

APR 1986

*Mr Pedde*  
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*Mr Khum*  
*M 11/74*  
*cc Mr Baker P2P2*  
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01 211 6402

TO <i>Mr Simpson</i>	COMES TO
FOR ADVICE (A.I.)	<i>PS MFT</i>
DRAFT REPLY IF APPROPRIATE)	<i>PS Sir B.H.</i>
PLEASE BY: <i>22-4-86</i>	<i>Mr Roberts</i>
IF DEADLINE	<i>Mr Gill</i>
CANNOT BE MET	<i>Mr Titchener</i>
PLEASE PHONE <i>295 5422</i>	<i>Mr Everett</i>
	<i>OT4</i>

The Rt Hon Paul Channon MP  
Secretary of State  
Department of Trade & Industry  
1/19 Victoria Street  
LONDON  
SW1H 0ET

14 April 1986

*Dear Secretary of State,*

EXPORTS CREDITS GUARANTEE DEPARTMENT: £5bn DEFENCE DEAL WITH SAUDI ARABIA

Thank you for sending me a copy of your letter of 25 March to Nigel Lawson.

I have doubts about the ECGD's proposal. As you say, it will be a massive commitment and will put Saudi Arabia in the top ten as far as exposure to individual countries is concerned. It hardly seems sensible to increase our exposure to Middle East, oil-exporting countries so dramatically when oil prices have just halved.

Saudi Arabia has a one-product economy. More than 95% of its export earnings come from oil. As you say, without painful readjustment, its liquid foreign assets could fall to zero by 1988. The Foreign Secretary says in his minute of 4 April that he is worried that this adjustment is not taking place quickly enough. I would add that we should not rely on Saudi Arabia's ability to make up for the fall in oil prices by increasing production. It is largely because the Saudis increased production last Autumn that prices have fallen so fast. Adjustment will be needed if their economy is not to face serious problems and, speaking personally, I am not quite as confident as the Foreign Secretary about the political stability of Saudi Arabia.

ECGD's experience of payment defaults, which led to the recent regrading of Saudi Arabia from A to B for premium charging purposes, and the possibility that the Saudis may refuse to pay interest because of Sharia law, are hardly encouraging.

I do not share the optimism as to the political stability during a period of oil recession.

I am copying this to the Prime Minister, members of OD and to Sir Robert Armstrong.

*Yours sincerely,*  
*Peter Walker*

*Mr PETER WALKER 8F/17/84*  
*(Approved by the S.O.S. and ...)*

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