005/111

No

Prime Minister CDO
Agree to some further delay?

CHIEF SECRETARY TO THE TREASURY

FROM: CHIEF SECRETARY
DATE: 3 April 1985

CDO 13/4

Yes - no option

PRIME MINISTER

**ECGD'S FINANCES**

At a meeting of EX on 13 February I was asked, in consultation with the Secretary of State for Trade and Industry, to report to EA on ECGD's finances. The background was ECGD's serious financial position, in particular the cash deficit which on the most recent assumptions including gloomier prospects for Nigeria, will rise to almost £2 billion by 1989-90 imposing a heavy burden on the PSBR, reflecting the effects of the international debt problem on business taken in the past, and the wide margin by which on present projections the Department will fail to meet its financial targets set only last year. During the period up to 1989-90, ECGD's reserves should remain positive assuming that all the overseas governments which had to restructure their debts ultimately repay them with a reasonable rate of interest.

2 I had hoped to be able to make this report about now on the basis of ECGD's first full Business Plan. However, the Plan is not yet ready and ECGD are approaching the end of a wide ranging Management Review which has been looking at ways of making ECGD more business like within its present status as a Government Department. I understand the Review will report radical conclusions towards the end of this month. In these circumstances, a limited further postponement would allow the Plan to cover not only the improvements in ECGD's finances which might be sought within the present arrangements but also those flowing from any changes in organisation and objectives recommended in the Management Review and in the other work which ECGD have in hand on greater use of the private sector. This would provide a better basis for a full EA discussion of ECGD's finances and, subject to your views, Paul Channon and I believe that we should work on this basis towards an EA discussion very early in July.

3 Meanwhile, Paul and I have considered whether there are any immediate decisions which might be taken to improve the Department's financial health. We believe that business now being underwritten by the Department should be required to pay its way. Much of it does, although there are a few loss making facilities which are effectively being cross-subsidised. We are in touch about the extent to which this is tolerable or whether these facilities should be closed down and about the extent to which ECGD's premium rates should be increased to bring the Department closer to the achievement of its financial target. I will report the outcome of our discussions in due course and any disagreements can be exposed in the course of the Review by EA.

4 I am copying this minute to members of EA and EX and to Sir Robert Armstrong.

PR

**PETER REES**

File DA

10 DOWNING STREET

*From the Private Secretary* 15 April 1985

Dear Richard,

**ECGD's Finances**

The Prime Minister has seen the Chief Secretary's minute of 3 April about the report which is in preparation on ECGD's finances. The Prime Minister agrees that it makes sense to await the conclusion of the Management Review before submitting the report. She is content, therefore, with a target of discussion by EA in early July but would not wish it to slip beyond this.

I am copying this letter to Private Secretaries to members of EA and EX and to Richard Hatfield (Cabinet Office).

Yours sincerely

Charles Powell

(Charles Powell)

Richard Broadbent,
HM Treasury.

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CC NO

DEPARTMENT OF TRADE AND INDUSTRY
1-19 VICTORIA STREET
LONDON SW1H 0ET
Telephone (Direct dialling) 01-215) 5144
GTN 215)
(Switchboard) 215 7877

*From the Minister for Trade*

cc. ECON POL
Indebtedness
Part 5

1) DAT to see
2) NBPM
CDP 17/4

The Rt Hon Peter Rees QC MP
Chief Secretary to the Treasury
Parliament Street
LONDON
SW1

16 April 1985

Dear Peter.

In your minute of 3 April to the Prime Minister you outlined the steps you and I are taking to improve ECGD's financial position. At our meeting before this, we discussed the relevant merits of refinancing and rescheduling ECGD's overseas debts which are subject to Paris Club treatment.

My starting point is that we should seek to refinance wherever possible on the grounds that this achieves a real improvement in ECGD's cashflow and to the PSBR.

The underlying debt is unchanged, whether we refinance or reschedule, but I attach considerable importance to the presentational advantages of reducing ECGD's cash deficit as far as we can. And I would imagine that you would welcome the relief to the PSBR.

I mentioned at our meeting that there were two big ticket items where in my view refinancing ought to be considered. They are Nigeria and Poland. Nigeria cannot be a serious candidate at this stage in view of their failure to come to terms with IMF: indeed the future prospects are looking somewhat bleak and we have already agreed to revise our projections for ECGD's overall cashflow in recognition that there is now some risk of the Nigerians defaulting on their medium term liabilities in the not too distant future. But Poland <u>is</u> a good candidate and I should like it to be seriously considered since we shall very shortly be talking to the Poles about restructuring their 1982-84 debts. We have already agreed two refinancing loans for Poland and the structure of their 1982-84 debt is such that a further refinancing would be relatively easy to arrange. Moreover, the amount (£486m) is substantial.

I understand, however, that Treasury officials have reservations about a refinancing deal for Poland, mainly on the grounds that their economy is so weak that there must be serious doubts as to whether they will be able to service a new loan over the term already agreed in the Paris Club. I cannot, however, see that this is relevant to the issue of whether the Polish debt should be refinanced or rescheduled. I regard both techniques as of equal merit and I cannot see that the risk of a further rephasing of the terms of the loan should preclude the granting of that loan. If the situation is so bad that we believe the Poles will be unable to pay on the agreed dates then we ought not to be going along with the Paris Club agreement in its present terms.

If on the other hand there are problems in relation to the monetary effects of a refinancing loan then of course we should have to take account of them. but in the absence of any compelling Treasury counter arguments I should like to authorise ECGD to identify the most appropriate refinancing technique and to invite tenders from the bankers.

I should welcome an early reaction since there is not all that much time to do this ahead of the bilateral discussions due to take place at the end of April or early in May.

I am copying this letter to the Prime Minister, to members of EA and EX and to Sir Robert Armstrong.

Yours.

PAUL CHANNON

Paul

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Trade Jan 80

ECGD