



Foreign and Commonwealth Office

London SW1A 2AH

11 April 1989

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*Prime Minister*

*Dear Charles*

*Not exactly a sparkling  
dialogue by Balfour Beatty*

*00/11/6*

ATP Malaysia: Pergau Hydro-Electric Project

You will recall that, when she saw Dr Mahathir on 15 March, the Prime Minister informally conveyed the offer of a package of financial support for the off-shore portion of this project, with a grant element of 35%, up to a maximum of £68.25 million.

The ATP offer was based on an estimate by Balfour Beatty, the lead contractor, of UK and eligible EC content amounting to a maximum of £195 million and an overall contract price of £316 million. We had not intended making an aid offer until the consortium had final prices but there was very strong pressure from them for an early offer and we accepted, in good faith, their assurance that £195 million was a maximum figure.

After the offer had been made, Balfour Beatty submitted revised figures which showed a very large increase in cost. The contract is now expected to consist of UK and eligible EC content of £282 million, with an overall contract price of £397 million. The new figures would imply an ATP contribution of £98.7 million, some 45% more than the ATP offer already made. Balfour Beatty have acknowledged that the costs presented earlier had been on the basis that they were the maximum figures likely in practice.

At this increased cost the project no longer looks economically viable, since the provision of gas turbines would be a cheaper alternative means of meeting demand for electricity. The increased ATP requirement will put severe pressure on the ATP budget to the possible exclusion of other business. Despite this, it would be extremely difficult not to support the project if the UK consortium succeeds in its negotiations.

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We are therefore proposing to authorise our High Commissioner in Kuala Lumpur to send a further letter to the Malaysians which reaffirms the informal offer made by the Prime Minister (which for Consensus reasons cannot be openly acknowledged) while leaving open the option of a soft loan (with a 35% grant element) to fill the gap that might still exist after negotiations. We assume the Malaysians will be surprised at the extent to which the UK consortium's price exceeds the price estimates given in a 1988 feasibility study, and that they will be aggressive in negotiating for reductions. We are simultaneously instituting our own value for money investigation, which will be very rigorous and will, we hope, be ready within a few days. We shall be putting the conclusions of our investigation to the consortium, making it clear to them that we shall not be ready to provide aid at a level higher than is consistent with the findings of the investigation.

As Balfour Beatty now accept, their failure to provide us with accurate cost estimates at the time we were considering the case for aid for the project has placed us in a very difficult position. This is all the more regrettable in view of the pressure they exerted in order to get a quick and favourable decision on ATP support before the meeting last month of the two Prime Ministers. However we shall make every effort, particularly by means of our value for money investigation, to retrieve the situation as far as possible.

I am copying this letter to Neil Thornton (DTI) and Jonathan Taylor (HM Treasury).

*Yours sincerely*

*R N Peirce*

(R N Peirce)  
Private Secretary

C D Powell Esq  
10 Downing Street

MALAYSIA: Relations  
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