, AS WELL AS THE NATURE OF THE SECURITY THEY WILL PROVIDE, ARE EVIDENCE OF TURKEY'S COMMITMENT TO THE PROJECT.
2. AS YOU KNOW, CANADA DOES NOT HAVE AN AID PROGRAMME FOR TURKEY, HENCE THE PROPOSED CANADIAN CONCESSIONAL FINANCING FOR THIS PROJECT IS IN THE FORM OF A SOFT LOAN WITH A 35 PERCENT CONCESSIONAL LEVEL FROM THE CANADIAN GOVERNMENT. THE LOAN IS MADE BY EDC ON BEHALF OF THE GOVERNMENT UNDER EDC'S CANADA ACCOUNT. THE FINANCING IS SUBJECT TO FINAL APPROVAL FROM THE CANADIAN GOVERNMENT WHICH EDC EXPECT TO SEEK IN THE NEXT MONTH OR SO, MEANWHILE AN APPROVAL IN PRINCIPLE HAS BEEN GIVEN. ONCE THE FINANCING HAS BEEN APPROVED, THE CANADIAN GOVERNMENT WILL DETERMINE WHETHER OR NOT IT SHOULD BE REPORTED INTERNATIONALLY AS AID. (THIS COMPARES WITH ATP SUPPORT WHICH WOULD INVOLVE AND 35 PERCENT GRANT FROM AID FUNDS).
3. WE NOTED FROM YOUR TUR THAT THE TURKISH GOVERNMENT APPEARS TO HAVE COOLED SOMEWHAT ON THE PROJECT.
4. THE FEASIBILITY STUDY BY CANADIAN CONSULTANTS IN 1987 INDICATED AN ECONOMIC RATE OF RETURN OF 9 PERCENT. WE THEREFORE MOUNTED OUR OWN APPRAISALS WHICH INDICATED AN ERR OF 4-6 PERCENT. (WE REGARD 10 PERCENT THE MINIMUM IF A PROJECT OF THIS TYPE IS TO PROVE VIABLE). THE RATE DECLINED BECAUSE:
 - I) THE BIDS FOR THE CAPITAL WORKS ARE 60 PERCENT HIGHER THAN THE CONSULTANTS ESTIMATE
 - II) OPERATING COSTS ARE ALSO FORECAST TO BE CONSIDERABLY HIGHER
 - III) THE CONSULTANTS' TREATMENT OF SAVINGS ON BUS INVESTMENTS WAS UNREALISTIC AND FAVOURBLE TO THE METRO
 - IV) THERE WAS NO PROVISION FOR CIVIL WORKS IN THE FIGURES IN THE 1987 APPRAISAL
 - V) THE CONSULTANTS' ESTIMATE OF PATRONAGE, WHICH DEPENDS ON COMPLETION OF A SATELLITE TOWN, IS OPTIMISTIC IN THE EARLY YEARS BY COMPARISON WITH EXPERIENCE ELSEWHERE.THE ECONOMIC APPRAISAL ALSO ESTIMATED THE SHORTFALL IN REVENUE IN THE FIRST 15 YEARS OF OPERATION COULD AMOUNT TO DOLLARS 20M-40M A YEAR, WHEREAS ANKARA MUNICIPALITY'S BUDGET IN TOTAL IN 1989 WAS DOLLARS 150M.

5. MINISTERS HAVE CONSIDERED THE PDS STG 18.76M ATP APPLICATION BY HAWKER SIDDELEY AND ARE CONCERNED AT THE ESTIMATED LOW ECONOMIC

MRS Chalker 927
MR Lancaster 9th
MR Ainscow 944
MR Hudson 847
MR Ireton 937
MR Raleigh 514
MR Wootton 837

Lord Tregearne DTI
MR Rogers Peplink DTI

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5. MINISTERS HAVE CONSIDERED THE PDS STG 18.76M ATP APPLICATION BY HAWKER SIDDELEY AND ARE CONCERNED AT THE ESTIMATED LOW ECONOMIC RATE OF RETURN AND THE HEAVY OPERATING SUBSIDY THAT WOULD BE REQUIRED. IN NORMAL CIRCUMSTANCES MINISTERS WOULD NOT APPROVE THIS ATP APPLICATION. BUT IN VIEW OF THE POLITICAL IMPORTANCE TO THE CANADIAN GOVERNMENT OF THE FRENCH CANADIAN ANGLE, MINISTERS HAVE AGREED WE SHOULD CONSIDER THE MATTER FURTHER. AS A FIRST STEP WE SHOULD FIND OUT MORE ABOUT THE TURKISH GOVERNMENT'S ATTITUDE IN THE LIGHT OF CURRENT APPRAISAL STUDIES, AND WHETHER THEY STILL WISH TO GO AHEAD WITH THE PROJECT. SECONDLY THEY WISH TO ESTABLISH WHETHER THE TURKISH GOVERNMENT AND THE ANKARA MUNICIPALITY HAVE FOCUSED ON THE QUESTION OF THE OPERATING SUBSIDY AND HOW IT WOULD BE FUNDED.

6. IN THE LIGHT OF THIS ONE WAY FORWARD WOULD BE TO SUGGEST THAT THE THREE GOVERNMENTS JOINTLY RE-APPRAISE THE PROJECT WITH A VIEW TO FORMING A COMMON BASIS FOR DISCUSSION. WE ACCORDINGLY WISH YOU, AS A MATTER OF URGENCY, TO FOLLOW UP THE CANADIAN DISCUSSIONS WITH THE TURKISH TREASURY AT MINISTERIAL LEVEL.

7. WE SUGGEST YOU DISCUSS THIS WITH YOUR CANADIAN COLLEAGUE AND INVITE HIM TO JOIN YOU WHEN YOU SEE THE APPROPRIATE TURKISH MINISTER. WE ARE INFORMING THE CANADIAN HIGH COMMISSION HERE TO WHOM EARLIER WE PASSED COPIES OF OUR APPRAISALS AND WITH WHOM WE HAVE HAD FRANK EXCHANGES. (YOU SHOULD KNOW, HOWEVER, THAT NEITHER THE CANADIAN GOVERNMENT NOR LAVALIN HAVE ATTEMPTED TO REFUTE OUR ECONOMIC APPRAISAL IN ANY SERIOUS MANNER).

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THE CANADIAN GOVERNMENT HAS CONSIDERED THE PDS STG 18.76M ATP APPLICATION BY HAWKER SIDDELEY AND ARE CONCERNED AT THE ESTIMATED LOW ECONOMIC RATE OF RETURN AND THE HEAVY OPERATING SUBSIDY THAT WOULD BE REQUIRED. IN NORMAL CIRCUMSTANCES MINISTERS WOULD NOT APPROVE THIS ATP APPLICATION. BUT IN VIEW OF THE POLITICAL IMPORTANCE TO THE CANADIAN GOVERNMENT OF THE FRENCH CANADIAN ANGLE, MINISTERS HAVE AGREED WE SHOULD CONSIDER THE MATTER FURTHER. AS A FIRST STEP WE SHOULD FIND OUT MORE ABOUT THE TURKISH GOVERNMENT'S ATTITUDE IN THE LIGHT OF CURRENT APPRAISAL STUDIES, AND WHETHER THEY STILL WISH TO GO AHEAD WITH THE PROJECT. SECONDLY THEY WISH TO ESTABLISH WHETHER THE TURKISH GOVERNMENT AND THE ANKARA MUNICIPALITY HAVE FOCUSED ON THE QUESTION OF THE OPERATING SUBSIDY AND HOW IT WOULD BE FUNDED.

13 OCT 1980

TURKEY: Relations Pt 2

