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PS/ *Secretary of State for Trade and Industry*

5 February 1986

David Norgrove Esq
Private Secretary to the
Prime Minister
10 Downing Street
LONDON
SW1

Dear David,

TIN

As you will see from the attached record of a meeting my Secretary of State held on 4 February with Mr Jacques Lion, the LME Chairman, the progress now being made by the ITC towards negotiations to resolve the tin crisis may be too late to prevent the collapse of the LME. I also attach a note from the Bank of England which sets out the background.

2 I understand that the LME have now deferred decisions on the unfulfilled tin contracts until Friday, 7 February.

3 There is a significant possibility that, following the meeting of the International Tin Council today, the ITC will be in a position to put forward a serious counter proposal to the banks and brokers on finance for "Newco". If the ITC offer to provide finance of £80m to £100m, this could lead to genuine negotiations to settle the crisis.

4 If the LME were to decide, despite such a move by the ITC this week, that it could hold out no longer, it is doubtful whether any intervention by HMG could be justified. If the ITC do not make any serious move this week, then the Bank of England may wish to consider whether any scheme to support the LME should be put to Ministers for urgent consideration.

5 Once the LME decides that payment must be made on suspended tin contracts, there appears to be no way in which the Government could intervene to delay or prevent a collapse of a number of the LME brokers.

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6 I am sending a copy of this letter and attachments to Philip Wynn Owen (Treasury), Robert Culshaw (FCO) and John Bartlett (Bank of England).

Yours ever,

Michael

MICHAEL GILBERTSON
Private Secretary

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MEETING WITH THE LONDON METAL EXCHANGE : 4 FEBRUARY 1986

Present:

Secretary of State for Trade & Industry	
Mr Mountfield	DTI
Mr Lunn	DTI
Mr Lion	Chairman, LME
Mr Gee	Deputy Chairman, LME
Mr Brown	Chief Executive, LME

The Secretary of State said that the Government well understood the difficulties which the LME faced, and appreciated that some LME brokers were nearing exhaustion. However, there was now a real prospect of achieving credible negotiations between the ITC, the banks, and the brokers, and if a credible counter-offer from the ITC countries to the £200m share which the banks and brokers had said ITC countries should bear, then real progress could be made. The Government was concerned that, although any decision the LME should take must be its own decision, the process of negotiation might be prejudiced if the LME took the decision to require payment on suspended tin contracts. He asked Mr Lion what the latest situation was.

2 Mr Lion said the position was "bloody and bloody-minded". He said that for the first time since the crisis begun, there was a division of views on the LME which was irreconcilable. He said that although he had been able to keep the market closed for three months, in practical terms there had been no progress in reaching a viable solution to the crisis. The "shorts", essentially brokers acting on behalf of clients outside the LME who had taken a hedge on the market, were financing an enormous amount of unpaid differences, and were demanding part payments from those brokers who were creditors of the ITC ("longs"). In addition, members of the Board and Committee of the LME were being threatened with writs by the "shorts", though none had actually been issued as yet.

3 Mr Lion was also very concerned about the implications for him and his fellow directors vis-a-vis their various responsibilities under the Companies Acts. They would have to be able to show that they had acted in the best interest of the LME as a whole. Mr Gee therefore asked whether it would be possible for the Government to indemnify members of the Board and Committee of the LME, to enable them to maintain their policy of sitting tight.

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4 Mr Brown said that of the 52,000 tons of tin that the 26 ring dealing brokers had sold to the Buffer Stock Manager 47,000 tons had come from clients outside the LME, who had sold tin short and could now not get their money back. These clients included producers, fabricators, and stockists. It was pressure from these clients on the "short" brokers which led to the present situation.

5 Mr Brown said that of the the 26 ring dealing brokers, 13 had contracts with the ITC. Seven of these 13 had said they would refuse to pay up if a proposal requiring them to pay the "shorts" were passed by the LME. If they refused to pay, then the LME Board would have no alternative but to suspend them.

6 Mr Brown said that these seven brokers would actually be able to make payments were a proposal to call further margins passed, but they would refuse to do so because it would make their negotiating position with the ITC untenable, since they would no longer have any resources to commit to a burden sharing agreement. Mr Brown said however that this was a false argument since if Newco were set up, then the brokers who were creditors of the ITC would immediately be able to borrow money from the banks. Mr Lion said, however, that in his opinion some of the seven ITC creditor brokers who had said that they would not pay up would in fact not be able to pay.

7 Mr Lion stressed that it was essential for the UK Government to be prepared to commit more money to the Newco proposals. The exact level of a further commitment was less important than the comfort that a readiness to make it would give to the LME.

8 Mr Lion said that up until now, the LME Board, in keeping the market closed, had been favouring the ITC creditor brokers at the expense of the "shorts", but from now on this would have to change. As Directors, they had a duty to the LME as a whole.

9 Mr Mountfield asked why the "shorts" would press for payment, given that the Government had said that it would not bail out the LME, and given that pressing for payment might well prejudice the burden-sharing negotiations and hence bring about a collapse of the LME. Mr Lion replied that the clients of the "shorts" as distinct from the "short" brokers themselves were only interested in being paid. They did not really have much interest in the continued existence of the LME.

10 Mr Lion said that he hoped that the LME meeting later that afternoon would defer a decision on requiring payments to be made to the "shorts" until 7 February. However, he was sure that it could not be delayed any further beyond that. The Secretary of State stressed that the Government's position on bailing out the LME remained the same as in his letter to Mr Lion of 30 January. Mr Lion said that he would not mislead the LME as to the Government's position, but he stressed that the future of the LME "rested in the Government's hands".

11 Mr Brown said that the only way the LME would be able to buy time beyond 7 February would be to require the ITC creditor brokers to pay the "shorts". If the ITC creditor brokers refused to do this, then that might lead to the closure of the LME as a whole.

12 Mr Gee warned that Chilean and African copper producers were quite likely within the next 48 hours to decide to abandon the LME as their yardstick for pricing purposes. This would have a very serious effect on the LME and on UK copper-using industry.

13 The Secretary of State concluded the meeting by repeating that it was for the LME to decide what it did, but that the Government were anxious that it took decisions in the light of the fact that there appeared at last to be a real prospect of credible negotiations between the ITC, the banks and the brokers.

Michael Gilbertson

MICHAEL GILBERTSON
5 February 1986

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LME - TIN - PROPOSAL TO CALL FURTHER MARGINS

A The Proposal

The LME Board is to consider further at a meeting this afternoon, a proposal that there should be margin calls on (all members who have purchase commitments from other members on tin contracts which are now in suspence "longs") based on a notional price for tin - reportedly either £7,500 or £7,000 a tonne.

The intention is to ease the burden falling on those who, because delivery of tin metal has been frustrated by market suspension, ("shorts") have faced difficulties with finance and the cost thereof in holding the tin. The assistance would take the form of provisional part payment to the shorts and it must be assumed that the MEMO system would be the route taken since such payments reflect directly the levels of open indebtedness by each broker to the ring as a whole.

It is also intended to release the original £50mn or so to those who provided it after all margin calls had been met. It would appear, therefore, that there would be a short but possibly crucial period when firms or their parents would need to finance both calls. It should, however, be possible to finance part of the margin call against the security of the trust and status of funds originally provided in most cases, one assumes.

B Why it is being done at this time

The LME Board has been under mounting pressure from shorts to take action to mitigate hardship. This pressure first manifested itself in a threat by Shearson to issue and serve a writ on MacLain Watson and others for fullfilment of "B" contracts. The threat was also made to the LME as the body whose decision had led to the frustration. This, as a potential legal wrangle between ring dealing members, strikes at the very heart of the LME and it is clearly more difficult for the Board to ignore or defer action on issues involving their central membership.

C The Effects of Such a Margin Call

The view has been expressed to us that the margin call at this time cannot be beneficial to the market as a whole because -

(i) if the call is met by all firms, it may be seen by the ITC as an indication that brokers are able to contribute significantly more to Newco than the £50mn offered so far;

(ii) if one or more firms are unable to meet the call it may at worst precipitate declarations of insolvency. Equally damaging would be simple default where solvency is unclear but where it would nevertheless be necessary for the LME to determine whether a member should be suspended on grounds of commission of an act of bankruptcy.

If Newco were to prove a viable solution, the ability of ITC creditor members to make subscription to capital might be critically impaired as a result of strains on liquidity imposed by the margin call. Firms affected would, of course, recoup the sum as a result of reduced payment liability to shorts but again there is a gap to be breached unless capital subscription can be temporarily deferred.

The only way out appears to b;c to persuade the LME Kto defer action for a further few days and for the talks with the ITC in that period to provide confidence that a Newco solution will emerge.