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PRIME MINISTER

EGYPT: ECGD SECTION 2 COVER

EX(82)1

BACKGROUND

There is currently a limit of £500 million on the cover given by the Export Credits Guarantee Department (ECGD), under its Section 2 (national interest) account, for exports to Egypt - cover is given under Section 2 for the larger deals, involving longer credit periods, which ECGD cannot deal with under their Section 1 commercial account arrangements. Of this £500 million, £430 million is already committed and the balance will probably be taken up shortly. The Treasury chaired official Export Guarantees Committee could not agree on an increase in the limit.

2. In EX(82)1 the Secretary of State for Trade asks the Committee to consider whether the limit should be raised and if so by how much, and whether £270 million should be earmarked for the sale of ships to the Egyptian Navy - this sale is discussed in more detail in the Secretary of State for Defence's letter of 11 December at Appendix 1 of EX(82)1. He invites the Committee to consider 5 options, listed on page 3 of his paper. These require the Committee to consider:-

(i) whether to stick to the present limit of £500 million, which would mean switching off fairly soon further cover for business with Egypt - Option 1;

(ii) whether to make a general increase in the present limit with civil and defence sales being dealt with on a first come, first served basis; and to decide between an increase to £650 million (Option 2) or to £900 million (Option 4);

(iii) whether to make a special reservation of £270 million for the warships, and either to leave the limit of £500 million unchanged

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(Option 5) or to increase it to £650 million (Option 3).

3. The Secretary of State for Trade does not reveal his own preference. He has to balance advice from the ECGD, who counsel caution because of doubts over political stability in Egypt, and his own officials dealing with exports who would like to see an increase. At the least he is likely to recommend an overall increase to £650 million and he might be willing to go along with a separate allocation for the warships. The Secretary of State for Defence - probably supported by the Lord Privy Seal and the Secretary of State for Industry - is likely to go for an increase in the general limit to £650 million plus a special reservation for 6 months for the warships order (i.e. Option 3). If the warship order did not go ahead he might then want to make the special allocation generally available - that is, in practice, to go for an overall increase to £900 million (Option 4). The Chancellor of the Exchequer will probably acknowledge the need for some increase but he may prefer not to go beyond a general increase to £650 million.

The arguments for caution

4. The reasons for being cautious in increasing limits for business with Egypt are set out in the paragraphs on the economic and political background on page 2 of EX(82)1. The Egyptian economy is heavily dependant on aid and on the continuing support of the Americans. Although President Mubarak has started well there are obvious worries over the political stability of Egypt. Any risks which ECGD take now in giving cover on major orders will be with them for a long time - in the case of the warships there will be a building period of 4 years or so and then a repayment period of 10 years. The Committee may well conclude that this points to increasing the limit by an amount which would lead to a review later in the year when, among other things, it will be known whether the Israelis have withdrawn successfully from the Sinai.

The industrial case

5. Subject to the availability of credit the Egyptians are interested in buying from Vospers either 6 corvettes or 2 frigates. Vospers will be running out of work in their Portsmouth and Southampton yards by about June this year. Either order would give them 4 years work and save around 1,000

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jobs in the area. The order would, therefore, be a helpful offset to the rundown of other defence activities in Portsmouth and useful in preserving capacity at Vospers.

6. The Secretary of State for Defence is also looking for a major order from the Egyptians for Rapier Missiles and for other defence equipment. On top of that there is a strong interest in civil exports to Egypt. If ECGD are to cover such business, the limit will have to be increased soon.

The political case

7. The Secretaries of State for Trade and for Defence have each visited Cairo in recent months to talk about possibilities of UK exports, including warships and Rapiers in particular. The Egyptians' expectations have been built up and if the Government were now to say that further credit will not be available that could be seen as a vote of no confidence in the stability and prospects of the new regime.

8. You are meeting President Mubarak on Saturday 6 February at Chequers. He will probably expect some indication of interest in civil and military exports to Egypt and the line you take will turn on the Committee's decision in this case.

HANDLING

9. You will wish the Secretary of State for Trade to speak to his paper and to advise the Committee on which of the 5 options listed he recommends them to adopt. You will then wish to hear the views of each of the other Ministers attending: the Secretary of State for Defence, the Lord Privy Seal, the Secretary of State for Industry and the Chancellor of the Exchequer.

10. If, as seems likely, it is generally agreed that there should be some increase in the present limit you will need to decide on the amount and on whether it should be an overall increase or whether there should be a special reservation of £270 million for 6 months for the warships order. (NB last year a similar provision was made outside the ECGD ceiling, with a time limit, in support of a proposed Hawk Aircraft deal).

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11. The option likely to command most support is that of increasing the present limit to £650 million with a separate and special reservation of £270 million for 6 months for the warships deal (Option 3).

- Option 2, a general increase to £650 million, would be insufficient to cover both warships and other civil and defence business for very long.

- Option 5, which reserves £270 million for warships but leaves the limit at £500 million, would mean that cover for civil and other defence business would quickly come up against the limit.

- Option 4, a general increase to £900 million, is probably too generous if the warship deal were to fall through. In that situation it would be better for Ministers to decide then, in the light of developments in Egypt, whether the £270 million should be added to the general limit.

CONCLUSIONS

12. In summing up you will wish:-

1. To record the Committee's decision on which of the 5 options, or variants of them, listed in EX(82)1 is approved.
2. To ask the Lord Privy Seal in consultation with the Secretaries of State for Trade and for Defence, to take account of the Committee's decision in your briefing for your talks with President Mubarak on 6 February.

PLG

P L GREGSON

21 January 1982