

CONFIDENTIAL

SUBJECT cc MASTER



FILE
JA.
cpc

10 DOWNING STREET

LONDON SW1A 2AA

From the Private Secretary

13 July 1989

Dear Stepler.

PRIME MINISTER'S MEETING WITH THE PRESIDENT OF MEXICO

The Prime Minister had a talk with President Salinas at the Elysee Palace in Paris this afternoon. The President was joined cumulatively by the Mexican Foreign Minister, the Deputy Foreign Minister and A.N. Other in the course of the talk. The Prime Minister was most impressed with President Salinas and his approach to Mexico's economic problems.

The Prime Minister began by congratulating the President on his election and commiserating on the scale of the task which he faced. She recalled her earlier contacts with Mexico and expressed admiration for President de la Madrid. He had tackled Mexico's problems with immense courage, having to contend with national disasters on top of everything else. She understood that Mexico's negotiations with the commercial banks on debt were making progress, indeed were nearly complete.

President Salinas said he was pleasantly surprised to discover how closely the Prime Minister followed Mexico's affairs. He was determined to take whatever tough measures were necessary to put Mexico's economy to rights. He intended to carry out a major programme of privatisation and had substantially relaxed the rules governing foreign investment. Subsidies were being reduced. But to give his people hope he had to solve Mexico's debt problem. On this, he had done everything by the book. Mexico had been to the IMF and the World Bank and then to the Paris Club. He had also tackled inflation, bringing it down from 160% per annum to 17%. But to keep inflation down he not only had to pursue the right fiscal policy, he needed a reasonably stable exchange rate. This was why the negotiations with the commercial banks on debt were so important. There was now agreement on the discount rate of 35%; on the interest rate of 6½%; and on the amount of new money which Mexico needed. Everything turned on the banks' late request for a step-up provision. (The Prime Minister's recollection is that he blamed the British banks for this, but this was not my understanding.) They were insisting that if Mexico's economy improved over

CONFIDENTIAL

da

a number of years, then they should revert to current interest rates for debt repayment. While he was prepared to make adjustments if oil prices rose significantly, he simply could not accept a general step-up provision, for political reasons. He hoped very much that the British banks would attend the crucial meeting in New York on 14 July in a constructive spirit. He was worried by reports that they did not want to be part of an agreement, but to be free-riders. He hoped that he could look to the Prime Minister for help.

The Prime Minister said that she was very impressed with the measures which President Salinas was taking. We could not instruct the British commercial banks what to do: they had to form their own commercial judgement. She would take steps to enquire about the latest position. Personally, she would be surprised if they were to stand out against an agreement. President Salinas said he wanted to underline once more the enormous benefits that would flow from a settlement. Flight capital would return to Mexico and people would begin to believe that sacrifices were worthwhile and would lead to improvements. The meeting on 14 July was really crucial. He had seen Secretary Brady earlier in the day. He had confirmed United States interest in reaching a settlement. The Prime Minister repeated that she thought that what President Salinas was doing was marvellous. She would enquire about the position of the British banks and let him know how matters stood. If he could solve Mexico's economic problems, it would be an example for the rest of Latin America.

President Salinas referred to the problem of drugs. The Prime Minister said that we were anxious to conclude an agreement on confiscation of drug traffickers' assets.

President Salinas said that he hoped the Prime Minister would find time to return to Mexico.

I have reported the exchange on debt to Nigel Wicks, who has been in touch with the Treasury.

I am copying this letter to Alex Allan (HM Treasury), Neil Thornton (Department of Trade and Industry) and Trevor Woolley (Cabinet Office).

John Wicks,
Chris Jones

(C.D. POWELL)

Stephen Wall, Esq.,
Foreign and Commonwealth Office.