Foreign and Commonwealth Office

London SW1A 2AH

17 September 1985

J Gill Esq, CB
Export Credits Guarantee Department
POB 272 Aldermanbury House
LONDON EC2P 2EL

Dear Gill,

RELATIONS WITH NIGERIA

The Foreign and Commonwealth Secretary paid a rapid visit to Nigeria on 10 and 11 September, with the purpose of making contact with President Babangida's new Government and of getting our relations back on to a more normal footing. As background I enclose a copy of the Post's general reporting telegram (Lagos telegram No 925 of 12 September).

During his visit, which coincided with the announcement of the new Nigerian Council of Ministers, Sir Geoffrey Howe was able to have a short, rather public, meeting with President Babangida. At the President's request however, an entirely private and undisclosed meeting was held with Major-General Yar'Adua, a senior military figure, a Northern Nigerian, and still a significant influence within Nigeria.

At the meeting General Yar'Adua was clearly briefed by President Babangida to emphasise the President's wish to restore the warmth of Anglo-Nigerian relations, whatever hestitations had been expressed during the programme of talks.

It became clear that the prime purpose of the meeting was to address the economic situation in Nigeria, about which (understandably) President Babangida was very worried. He had no illusions about the difficult choices which faced him. He was particularly concerned about the enormous weight of ECGD short and medium term debt, mounting to some £700 million. President Babangida wanted to put forward a personal suggestion which had not been discussed with any other Nigerian Ministers or officials. He very much hoped that we would be prepared to consider a formula which would effectively enable the ECGD debt to be repaid through supplies of oil from Nigeria. The formula might be on the lines that the Nigerian Government would supply oil to the oil companies, who would then open letters of credit using oil as collateral: the Nigerian Government would then allocate the finance made available to the repayment of ECGD debts. President Babangida had not worked out a detailed scheme and there might be various ways in which this could be done. President Babangida hoped that we would consider it and then let him have a response on the same entirely unofficial channel without involving any other Nigerian Ministers of officials.

/Sir Geoffrey

Sir Geoffrey Howe said that we would obviously need to consider the proposal and he could not give an immediate response. Instinctively, he had to point out that ECGD basically preferred money, and that there could be no question of ECGD taking any risks on oil prices. He would obviously need to consult experts back home before giving a response. But we would come back to him when we had had time to consider the proposal.

There are a number of large question marks over this approach. Given the appointment of a new Finance Minister, Dr Kalu i Kalu, and the prospect that Nigeria may now be prepared to move towards discussions with the IMF, which if successful would help to unlock new credit arrangements, it is not clear why President Babangida is using this back channel. We know, however, that there is widespread opposition in Nigeria, partly because of the many vested interests involved, to the IMF's requirement of a substantial de-valuation of the Naira; the presumption must also be that the President fears that he might not be able to get his colleagues to agree to this proposal relating to Nigerian oil. Sir Geoffrey Howe recognised that we must look at the idea with considerable caution. It is clear that President Babangida attaches importance to it and if it helps him it could provide a significant boost to Nigerian stability and to our future relations. How far would it help ECGD? What are the practical implications? How far would it affect relationships within the Paris Club? How far would it cut across Nigerian relations with the IMF? What would the mechanics be? Who would handle the off-take of Nigerian oil? These are only a few of the questions which come to my mind. The Nigerians will be aware, of course, of the Tornado contract with Saudi Arabia and of our willingness, in particular circumstances, to do a deal involving oil.

Sir Geoffrey Howe wishes to give as early a response to President Babangida as possible. Given the secrecy of the contact with Major-General Yar'Adua, and the possible implications for President Babangida if information about the suggestion, or our reaction to it, were to leak out, he has instructed that the circle of those knowing about the proposal should be kept to an absolute minimum. This accounts, therefore, for the classification which I have given this letter.

Since the proposal relates to the payment of ECGD debt, I am addressing this letter to you and am copying it to those who seem likely to have a direct interest. I should be grateful for your preliminary reactions as soon as possible. We can then consider further co-ordination in Whitehall and, as necessary, the preparation of a more detailed reply to President Babangida.

Yours ever,

Ewen Fergusson

E A J Fergusson

/cc:

SECRET

Foreign and Commonwealth Office

London SW1A 2AH

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23 September 1985

Dear Charles,

Nigerian Debts: Oil

I understand that in a letter to the Prime Minister about the Tornado deal the Secretary of State for Energy has referred to a Nigerian proposal, put privately to Sir Geoffrey Howe in Lagos, that outstanding ECGD debts might be settled by the Nigerians in oil.

You will want to be aware of the details: I therefore enclose as background a copy of Ewen Fergusson's letter of 17 September to Gill in ECGD. But I should stress that this idea of President Babangida's is being examined on a purely hypothetical and exploratory basis. We are in no way committed to it.

I am copying this letter to Geoff Dart (Department of Energy).

Yours ever,

Colin Budd

(C R Budd)
Private Secretary

C D Powell Esq
10 Downing Street

SECRET

PRIME MINISTER

I was surprised that I was not consulted about the implications for the oil market of the proposed Saudi purchase of aircraft, which I heard about for the first time only 10 days ago. I only learned about the oil aspects of the deal from the weekend press.

The quantities of oil which will be needed to pay for this deal could have a major impact on the oil market, however carefully handled. The rapid fall of around $2 in the market in July 1984 simply on the rumours of a large Saudi barter deal involving Rolls Royce and Boeing illustrate this.

At the moment the oil market is reasonably firm. Other things being equal there are a number of factors that point to it remaining so in the period immediately ahead, eg stocks are very low, the intensification of the Iraqi attacks on Kharg and hopes for a cold winter. But this fragile balance could very easily be upset and the market could well be very weak indeed in the 2nd and 3rd quarters of 1986.

I understand that MoD and British Aerospace have been talking to the Saudis in terms

BP and Shell have made it quite clear that there can be no question of their absorbing anything like this quantity in their own systems,

To go above this figure would run the risk of seriously undermining the market. The companies are no keener to push down the oil price through mishandling the flow of oil than I imagine the Exchequer is. Every $2 fall would cost the Exchequer about £1bn in 1985/6. At the limit our loss in oil earnings could exceed the value of the order. Shaikh Yamani shared this concern, when the new Chairman of Shell saw him in Saudi Arabia over the weekend. I am not at all clear about the imperatives for proposing such a high level of sales, other than internal Saudi considerations.

The fact that a representative of the new Nigerian President has recently raised, on a very private basis, with Sir Geoffrey Howe the possibility of a major deal involving payment in oil simply heightens my concerns.

The incident raises a major question about how such decisions as these are handled within the Government. Clearly the issues I have raised here would have been better raised at an earlier stage in the formulation of the deal. Can I take it that for the future, where deals such as this are contemplated, which have an energy policy aspect, I will be closely consulted at an early stage.

I am sending copies of this minute to the Chancellor, the Foreign Secretary, the Secretary of State for Defence and the Secretary of State for Trade and Industry.

SECRETARY OF STATE FOR ENERGY

25 September 1985