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TO IMMEDIATE FCO

TELEGRAM NUMBER 2176 OF 31 JULY

INFO IMMEDIATE PEKING

FOLLOWING FROM PRIVATE SECRETARY.

FUTURE OF HONG KONG: SECRETARY OF STATE'S MEETING WITH CHAIRMAN DENG XIAOPING.

SUMMARY

1. THE SECRETARY OF STATE HAD NINETY MINUTES WITH DENG THIS MORNING. DENG WAS EVIDENTLY WELL PLEASED WITH THE POINTS OF AGREEMENT REACHED DURING THE VISIT. BUT HE AGAIN EXPRESSED CONCERN, AS HE HAD DONE IN APRIL, THAT IN THE PERIOD BEFORE 1997 THE HONG KONG GOVERNMENT WOULD TAKE ACTION IN THE FIELD OF FINANCE, LAND AND THE PUBLIC SERVICE THAT WOULD ADVERSELY AFFECT THE INTERESTS OF THE FUTURE SAR, AND CHINA. THE SECRETARY OF STATE APPLAUDED DENG'S CONCEPT OF "ONE COUNTRY TWO SYSTEMS", ANSWERED HIS POINTS IN DETAIL AND ASSURED HIM THAT THE PRESENT PRUDENT MANAGEMENT OF HONG KONG WOULD CONTINUE.

DETAIL

2. IN THE COURSE OF INTRODUCTORY EXCHANGES, DENG OBSERVED THAT THE TWO SIDES COULD BE SAID TO HAVE ALMOST REACHED AGREEMENT ON THE HONG KONG QUESTION. ONLY SMALL DETAILS REMAINED. THE THANKED THE SECRETARY OF STATE AND ALL CONCERNED WITH THIS ACHIEVEMENT, WHICH WOULD SET AN EXAMPLE TO THE WORLD.

3. THE SECRETARY OF STATE REPLIED THAT THE PRIME MINISTER AND HE BOTH ATTACHED GREAT IMPORTANCE TO THIS SUBJECT. HE WAS VERY GLAD THAT SUBSTANTIAL PROGRESS HAD BEEN MADE AND PAID A TRIBUTE TO WU'S ROLE. DENG'S IDEA OF ONE COUNTRY TWO SYSTEMS WAS OF GREAT IMPORTANCE IN CARRYING THROUGH THE HISTORIC ENTERPRISE OF ENSURING HONG KONG'S CONTINUING STABILITY AND PROSPERITY BOTH BEFORE AND AFTER 1997. SOME IMPORTANT ISSUES REMAINED TO BE RESOLVED IN SPIRIT OF THIS APPROACH.

4. AFTER A LONG DIGRESSION ON ONE COUNTRY/TWO SYSTEMS, DENG SAID THAT HIS STRONG PERSONAL CONVICTION WAS THAT IT WOULD WORK IN THE CASE OF HONG KONG. THE QUESTION OF SOVEREIGNTY WOULD NOW BE SOLVED. THE CENTRAL CHINESE GOVERNMENT HAD NO INTENTION OF TAKING A SINGLE PENNY



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5. DENG CONTINUED THAT HE WAS VERY CONCERNED ABOUT THE PERIOD BEFORE 1997. IF THIS WENT WELL, SO WOULD THE SAR. THE FIRST ISSUE HE RAISED WAS PERSONNEL. THERE WERE MANY COMPETENT PEOPLE IN HONG KONG (HE INTERJECTED THAT HE DID NOT INCLUDE PEOPLE LIKE SIR S.Y. CHUNG, WHO HAD EVIDENTLY IRRITATED DENG WHEN IN PEKING RECENTLY). HONG KONG PEOPLE, NOT PEKING PEOPLE, SHOULD RUN HONG KONG. THE MAIN DEPARTMENTS OF THE HONG KONG GOVERNMENT SHOULD BE RUN BY 'PATRIOTS'. THE OVERWHELMING NUMBER OF GOVERNMENT OFFICIALS SHOULD ALSO BE PATRIOTS. BY THIS HE MEANT THOSE WHO LOVED HONG KONG AND THE MOTHERLAND, I.E. FAVOURED REUNIFICATION WITH CHINA.

6. THE SECRETARY OF STATE ASSURED DENG THAT WE WERE DETERMINED TO DO ALL WE COULD TO ENSURE A SMOOTH TRANSITION IN 1997. WE CARED AS MUCH ABOUT THIS AS DID CHINA. BOTH COUNTRIES HAD THE HIGHEST INTEREST IN MAINTAINING STABILITY. HE HOPED THAT IN THE YEARS UNTIL 1997 WE WOULD CONTINUE TO COOPERATE, AND THAT CHINA WOULD LISTEN TO BRITAIN'S ADVICE. HE ENTIRELY AGREED THAT HONG KONG PEOPLE SHOULD RUN HONG KONG. THE HONG KONG GOVERNMENT WERE ALREADY BRINGING FORWARD HONG KONG PEOPLE INTO SENIOR POSITIONS (HE WENT ON TO GIVE EXAMPLES). DENG COMMENTED THAT THE IMPORTANT QUESTION WAS WHAT KIND OF PEOPLE THEY WERE. BRITAIN AND CHINA SHOULD TACKLE THIS QUESTION IN THE LATTER HALF OF THE TRANSITION PERIOD. IT WAS NOT NECESSARY TO HAVE LEFTIST PEOPLE IN SENIOR POSITIONS. BUT THEY MUST BE PATRIOTS.

7. DENG THEN PUT THE FOLLOWING POINTS, MAKING IT CLEAR HE WAS ADDRESSING THE GOVERNOR:

(I) NOTHING SHOULD BE DONE TO AFFECT THE VALUE OF THE HONG KONG DOLLAR. ITS CREDIBILITY WAS BASED ON THE LARGE SUM IN THE EXCHANGE FUND. HE UNDERSTOOD THAT THERE WAS MORE IN THE EXCHANGE FUND THAN THE TOTAL OF HONG KONG DOLLARS ISSUED. THERE SHOULD BE NO CHANGE IN THAT SITUATION.

(II) LAND.

THE CHINESE HAD AGREED THAT LAND LEASES COULD BE GRANTED BY THE HONG KONG GOVERNMENT FOR 50 YEARS AFTER 1997. THEY HAD ALSO AGREED THAT THE HONG KONG GOVERNMENT COULD USE THE INCOME FROM PREMIA CORRESPONDING TO THE PERIOD AFTER 1997. THEY HAD DONE SO ON CONDITION THAT INCOME FROM THE LAND LEASES SHOULD BE USED FOR LAND DEVELOPMENT AND CAPITAL CONSTRUCTION: NOT FOR CURRENT EXPENDITURE.

(III) HE HOPED THE HONG KONG GOVERNMENT WOULD NOT INCREASE THE SIZE OF THE PUBLIC SERVICE BEFORE 1997, NOR MAKE SUBSTANTIAL INCREASES

(III) HE HOPED THE HONG KONG GOVERNMENT WOULD NOT INCREASE THE SIZE OF THE PUBLIC SERVICE BEFORE 1997, NOR MAKE SUBSTANTIAL INCREASES IN THEIR SALARIES AND PENSION RIGHTS. OTHERWISE THE SAR GOVERNMENT WOULD BE FACED WITH A MAJOR BURDEN.

(IV) HE HOPED THE HONG KONG GOVERNMENT ~~WOULD~~ NOT SEEK TO IMPOSE A TEAM OF THEIR OWN PEOPLE ON THE FUTURE SAR GOVERNMENT.

(V) HE HOPED THE HONG KONG WOULD DISCOURAGE A WHOLESALE FLIGHT OF CAPITAL. HE MENTIONED JARDINES AND RUMOURS THAT THE HONG KONG AND SHANGHAI BANK WAS THINKING OF MOVING ITS CAPITAL OUT OF HONG KONG. U.S. AND JAPANESE CAPITAL WOULD NOT LEAVE; THEY HAD SAID THAT IF OTHERS LEFT, THEY WOULD BRING IN MORE. IF BRITISH CAPITAL STAYED, SO WOULD THE REST. HE HOPED THE GOVERNOR COULD PERSUADE THE HONG KONG SHANGHAI BANK NOT TO MOVE OUT.

8. THE SECRETARY OF STATE UNDERLINED THE COMMON OBJECTIVE OF BRITAIN AND CHINA IN PRESERVING PROSPERITY AND STABILITY IN HONG KONG. HE ADDED THAT, IN FAIRNESS TO SIR S.Y. CHUNG, IT SHOULD BE SAID THAT HE AND HIS COLEAGUES ALSO CARED ABOUT THE FUTURE OF HONG KONG. THE GOVERNOR'S PRIME PURPOSE WAS TO PRESERVE ALL THAT WE AND CHINA CARED ABOUT IN HONG KONG. HE ASSURED DENG THAT, DRAWING ON HIS EXPERIENCE AS CHANCELLOR AND CHAIRMAN OF THE IMF INTERIM COMMITTEE, NO COUNTRY'S FINANCES WERE MORE PRUDENTLY MANAGED THAN THOSE OF HONG KONG. THAT WOULD CONTINUE. THE SAME APPLIED TO THE PUBLIC SERVICE. HE ENTIRELY AGREED ABOUT THE FUNDAMENTAL IMPORTANCE OF THE HONG KONG DOLLAR FOR HONG KONG'S ECONOMY. WE WOULD CONTINUE TO SUSTAIN IT AS WE HAD DONE IN THE PAST. THE EXCHANGE FUND WOULD CONTINUE TO BE MANAGED FOR THE GOOD OF THE HONG KONG ECONOMY.

9. ON LAND, THE SECRETARY OF STATE SAID THAT DENG NEED HAVE NO FEAR. HE GAVE HIS PERSONAL ASSURANCE THAT THE HONG KONG GOVERNMENT WOULD CONTINUE TO MANAGE LAND IN THE BEST INTERESTS OF THE SAR. WE HAD PUT PROPOSALS TO CHINESE EXPERTS.

10. ON THE HONG KONG AND SHANGHAI BANK, THE SECRETARY OF STATE MADE CLEAR THAT IT HAD NO PLANS TO MOVE. THE JARDINES MOVE HAD NOT BEEN TIMELY, BUT THEY HAD AT LEAST MAINTAINED THEIR HQ AND OPERATIONS IN HONG KONG. THE MAIN POINT WAS THAT BRITAIN AND CHINA NEEDED TO WORK TOGETHER TO ENSURE THAT HONG KONG REMAINED A MAGNET FOR CAPITAL. WE ALL WANTED TO SEE THE U.S. AND JAPAN KEEPING THEIR CAPITAL IN HONG KONG. BUT THIS WAS NOT A DECISION FOR GOVERNMENTS. IT REQUIRED THE CONTINUING CONFIDENCE THAT THE CAPITALIST SYSTEM WOULD CONTINUE. THAT WAS WHY WE WERE SEEKING COMPREHENSIVE AND PRECISE PROVISIONS ON SUCH ISSUES AS THE LAW, CIVIL AVIATION ETC. HE HOPED THAT THE CHINESE SIDE WOULD LISTEN TO OUR ADVICE ON THIS.

11. DENG SAID THIS WAS VERY GOOD. THE CHINESE SIDE HAD THE HIGHEST TRUST IN THE SECRETARY OF STATE AND THE PRIME MINISTER. THEY HAD COME TO THAT CONCLUSION IN THE COURSE OF THE HONG KONG NEGOTIATIONS. HE WAS FULL OF CONFIDENCE THAT ONE COUNTRY TWO SYSTEMS WOULD WORK.

12. IN CONCLUSION DENG INVITED THE QUEEN TO VISIT CHINA AND SAID THAT PRIME MINISTER ZHAO HOPED TO VISIT THE U.K. NEXT YEAR; BOTH

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13. HE ASKED FOR HIS GOOD WISHES TO BE CONVEYED TO THE PRIME MINISTER AND EXPRESSED HIS THANKS FOR HER CONTRIBUTION TO THE SOLUTION OF THE HONG KONG QUESTION.

14. ON THE WAY TO THE AIRPORT, ZHOU MAN TOLD THE SECRETARY OF STATE THAT THERE WAS AN ADDITIONAL POINT WHICH DENG INTENDED TO MENTION. THIS WAS THAT HE HOPED THE HONG KONG GOVERNMENT WOULD NOT UNDERTAKE VERY LARGE PROJECTS BEFORE 1997 WHICH WOULD BE A SUBSTANTIAL DRAIN ON THE SAR'S RESOURCES.

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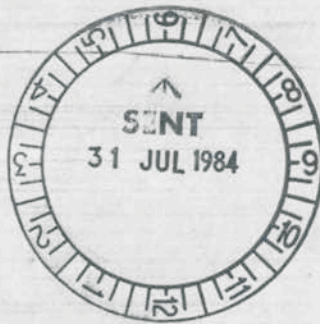
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FOLLOWING FROM PRIVATE SECRETARY

MEETING WITH SHAIRMAN DENG XIAOPING: INVITATIONS TO THE QUEEN AND PRIME MINISTER

1. THE SECRETARY OF STATE SAW CHAIRMAN DENG XIAOPING THIS MORNING. REPORTING TELEGRAM WILL FOLLOW SHORTLY. BUT YOU SHOULD KNOW IMMEDIATELY THAT AT THE CONCLUSION OF THE MEETING, DENG EXTENDED ON BEHALF OF THE CHINESE GOVERNMENT AN INVITATION TO HER MAJESTY THE QUEEN TO VISIT CHINA AT A TIME CONVENIENT TO HER. THE SECRETARY OF STATE THANKED DENG AND UNDERTOOK TO CONVEY THE INVITATION TO THE QUEEN. IN DOING SO HE POINTED OUT THAT TH QUEEN'S PROGRAMME OF OVERSEAS VISITS WAS OF COURSE PLANNED WELL AHEAD.
2. DENG ALSO SAID THAT THE CHINESE PRIME MINISTER ZHAO ZIYANG LOOKED FORWARD TO VISITING BRITAIN EARLY NEXT YEAR. HE HAD NOT INCLUDED BRITAIN ON HIS RECENT EUROPEAN TOUR BECAUSE IT WOULD NOT HAVE BEEN APPROPRIATE GIVEN THE STATE OF THE HONG KONG NEGOTIATIONS AT THAT TIME. THE SECRETARY OF STATE AGAIN THANKED DENG AND SAID THAT WE WOULD BE VERY GLAD TO SEE ZHAO AT A MUTUALLY CONVENIENT DATE.
3. YOU WILL WISH TO ALERT THE PALACE AND NO.10 TO THESE INVITATIONS AS DENG, OR THE CHINESE, MAY WELL MAKE THEM PUBLIC TODAY IN PEKING.

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