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PRIME MINISTER

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INTERNATIONAL TIN AGREEMENT

I wrote to you on 11 October to say that there was a possibility that the International Tin Agreement (ITA) could be in difficulties in the near future. On 24 October I discusssed the situation with the Chancellor, the Foreign Secretary and the Governor of the Bank of England.

The present situation

2 On the 24 October the Executive Chairman of the International Tin Council (ITC) informed the London Metal Exchange that the Buffer Stock Manager (BSM) was no longer in a position to intervene in the market. The London Metal Exchange decided to suspend dealing in tin immediately and they will remain suspended at least until close of dealing on Monday, 28 October, and possibly longer.

3 The International Tin Council held a meeting on 25 October for Heads of Delegations to set out the position in preparation for a full meeting of the Council on 29 October.

4 At this meeting the Executive Chairman of the Council said that he would be seeking guidance from member countries as to the level at which they would like the price of tin to be maintained and he circulated a table showing the amount of money necessary to keep the agreement going at various

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price levels. In addition member countries would be asked to undertake that they would honour their share of any debts due by the Council which it could not meet from its existing resources as a result of a fall in the tin price. Subsequently, once confidence had been restored, member countries should get together to devise a package to reform the Agreement.

Member countries' liabilities

5 I am advised that the Council itself would be liable, to the extent of its existing resources, to meet the obligations of the Buffer Stock Manager (including obligations under contracts not contemplated by the 6th ITA but which the Council may have ratified). Whether individual Council members would be liable for that proportion of the BSM's debts which could not be met from the Council's existing resources is not clear. But lawyers from DTI and FCO advise that individual members would probably not be liable.

6 If these debts were to be met in full the precise amount which member countries would be required to cover cannot be quantified, because it would depend on the level to which the price of tin would fall in the absence of Tin Council support. Should the Agreement collapse and not be revived, it is likely that the price would fall to about £4-5,000 per tonne. In that case the total amount of additional money required to cover the ITC's obligations would be a once-off payment of between £3-400m, of which the UK share would be 4 per cent (i.e some £12-16m). In the light of the legal advice in paragraph 5 above, we might not be bound to pay this. But even if we did pay it, I believe that letting the Agreement collapse is almost certainly the cheapest option from the point of view of straight Exchequer cost.

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7 Should the Agreement be re-negotiated so that the price level were still maintained at, say, £7,000 per tonne (compared with the last supported level of about £8,500 per tonne) the total initial payment required to cover the debt which has been incurred and to keep the Agreement going would fall to around £250 million (of which the UK's share would be about £10m). But within this initial total would be ongoing costs which in subsequent years would continue to include at least £50m p.a. for interest payments (UK share about £2m p.a.) and perhaps £50m p.a. for working capital (UK share about £2m p.a.)

UK interests

8 We need to take three considerations into account:

(a) The Cornish tin industry (1,500 direct employees) would be unlikely to survive in the longer term if the price were to fall below about £7,000 per tonne.

(b) The London Metal Exchange (LME). The potential shortfall in the Buffer Stock Manager's existing resources in relation to members of the London Metal Exchange would be approaching £300m should the price of tin fall to about £4,000 per tonne. The Chairman of the Exchange believes that this might be sufficient to cause the Exchange as a whole to fall because a large number of brokers would be unable to meet their commitments. The Chairman of the London Metal Exchange considers that the ITC is now in default under its contracts to members of the Exchange,

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and that HMG, as a member of the Council, is a party to the default. He argues that there is therefore a moral obligation on HMG, which taken together with the importance of the LME to the British economy, requires us to take the lead in organizing a rescue operation. The Bank of England is uncertain whether in fact the Exchange as a whole would fall in the event of a collapse of the Agreement. [But it is impossible to be sure, although on balance it seems unlikely.]

The Bank would no longer say this – see my covering minute.

(c) It is possible that our relations with the producing states, chief of which are Malaysia, Indonesia and Thailand, would suffer, particularly in the case of Malaysia where the LME and the Bank of England who exercise an oversight of the LME might be seen, however unfairly, as the cause of the collapse. So far, however, since Thursday when trading was suspended, there does not seem to have been any attempt to lay the blame at our door.

9 However, set against these possible adverse implications is the essential point that if the Agreement collapsed or was satisfactorily re-negotiated UK consumers of 10,000 tonnes of tin per annum would benefit from the consequential price fall. If the price fell by £4,000 per tonne, the benefits to UK consumers would be about £40m p.a. If the Agreement were re-negotiated to set the price at a level somewhere between what would be the free market price and the last supported price of £8,500 per tonne, there would still be some benefit to consumers, though less than if we let the Agreement collapse.

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Options

10 We would appear to have three broad options:

(a) Agree to a package to enable trading to resume on condition that reforms to the Agreement would follow;

(b) Let the Agreement collapse.

(c) Be prepared to see the Agreement collapse, but, if international and domestic pressure is sufficiently strong, to undertake to examine, without commitment, any rescue package which may be put forward. But agree to give Government guarantees or additional resources only if the package includes fundamental reforms, including a more realistic market-related price and proper control over the BSM's operations.

11 In my view we should not be prepared to consider (a), not only because I am very reluctant to contemplate putting any more money into this agreement, but also because there could be no certainty that satisfactory reforms could be obtained.

12 However, the UK is to some extent bound by the position taken by other member countries (particularly consumer countries). It is possible that a two-thirds majority of both producer and consumer countries separately could vote to provide additional resources to the Agreement. In that case we would have two alternatives: either we could stay in the

ITC and necessarily comply with the new arrangements or we could leave the Agreement.

13 I believe that the consumers are unlikely to decide to commit additional funds to the Agreement without substantial reforms. But some, such as West Germany and Japan, appear ready to support a rescue package. Others, such as France and The Netherlands, appear less so. As yet, the producers have shown little inclination to make concessions by way of a price fall.

14 Although the European Community has competence in certain matters relating to the ITA, this competence does not extend to the injection of financial resources. Indeed, the Commission has implicitly accepted that some Member States might not be prepared to put in additional funds, even if others did.

Next Steps

15 I have already recommended that we do not pursue option (a) in paragraph 10 above.

16 I recommend that our preferred option should be (b): to let the Agreement collapse. Our representative at the ITC meeting on 29 October should not support moves to rescue the Agreement. I recognize that this course could have some adverse implications for the UK (paragraph 8 above) but I believe that the disadvantages of a rescue would outweigh the benefits.

17 However, I recognize that at the meeting on 29 October we may come under heavy pressure to accept a rescue package, particularly if our vote were required in order to make up a

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two-thirds majority among consumer countries for an Agreement. In that case, I recommend that we should hold to option (c) and say that we would require perhaps 2-3 days to examine the proposed package, before going back to the ITC. Following the 29 October meeting we would have to consider urgently, in the light of the details of the proposed package, whether we would be prepared to go along with it. It would need to involve substantial reforms to the Agreement, including a reduction in the price level to much nearer what it would be in a free market, and proper control over the BSM's operations. Otherwise, we should not agree to a rescue, since in its present form the Agreement is plainly absurd.

18 I am copying this minute to the Foreign Secretary, the Chancellor of the Exchequer, the Minister of Agriculture, Fisheries and Food, and the Governor of the Bank of England.

MRh

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28 October 1985

(Approved by the Secretary of State and signed in his absence)

Department of Trade and Industry

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Trade; Movements in Volume of Trade by Commodity; Jan '85

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10 DOWNING STREET

From the Private Secretary

29 October 1985

INTERNATIONAL TIN AGREEMENT

The Prime Minister has seen your Secretary of State's minute of 28 October and the Chancellor's of the same date. I also received a message from the Bank of England to say - in summary - that while the exposure of the London Metal Exchange was larger than they had earlier thought and that they could not now say that ~~the~~ collapse would be unlikely if the ITC failed to meet the Buffer Stock Manager's obligations, they were in general agreement with the line proposed by your Secretary of State.

As you know, the Prime Minister also agreed with your Secretary of State's recommendations. She did, however, comment that she is concerned about the proposition that as a member of the Tin Council the Government would be partly responsible for the Council's default, if that is the way the decision eventually goes.

I am copying this letter to Len Appleyard (Foreign and Commonwealth Office), Rachel Lomax (H.M. Treasury), Ivor Llewelyn (Ministry of Agriculture, Fisheries and Food) and to John Bartlett (Bank of England).

DAVID NORGROVE

Michael Gilbertson, Esq.,
Department of Trade and Industry.

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