

Poland

Ref: B06456

PRIME MINISTER

c Sir Robert Armstrong

Economic Measures Against the Soviet Union
(OD(82) 15)

BACKGROUND

File AF

The Foreign and Commonwealth Secretary's paper for OD tomorrow has been prepared in response to your suggestion (Mr Coles' letter to the Foreign and Commonwealth Office of 16th March) that, in the light of the Buckley mission, he should provide a basis on which Ministers could discuss in depth the policy implications underlying current exchanges between the Americans and their European allies about East-West economic relations. You were concerned at the prospect of a further unsatisfactory bout of frustration within the Alliance. The Secretary of State for Trade's letter to the Foreign and Commonwealth Secretary of 23rd March, about John Brown's pipeline contract, is also relevant.

Submitted to you in folder 2 earlier today.

2. The Buckley mission was designed to promote current United States ideas about the need to end or restrict the subsidisation and guaranteeing by Western Governments of export credit for the Soviet Union. Although these ideas are not supposed to be Poland-related, it was clear that the mission's report was likely to affect American decisions about existing contracts (including John Brown) and about possible further measures in the Polish context. It was received without enthusiasm in Paris, Bonn and Rome. In London our agreed attitude was receptive but interrogative; in practice, the Americans cannot have found us much more encouraging than our Continental partners, and we effectively refused to agree to a 60-day "pause" in government-supported export credit for the Russians.

3. The recommendations now made by the Foreign and Commonwealth Secretary are procedural rather than substantive. They involve agreeing to a multilateral meeting on the credit issue with the Americans and the other Versailles participants, and private soundings of our European allies. With some grumblings, the Economic Ministers are likely to agree; their main concerns will be that we should not get out ahead of our partners or inflict more damage on ourselves than on the Soviet Union. But the paper's



rather blatant tone leaves it far from clear whether such procedural steps will in fact be enough to achieve our immediate objectives of saving the John Brown contract, averting further American measures detrimental to our interests and avoiding a major open split in the Alliance. If that underlying question is not probed now, it will be difficult to do so collectively until after the Easter recess; Lord Carrington is abroad almost all next week and on holiday the week after.

4. The Secretary of State for Trade's letter seems to suggest that, provided the Government undertakes not to be obstructive, John Brown may be able to find some means of saving their project even if the Americans do not exempt existing contracts. It is not clear how financially damaging this would be to them; nor how embarrassing vis-a-vis the United States Government it would be for us to give such an undertaking. But the matter is certainly urgent and should be considered by the meeting.

5. As background for the meeting, the Chancellor of the Exchequer has circulated his minute of 24th March on East European Indebtedness. This updates the January report of the Official Committee concerned (OD(82) 1) without challenging the broad conclusions then agreed. But it highlights an immediate and unexpected liquidity crisis in Hungary and the liquidity problems also faced by the Soviet Union; and it stresses the danger that American-inspired action against credit support could undermine the banking community's declining confidence in Eastern Europe and so precipitate a general collapse.

FLAG B

FLAG C

6. The Secretary of State for Industry will be represented by Mr Lamont.

HANDLING

7. The Foreign and Commonwealth Secretary should introduce his paper. The Secretary of State for Trade will wish to comment, as will the Chancellor of the Exchequer and Mr Lamont. It should not be too difficult to agree on the procedural way forward suggested by Lord Carrington.



8. You will need to probe the following issues of substance.
- (a) Are dramatic developments likely before the end of the Easter Recess (when the Committee will next be meeting with the Foreign and Commonwealth Secretary present)? In particular
- (i) Are the Americans likely to announce new sanctions? If so how far would they be likely to damage our interests? The Foreign and Commonwealth Secretary and Secretary of State for Trade should comment.
- (ii) Is time likely to run out for John Brown? If so, are we content with the fall-back measures canvassed in the Secretary of State for Trade's letter of 23rd March? How much damage will the company suffer? The Secretary of State for Trade and Mr Lamont should address the company's position, and the Foreign and Commonwealth Secretary likely American and European attitudes.
- (iii) How likely is a major public split in the Alliance? How short is American patience running? How resentful are the Germans and French? The Foreign and Commonwealth Secretary should comment; and you may yourself wish to mention Chancellor Schmidt's attitude.
- (iv) How likely is a general financial collapse in Eastern Europe? How vulnerable are the Russians to economic pressure? How damaging would a collapse be to Western interests? The Chancellor of the Exchequer should speak to this, and the Foreign and Commonwealth Secretary should comment.
- (b) To the extent that any of these dangers seem imminent, what does the Foreign and Commonwealth Secretary recommend we or anyone should do about them? How seriously should we be prepared to consider, if necessary, restricting credit support? The Secretary of State for Trade will wish to comment.
- (c) Does the Committee accept the American thesis that the Soviet military threat can and should be limited by hostile economic measures?



(d) Is enough being done to ensure that any measures taken by the United States and Europe are also taken by Japan? Should this problem be tackled at, and at the preparations for, the Versailles Summit? What do the Foreign and Commonwealth Secretary and the Secretary of State for Trade suggest?

CONCLUSION

9. If the underlying problems are unlikely to reach crisis proportions before late April, the Committee need only endorse the Foreign and Commonwealth Secretary's paper; take note of the Chancellor of the Exchequer's minute; and approve the policy on John Brown suggested in the Secretary of State for Trade's minute.

10. If an earlier crisis seems likely, the Committee will need to decide

- whether there are any practical steps that you or the Foreign and Commonwealth Secretary could take to try to bridge the gulf between our continental allies and the Americans;
- how far in that context Britain should be willing to sacrifice her economic interests as a trading nation in order to try to avert grave political damage to the Alliance on which our security depends.

Given a clear steer on these points, specific contingency planning could be referred to officials.

24th March 1982

R L WADE-GERY