



10 DOWNING STREET

THE PRIME MINISTER

15 July 1980

Dear Ted,

Thank you for your letter of 12 June, and for sending me a note of your personal thoughts before the Venice Summit.

I think we all agreed with much of the analysis in your paper; and I do not doubt that the fact that we did so owed a good deal to the Brandt Report, and to what you yourself are doing to draw attention to the problems.

As you say, the scale of the problem following the latest round of oil price increases is tremendous. And it hits the poorest countries hardest. Many of them have reached or passed the limit of potential indebtedness. It is no use their piling up larger and larger debts; they have to have grants if they are to survive.

But, as Helmut Schmid said to us in Venice, the figures speak for themselves: for the oil-exporting countries a surplus of \$120 billion; for the industrialised countries a deficit of \$70 billion; for the non-oil developing countries a deficit of \$50 billion. There are limits to what the industrialised countries of the West, themselves with a deficit of \$70 billion, can do; and our own public expenditure constraints make it especially difficult for us to contemplate major new aid commitments. So the need is to convince the oil-exporting countries, not only that they have caused the problem and they alone have the resources on the scale that solutions will require, but

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also that it is in their own interests as well as the interests of the rest of us that they should contribute to the solutions on a much larger scale than they do at present.

One of the unsatisfactory aspects of the present recycling arrangements is that the industrialised countries mediate both the term and the risk of most of what the oil-exporting countries put up. Of course the international banks are used to doing this; it is the traditional role of the bank to borrow short and lend longer. But there are grave dangers - as you recognise - of the system becoming over-exposed, and a collapse could have catastrophic consequences. Helmut Schmidt in Venice insisted upon the need to ensure sound lending standards - even if it meant a greater degree of prudential supervision of the international currency markets - and this thought was reflected in our declaration.

We thought that the international banking system should have, and should be able to discharge, the primary role in recycling surpluses. But I agree with you that the scale of the problems is even bigger this time round, and it is not going to be possible to deal with it so easily as proved to be the case after 1973-74. The international financial institutions are going to have to play an increasing role - and we backed the current programmes for replenishing the institutions. We also encouraged the World Bank to think in terms of a new facility or affiliate, in which some of the oil-exporting countries might be persuaded to put money, and which would help the non-oil developing countries to improve energy conservation and develop alternative indigenous sources of energy. That could help them to develop their own sources of food production, which ought to be a first call on the resources available for development.

As to what the industrialised countries are doing on the energy front, we committed ourselves at Venice to programmes

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for reducing our consumption of oil, and for developing other energy sources - in the medium term mainly coal and nuclear, but looking in the longer term to renewable sources. This was not new: it drew together work which is being done in the International Energy Agency and other international bodies. But it was important that this programme of measures and policies was approved and endorsed by the needs of the seven Governments represented at Venice.

You will see from what I have said that we endorsed your views of the characteristics for which we should look in any initiatives that are taken to deal with this whole range of problems. Venice was not an occasion for discussing detailed initiatives; but the discussion there enabled us to reach general agreement on an approach to the problems, which was reflected in the declaration and which will be a framework within which policies and initiatives can be pursued.

(Signed MT)

The Rt. Hon. Edward Heath, MBE, MP.