



PM/90/041

PRIME MINISTER

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Prime Minister

European Council, 25/26 June 1990: Western Assistance to the

Soviet Union

1. We agreed that this was now likely to be a major subject of discussion at the European Council, and I have seen Chancellor Kohl's letter, to which I do not think we should reply. The issue will also be high on the agenda at Houston.

2. There are 5 distinct strands to consider. First, the short term issue of Soviet bids for FRG aid, partly to cover the cost of their troops in Eastern Germany, partly to meet what they claim are the costs to them of GDR absorption into the FRG, and partly as the price for their acquiescence to unification. They also envisage a short-term credit initiative by private German banks, with the Federal Government acting as guarantor. All this is best left to the Germans.

3. Secondly, credit. I am not convinced that there is as yet a major problem here. All major export credit agencies, apart from the US EXIM Bank, are open for credit cover for the Soviet Union. ECGD's exposure is just over £1132 million, against a current limit of £1925 million which is under review and may be reduced. Soviet commitments guaranteed by the Soviet Bank of Foreign Economic Affairs are being met in full, though there have

/been delays

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We need to select to Douglas

new organization like Confella. 1 member

for in computer admin? like the Banks of Britain.

and second line loans to him.

To propose funding credit - Russia the Banks would be disastrous especially for us having jobs the banks in London not

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The Foreign Secretary needs your approval of the attached line to take on aid to the Soviet Union. Generally it seems right: but asking funding

to coordinate the exercise will

inappropriate. Alternative to French etc very counter-productive. There is no need to mention any name. Agree otherwise?

CB 21/6



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been delays in payment by certain Soviet Foreign Trade Organisations and enterprises not subject to its guarantees. (Most ECGD business is covered by these guarantees.) The Bank of Foreign Economic Affairs seems to be attempting to re-impose discipline. The Soviet Union has recently undertaken some limited gold swaps to raise foreign currency, and the signs are that delays will be made good over the next few months. Delayed payments are believed to be some \$2 billion (out of a total debt of some \$48 billion).

4. Provided the Russians do regularise the position and continue to provide guarantees, they will not be denied access to continued cover in the medium term. There seems no case for a major effort to secure increases in everyone's limits on them. Extra credit would be wasted and add to the present debt burden.

5. The third element is "Know How/technical assistance", where many countries have bilateral programmes (we provide some management training). We are all agreed that perestroika requires our encouragement. Gorbachev deserves our help if this process is to be sustained. Managerial and entrepreneurial know how is directly relevant to the fundamental economic reforms the Russians should be introducing. I believe we now need to be ready to help on lines comparable to the Know How Fund for Eastern Europe. We need not use a figure in public at this stage, but a credible programme capable of making an impact would require substantial sums and would have to stand comparison with what we are doing for Poland and Hungary. This suggests a figure for the UK of the order of £100 million over several years. The level of our activity would build up as reforms are put in place. This would entail additional PES

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provision. The existing provision and my bid in this year's Survey for the Eastern European Know How Fund do not cover the situation in which we now find ourselves.

6. Fourth, the Community has concluded a Trade and Economic Co-operation Agreement with the USSR. This covers gradual removal of quantitative trade restrictions, reciprocal access for EC business in the Soviet Union, and provides for economic co-operation in areas such as environment, research and development etc. We can take credit for that, and can press in the Community for more rapid implementation. But it will not cut much ice with, for example, the Germans.

7. The Soviet leadership appear to be looking for untied credits to allow them to import consumer goods to ease the inevitable pain involved in introducing real reform. They have suggested a figure of US\$10-20 billion over 3 years. The Germans envisage medium term assistance on a massive scale, to oil the wheels of unification and fend off the threat of growing instability in Moscow. But as I said at Monday's Foreign Affairs Council, we should only contemplate economic support for Soviet reform when there is reform to support. The Russians must first adopt the right policies and agree a framework and timetable for their implementation. Such conditionality is, rightly, at the core of our, and the G24's, approach to Eastern Europe. Much further analysis is necessary before we can establish what sort of help might make sense once the right Soviet economic policies are in sight. Consideration of how we should respond will only then be possible, and the task for Dublin and Houston is to get our partners to accept that, without our becoming isolated or accused of obstructionism. I was encouraged that Attali told me yesterday that he thought this was all that was possible now.

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8. Offering only "Know How" will not, I think, take the trick: we need also to devise a constructive proposal for a mechanism to

That is what the new Bank is for

- (a) conduct the necessary analysis and data on the Soviet economy;
- (b) advise the Russians on reform and how to mobilise their resources;
- (c) set out the conditions for support and, at the right time, put together that support.

9. There are at least four possibilities:

- (a) Help from the G24, now being extended to all the emerging democracies of Eastern Europe but not to the Soviet Union, has so far worked well, with the European Commission working effectively as co-ordinator, and collector of data. But at its core have been EC measures, proposed by the Commission, and, where financing was involved, funded by the EC Budget. A parallel G24 approach to the Soviet Union would undoubtedly involve Commission proposals for a substantial EC contribution. That is plainly what M. Delors wants, and we ought to divert him, though I think we should recognise that it will be difficult to avoid some role for the Commission, given their success with G24.

No role for G24 - we now have the Bank which is

- (b) The EBRD is the only major financial institution to which the Russians already have a ticket. But it is not yet open for business, will take time to build up expertise, and will lack a capacity to impose balance of payments conditionality. Soviet borrowing from it will be limited in the first 3 years to no more

larger than Europe

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We will have to build up such a capacity. In the meantime it could be supervised from the IMF.



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than its contribution to the Bank's capital. But it will bring together all interested parties. The Bank itself, or Attali personally, could have a role, and indeed M. Attali has already staked a claim. I conclude that EBRD could play a part, but not a dominant one.

Why diminish the role of the Bank in London? Why?

- (c) The OECD has a wealth of experience on general economic policy and on specific sectors such as energy, agriculture and labour markets. It prepares detailed policy analysis for member countries, and could provide a useful input into any study of the Soviet economy. It has no expertise in providing technical assistance or in imposing conditionality. We have already proposed that the OECD should have a major role in the economic aspects of CSCE follow up. An enhanced CSCE/OECD role could be attractive to the Russians.

No - what is the point in setting up more committees

- (d) The IMF is the best source of the analytical expertise to determine macro economic conditionality; the IBRD similarly on micro economic aspects. The Soviet Union is not a member of the IFIs, but it might nevertheless be possible to devise a mechanism which would use IMF skills, and give them the lead in co-ordinating western support. At a minimum, suitable staff could be seconded to this work. Using the IMF/IBRD expertise would have the additional advantage of ensuring that oversight was by Finance Ministers. There would be advantage in appointing a leader of a Task Force to take on the work. Onno Ruding would be an ideal choice, and would help make it more attractive to the US.

See White Paper London Bank

Monroe - we already have a task force in the Bank

10. I conclude that setting up a Task Force involving mainly the IMF/IBRD is much the best option, drawing on the expertise and experience of the other three.



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11. On this basis, the right line for us at the European Council might therefore be along the lines of the attached note. It suggests a remit to report initially to Finance Ministers at the IMF/IBRD meetings in September. US support will be crucial to this approach and I plan to discuss it with Secretary Baker in the margins of 2 + 4 on 22 June.

12. Copies of this minute go to the Chancellor of the Exchequer, the Secretary of State for Trade and Industry, and to Sir Robin Butler.

(DOUGLAS HURD)

Foreign and Commonwealth Office
21 June 1990

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10 DOWNING STREET

LONDON SW1A 2AA

From the Private Secretary

22 June 1990

Dear Stephen,

EUROPEAN COUNCIL: WESTERN ASSISTANCE TO THE SOVIET UNION

The Prime Minister has considered the Foreign Secretary's minute of 21 June about the likely discussion at the European Council of Western assistance to the Soviet Union. She is generally content with the line set out in paragraphs 1-7 of the minute. But she feels very strongly that we are going down the wrong track when it comes to devising the mechanism for such assistance, as set out in paragraphs 8 and 9. Her basic points are that we do not want to proliferate new institutions: and that it would be tactless and counter-productive in the extreme to propose the appointment of Ruding to co-ordinate the work. She points out that we have gone to a great deal of trouble and very considerable expense to secure the European Bank for Reconstruction and Development for London, and should now build up their role rather than try to minimise it and provoke Attali by appointing Ruding to the task of co-ordinating the study of assistance to the Soviet Union. She agrees that we shall need to have the co-operation of the IMF and the World Bank and possibly of staff from the OECD. But she feels that we should give the EBRD a leading role in the work. The fact that Attali does not yet have any significant staff will be a constraint on him, since he will in practice have to rely on the expertise of other institutions.

The Prime Minister thinks, therefore, that we shall have to revise this part of our approach radically before the Dublin European Council.

I am copying this letter to the Private Secretaries to the Chancellor of the Exchequer and the Secretary of State for Trade and Industry.

(C. D. POWELL)

Stephen Wall, Esq.,
Foreign and Commonwealth Office.

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