

PO-CH/NL/008

PART A

Part A.

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Begins: ¹³~~25~~ / 6 / 86
Ends: 20 / 2 / 87


PO -CH /NL/0081

PART A

Chancellor's (Lawson) Papers:

GROUP OF FIVE AND GROUP
OF SEVEN MEETING 1987

PO -CH /NL/0081
PART A

Disposal Directions: 25 Years

Andrew
27/7/95

June 13, 1986

Tokyo Summit Agreement:
Next Steps in Implementing
Closer Economic Policy Coordination

This memorandum outlines possible next steps in implementing the Tokyo Summit commitments on closer economic policy coordination based on the consensus emerging from the May 29 meeting of the G-5 Deputies. In particular, the memo outlines the roles that could be played by the IMF, Deputies and Ministers and possible topics for discussion at the initial round of meetings.

Role of the IMF

The IMF Managing Director has circulated a note to the Deputies discussing the role the Fund might play in closer economic policy coordination among Summit countries. In addition, an IMF staff paper on indicators relating to economic policy actions and performance has been issued for a July 14 Executive Board discussion. The staff paper responds to a request by the Interim Committee and is intended to improve the discussions of the world economic outlook by considering external imbalances, exchange rate developments and policy interactions in a medium-term framework. However, elements of the staff paper may well be relevant for the Tokyo exercise.

The Managing Director's note suggests that the IMF staff could:

- o compile the economic forecasts and projections based on discussions with national authorities;
- o help to assess consistency, particularly whether projections for current account "add up" across countries; and
- o provide an analytical framework to assess whether projections are compatible and sustainable.

The note also suggests that the role of the Managing Director in Ministerial meetings would be to explain where necessary the analytical background and implications for other countries of options for remedial action developed by the Deputies.

The IMF staff paper for the Executive Board discussion:

- o describes the types of indicators that would be used in considering economic policies and performance. The indicators suggested by the IMF staff are broadly consistent with those mentioned in the Tokyo communique (Tab A) although in some areas they are more specific in order to provide a more complete description;

- o presents a framework for assessing consistency and compatibility based on a reconciliation of country forecasts and an analysis of compatibility which focuses on the sustainability of external positions as determined by national savings and investment patterns.

Role of Deputies

There appears to be strong sentiment among the Deputies to use the IMF to prepare economic forecasts for each country and, possibly, to highlight the key issues concerning consistency and compatibility. These forecasts, as suggested by the Managing Director, would be based largely on consultations with national authorities. At the June 18 meeting, the Deputies could discuss issues relating to the role of the IMF posed by these papers including:

- o which of the IMF proposed indicators should be used in Fund prepared forecasts;
- o whether the framework for assessing consistency and compatibility described by the Fund for use in the World Economic Outlook should be applied in the G-5 exercise; and
- o who from the IMF would attend as a representative of the Managing Director at a September Deputies meeting.

The early September meeting of the Deputies could focus on:

- o the IMF forecasts, particularly situations where there may be disagreements with the Fund's projections;
- o the compatibility of the forecasts; and
- o the appropriate measures to resolve any problems.

Based on their discussion, the Deputies would prepare a paper for the Ministers which:

- o summarizes the IMF forecasts for the group, including where there are disagreements;
- o describes areas of inconsistency in national policies and incompatibilities in economic projections; and
- o presents the major questions of concern to the Deputies which required Ministerial consideration.

The IMF representative at the Deputies meeting would participate in the discussion of the forecast and perhaps assist in assessing the consistency and compatibility of the projections. However, it would be the responsibility of the Deputies themselves to address the key issues and undertake the preparations for the Ministerial meeting.

Ministerial meetings

The G-5 Ministers and Central Bank Governors could have their regular meeting at the time of the IMF/World Bank annual meetings but with multilateral surveillance as an agenda item. Based on the paper prepared by the Deputies, the meeting could:

- o review the procedures agreed by the Deputies for conducting closer economic policy coordination;
- o review the initial set of forecasts prepared by the IMF and discussed by the Deputies;
- o consider the need for and possible content of actions to deal with incompatibilities;
- o discuss the key areas of disagreement and concerns identified by the Deputies; and
- o agree on those policy areas and indicators that should be monitored closely in the ensuing period, presumably to serve as the focus of discussion at the next Ministerial meeting.

The IMF Managing Director would be invited to participate in the discussion and could submit a paper setting forth his

personal views on the key issues. The Ministerial discussion would be informal, off the record, and confidential.

A G-7 meeting could also be scheduled shortly after the G-5 autumn meeting. The purpose of this meeting would be to familiarize Italy and Canada with the procedures for economic policy coordination developed by the G-5 and to set a date for the annual G-7 exercise. The Finance Ministers might also discuss their economic forecasts and objectives in order to provide a basis for assessing subsequent performance.

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From: Sir G.Littler
Date: 17 June 1986

CHANCELLOR

*Thanks.
Muel
I agree with X & ✓
and the rest
of the rest. Save Y:
No just speak with
on this one. I think,
Frank*

- c.c. Sir P.Middleton
- Sir T.Burns
- Mr Lavelle
- Mr Fitchew
- Mr Sedgwick
- Mr Peretz
- Mr Scholar
- Mr Matthews

G5 DEVELOPMENTS

David Mulford's revised paper arrived yesterday. I attach a copy.

*mt, 2 thus s/s
86 @ N.K.-B
copy*

2. It offers a totally different approach from the earlier one, building on the ideas sketched by myself and Tietmeyer at our last meeting of G5 deputies, and is broadly acceptable. There are lurking difficulties over the choice and presentation of forecast data which may be published or at least leak, but I think we can cope with these problems, which are shared by some others.

X | 3. There is clearly no point in my offering a rival proposal at this stage. (My reading of the Mulford revision is that Baker wants to stay in the lead, but has accepted that his own first proposal commands insufficient support and has therefore decided to father something more acceptable).

4. We have also just received from the IMF a detailed paper on objective indicators which is their first draft of the results of the study commissioned at the Interim Committee. This also at first sight seems broadly on the right lines, but we need to go over the detail carefully.

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5. What I now propose is:

- to work tomorrow night with G5 colleagues on the Mulford draft and future arrangements; I shall report on my return after the week-end;
- to ask Mr Sedgwick to prepare detailed notes on the IMF paper, as a brief for Mr Lankester when the paper comes up for Board discussion in mid-July; we will report to you the main points when we have done more work on this;
- to continue working up a U.K. statement of how we see all this developing - for use as speech material; I shall let you have this next week; some of it might come in handy for the Zurich Kemp-Bradley conference.

yl



(Geoffrey Littler)

PS A

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From: Sir G.Littler
Date: 20 June 1986

MRS LOMAX

Handwritten notes:
on the 18th
date for G5 in
Paris
28/6

c.c. Sir P.Middleton
Sir T.Durns
Mr Lavelle
(Mr Fitchew)
Mr Sedgwick
Mr Peretz
Mr Scholar
Mr Matthews

G5 DEVELOPMENTS

Thank you for your minute of 18 June. This note covers further developments in which the Chancellor will be interested, mainly from a good meeting of G5 deputies on the evening of 18 June in Paris (incidentally the first with Gyohten instead of Ohba and he proved as expected a good contributor).

2. I shall be grateful for quick reactions to the question of dates for a meeting of G5 Ministers. (I am copying this minute and relevant earlier papers to the Governor and Mr Loehnis).

The Revised Mulford Proposals

3. These were generally welcomed, and none of us offered any dissenting comments on his paper. Instead we focussed on detailed procedural arrangements, and on the question of choice and use of indicators, with reference to the full IMF paper which has now been circulated.

G7 Arrangements

4. We all agree that there must be a G7 Ministerial Meeting in the margins of the Annual Meetings in Washington in September.

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Secretary Baker stands ready to issue invitations (following the G5 tradition of "local host"); but he is due to have a bilateral with Goria in Washington next month and has decided to wait for that, get Goria's agreement, and then issue invitations. We all agreed with Mulford's suggestion that the best slot would be the evening of Saturday, 27 September (the Interim Committee is on the Sunday and the Development Committee on the Monday).

5. However we noted a number of possible awkwardnesses:

- We all suspect that Ruding will try to mount a meeting of G10, probably on that Saturday, pursuing his attempt to make it a more important forum: there is not much sympathy for this as an addition to G7, but we saw no way of refusing.
- There is still a strong feeling (especially Germany) that Central Bank Governors should **not** be included in this kind of "routine" G7 meeting.
- There is also, as seen by the deputies, a problem over whether deputies should attend. We would all like to avoid setting up a G7 deputies group, and we think we can argue that there is no need; but we are conscious of the risk that some point comes up among G7 Ministers which prompts an Italian or Canadian suggestion that deputies be invited to consider it further which others might find it inconvenient to refuse! Mulford wanted Ministers to meet alone; Lebegue was horrified (his comments straight out of "Yes, Minister"; Tietmeyer then raised the special problem that for Germany any second seat at the

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table would be demanded by Bangemann (on the ground that he has a Summit role); Gyöhten said he had both the French and German problems in some degree; I said that I was sure the Italians, and probably the Canadians, would expect and want deputies present, and that we would have to take the risk that this would breed a separate group of deputies, while briefing our own Ministers to try to resist it. Mulford then said that at least the first G7 meeting might be Ministers alone, because only they could decide what their own procedure should be; but none of us was particularly impressed by this. He thought that Baker might pursue the question with Goria.

6. It is relevant to the last point that Sarcinelli was quite active just before and during our visit to Paris to try to mount a breakfast meeting of G7 deputies, and he readily persuaded Drabble of Canada to join his efforts. We were able to resist this on the quite genuine ground that there was no time available at which even a reasonable quorum could be found; I and one or two others also argued that there was no need, and that we should concentrate instead on getting our Executive Directors in Washington to keep informally in touch with each other for the discussion of the IMF paper on indicators in the Executive Board (Sarcinelli seemed to welcome that idea).

G5 Meetings

7. There is happily no remaining trace of Baker's pressure for a July meeting. But he does feel that there would be advantage in

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holding a full G5 Meeting early in September, and Balladur (as we heard during his visit to London) inclines to the same view on the condition that it can be in Europe. Balladur has offered to host in or near Paris.

8. The main reason is fear that time will prove to be far too compressed if we leave this until the main Washington gathering, and that there might prove to be great advantage in an interval for reflection and possible further work by deputies between the G5 Meeting and the G7 and other Washington meetings.

9. Without commitment we discussed dates and agreed to try out on our Ministers the two alternatives:

- early September would probably have to mean the weekend of 6/7 September, most likely Sunday, 7 September; the deputies would meet either 10 days before or, preferably, for two days immediately before; all in or near Paris;
- in Washington, probably on Friday 26 September, starting as early in the day as travel arrangements permitted; and the deputies would still reckon to meet earlier in the month, probably in Europe.

10. There was general agreement - with Tietmeyer, Gyohnten and myself the most pressing - that we should try to keep the meeting as quiet as possible (recognising that total secrecy is unlikely to be attainable), with no substantive announcements. Mulford seemed to accept this without reservation.

11. I should welcome the Chancellor's views on the dates.

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Indicators

12. There seemed to be a good spread of agreement on elements of the indicators suggested by the IMF. I led the discussion on this (and am grateful for helpful briefing from Mr Sedgwick after discussion with Sir Terence Burns). In particular I found very strong sympathy for rejecting forecasts of exchange rates or of interest rates or of unemployment, for giving no or low value to attempts at cyclically-adjusted fiscal data, and for focussing a good deal on key nominal variables.

13. The next round of discussion of this will be in the IMF Executive Board on the basis of the full IMF paper. Mr Sedgwick is working up a brief and will submit general comments when he has finished going through the (very extensive) IMF material.

Procedure for Analysis and Forecasting

14. Over-riding some rather plaintive but muted comments from Mulford, we agreed:

- that the IMF should be asked to prepare basic material for the G5 discussion;
- that they might wish to visit each country to check for broad agreement on their assessment, but that we would not set up a special multilateral group of experts;
- that somebody (probably Whittome) should join deputies for a meeting (early September) to go over the figures and assessments;
- that the meeting of deputies would seek to identify the problems and disagreements worth discussion by Ministers.

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Next Steps

16. We agreed that Mulford would be the immediate channel of communication with the IMF, to secure their cooperation in the arrangements for the September exercise. I am copying this to Mr Lankester in case the Managing Director wishes to consult us at all through him; but no need for him to take the initiative.



(Geoffrey Littler)

DATE OF
NEXT G5

5

SECRET

From: Sir G.Littler
Date: 7 July 1986

MR KUCZYS

c.c. Sir P.Middleton
Mr Lavelle
Mr Evans

POSSIBLE G5 MEETING

Although firm arrangements have not yet been made - and may not be made for several weeks - I think you ought to note as a firm probability in the Chancellor's diary the need for him to attend a G5 Ministerial meeting in or near Paris on Sunday, 7 September.

2. He may want you to accompany him. I shall be likely to be spending the previous two days in Paris with other deputies to prepare the ground for the Ministerial meeting. I would hope it would be possible for the Chancellor to travel out and back in the day, perhaps with recourse to a private plane.

3. The Governor would of course also be involved in the Sunday meeting. I am copying this minute to his Secretary.



(Geoffrey Littler)

FROM: H G WALSH

DATE: 16 December 1986

NOTE FOR THE RECORD

cc: PS/Chancellor
 PS/Economic Secretary
 Sir G Littler
 Mr Lavelle
 Mr Evans
 Mr Mountfield
 Mr Davis
 Ms Life

IDA 8

The following contributions were agreed in IDA Deputies in Rome yesterday for IDA 8, towards a final total of \$12.4 billion.

\$ million

| | <u>Original Contribution</u> | <u>Supplementary Contribution (15 December)</u> | <u>Total IDA 8</u> |
|-----------------------------|----------------------------------|---|------------------------|
| <u>G5</u> | | | |
| UK | 770.50 | 15 | 785.50 |
| Germany | 1322.50 | 50 | 1372.50 |
| Japan | 2150.50 | 450 | 2600.50 |
| US | 2875.00 | - | 2875.00 |
| France | 839.50 | - | 839.50 |
| Italy | 534.75 | 90.5 | 625.25 |
| New Zealand | 16.10 | 0.7 | 16.80 |
| Netherlands | 345.00 | 125.5 | 470.50 |
| Other IDA | 2646.15 | | 2646.15 |
| Switzerland (non-member) | | 165 | 165.00 |
| Total | 11,500.00 | 896.7 | 12,400 |

2. The ODA contribution will be absorbed within the ODA aid budget, including the supplementary element.

H. W.

H G WALSH

Thanks. I can't do ~~more~~ ^{more} of ~~you~~ ^{you} w/ ~~7th~~ ^{7th} @ all, & 1st half of ~~morning~~ ^{morning} (Wt must discuss @ Chou) ~~for~~ ^{for} v. diffcult. ~~NR~~ ^{NR}

CONFIDENTIAL

From: Sir G.Littler
Date: 9 January 1987

MR KUCZYS

c.c. Sir P.Middleton
Mr Lavelle
Mr Huw Evans

CONVERSATION WITH DAVID MULFORD

Mulford telephoned me last night - his main purpose being to try out on me the idea of a G5 (or G7) meeting earlier in February than 14/15, possibly the 7/8.

2. I said that I knew that one of the two days (I had forgotten which) was impossible for the Chancellor, and reminded him that in general February is not an easy month for the UK, as for Japan. I also took the opportunity of putting reservations to him about the whole idea. I did not mention the trade issue (I suspect the US would try to turn that argument to support their own wishes), but I reiterated that the Chancellor found the idea of a meeting which was public and not seen to be a clear success very unattractive. We spoke briefly of prospects for action by Germany: I suggested that Germany would probably want to choose its own form of announcement of any action, not letting it appear to be simply a response to US and other pressure; that in any case I was not sure that a meeting was necessary to stimulate German action, or to enable the US to exploit its value vis-a-vis Congress.

3. Mulford took note, and acknowledged also my point that further progress on "indicators" could be attempted by deputies without prior need for a further Ministerial discussion. But he

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added that Baker would be spending a day or two in Saudi Arabia around 1-3 February and was interested in the possibility of some useful talk in Europe on the way there or back.

4. I took the opportunity also of asking Mulford about the FT article of yesterday on US Treasury views on debt. He said he and Baker were very upset about this: the intention had been very carefully to point banks, regulators and general opinion towards the idea that some writing-down of values of outstanding loans would not be incompatible with continued future lending; the Washington Post (which I have seen only since this conversation) had carried an exaggerated story; they had worked hard in trying to correct this and were very annoyed that the FT had developed an even more exaggerated version. He assured me that there was no question of a new US initiative on debt being trailed.



(Geoffrey Littler)

SECTION OF REUTERS STORIES

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See X: Japanese
Attorney's Start
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CC
93.
Mr.
PS / CHANCELLOR 12/2
SIR. J. G. LITTLER.
MR. CASSELL.
MR. PERETZ -
MR. CULPIN.

0023 GMT

"A west European monetary official ruled out a meeting of the G5 - the US, Japan, West Germany, Britain and France - before next Sunday's German general elections. But one soon afterwards, was a possibility, he said. "

REAGAN TOLD NO IMMEDIATE HARM IN \$ FALL (0540 GMT)

"Washington, Jan 21 - the top advisers told President Reagan the \$ could continue to decline without any immediate harm to the US economy, but that a long term \$ fall could rekindle US inflation, the Washington Post said today. It quoted administration sources as saying aids including Reagan's Chief of Staff Donald Regan, and Council of Economic Advisers chairman Beryl Sprinkle gave that advice when Reagan asked yesterday when the \$'s fall would begin to hurt.

They told Reagan the \$ could continue to fall without hurting the US economy until the US trade deficit began to ease, the Post said. They told the President that after that point a continued fall in the \$ might be inflationary, the newspaper said."

JAPAN RATE CUT HINGES ON US HELP, BANK SOURCES (0546 GMT)

" Tokyo, Jan 21 - The Bank of Japan would need concrete assurances the US was willing to stabilise foreign exchange rate before it would be ready to consider a discount rate cut, central bank sources said. They also expressed doubts Finance Minister Miyazawa would be able to secure such concrete assurances during his talks today with US Treasury Secretary Baker. At the moment, the central bank has no plans to cut its 3% discount rate, the sources said, echoing comments made yesterday by

Bank of Japan Governor Sumita.

The assurances the Bank wishes to get from the US might include a promise of concerted intervention and other policy co-ordination amongst major industrial nations, the sources said. But they said the central bank does not consider market intervention by the US a pre-requisite for Japan to consider a discount rate cut. The Bank will welcome any assurances from the US that would be effective in bringing about currency stabilisation, they said. The central bank thinks it urgent to stabilise exchange rates because of possible adverse effects of a further Yen rise on the Japanese economy, they said. "

JAPAN MINISTER COMPLAINS OF US CURRENCY COMMENTS (0926 GMT)

"Tokyo, Jan 21 - Foreign Minister Kuranari said he wants US officials to stop commenting on currency rates because they make the foreign exchange market erratic a Foreign Ministry spokesman said. Kuranari complained to a meeting here of the Asian Affairs Research Council, a research group, that when US Treasury Secretary Baker makes any approving remark about the weak \$, it has an immediate effect on exchange rates, which the Japanese Government does not like, the spokesman said. Japan wants US officials to refrain from making such comments about currency rates, he quoted Kuranari as saying.

Finance Minister Miyazawa left today for Washington to discuss currency rates with Baker after the \$'s sharp fall this week. Kuranari said that because it looks impossible for the US, Japan and West Germany to discuss the currency problem, it is important to start separate two way discussions between Japan and West Germany and the US and West Germany on currency market intervention."

BANK OF JAPAN OFFICIAL WANTS G5 MEET SOON, KYODO (0930 GMT)

"Tokyo, Jan 21 - A high ranking Bank of Japan official was quoted by Kyodo News Agency as saying it is desirable that multi lateral consultations such as a meeting of the Group of 5 industrial relations, be held as soon as possible to bring about currency stabilisation. The official, who declined to be identified, told reporters the Bank plans no discount rate cut at the moment but said every effort is required to stabilise exchange rates, Kyodo said. Kyodo interpreted the statements as indicating the Bank will consider a cut in its 3% discount rate after today's Miyazawa-Baker meeting in Washington.

High ranking central bank officials, including Governor Sumita, had previously said the Bank did not have such a plan for the time being, Kyodo said. The official was also quoted as saying Japan wants the US to do its best to stabilise foreign exchange rates."

SIR G
LITTLE
→ MR A
ALLAN
2/1/87

pay.

(or warned
Baker when he
came to the meeting)

SECRET

From: Sir G.Littler
Date: 21 January 1987

MR ALEX ALLAN

Ch
We are trying
up a meeting next
week
AA

c.c. Sir P.Middleton
Mr Cassell
Mr Lavelle
Mr Huw Evans

G5, etc

You will have noticed a flood of rumours and denials in the last day or two about a possible G5 meeting (or even G3, but curiously not G7!). To the best of my knowledge there is still nothing planned for Ministers, and the difficulties of logistics over any February meeting still exist.

2. Miazawa is in Washington for talks with Baker. The US are very disappointed with what they now understand to be the content and impact (lack of impact) of the Japanese budget. Our analysis also suggests very little net impact. If the US are to consider joint action to stabilise the dollar, they will surely want more than a token Japanese interest cut to persuade them.

3. I should record that Drabble (my Canadian opposite number) telephoned me last night, his purpose to probe whether any meeting of Ministers was envisaged among G5. Baker is due in Ottawa this week, with Shultz and others, for bilaterals: the main item on the bilateral agenda will be trade questions, in which Baker seems now to be taking a prominent part. I told Drabble that there had been interest in December in the possibility of some meeting of Ministers around February, of unspecified composition, but for logistic and other reasons it had seemed to fade, and I knew of no Ministerial meeting being planned now.

SECRET

4. There will be a meeting of G5 deputies which I shall attend in Zurich on Thursday 29 January (I shall have to stay overnight but expect to be back in the office by lunch-time Friday). Our main agenda will be: current situation; and indicators exercise. Unless the Chancellor has other thoughts, I suggest my guidelines should be:

- treat the indicators exercise as secondary, with further work to be done by deputies aiming at agreed advice to Ministers in time for the April meetings in Washington; on substance I follow earlier Treasury discussions;
- on the current situation, I assume that the Chancellor still wants to avoid a February meeting and has genuine problems with several dates, and would still oppose the idea of a meeting on merits unless there is a clear and relevant outcome in sight; plainly the US, Japan and Germany are in the lead here; I cannot think it likely that the UK would be asked for substantive commitments (and certainly not for changes in policy).

5. My guess is that all G5 deputies will have instructions to report back before any commitment is even provisionally planned. We shall in any case all be meeting again the following Tuesday or Wednesday just before a Summit preparation meeting, and can therefore plan further early discussion in the light of reactions by Ministers to our first report.



(Geoffrey Littler)

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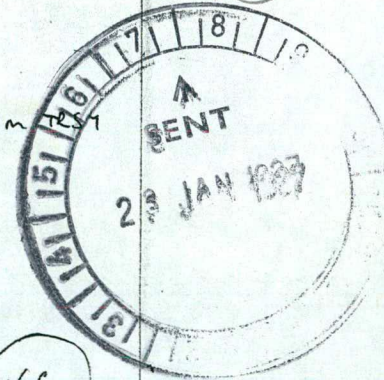
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SI G LITTLE
N H P EVANS
N GOODMAN

PS | GOVERNOR
N LOENNIS

Hm

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AND TO IMMEDIATE OTTAWA, BONN, PARIS, ROME, TOKYO, UKDEL OECD
AND TO IMMEDIATE UKREP BRUSSELS

US-JAPANESE STATEMENT ON EXCHANGE RATES

SUMMARY

1. BAKER/MIYAZAWA STATEMENT FOLLOWING UNSUCCESSFUL TALKS IN WASHINGTON ON JANUARY 21 DISAPPOINTS AS DOLLAR WEAKENS FURTHER. LATEST GNP FIGURES (FOR THE FOURTH QUARTER) ALSO A SETBACK.

DETAIL

2. THE FOLLOWING US/JAPANESE STATEMENT ON EXCHANGE RATES WAS ISSUED LAST NIGHT IN WASHINGTON.

BEGINS

THE JAPANESE MINISTER OF FINANCE, KIICHI MIYAZAWA AND THE US SECRETARY OF THE TREASURY, JAMES A. BAKER III, MET TODAY TO DISCUSS ECONOMIC, TRADE, AND FINANCIAL ISSUES OF MUTUAL INTEREST TO THEIR COUNTRIES.

BOTH MINISTERS STATED THEIR CONTINUED SUPPORT FOR THE UNDERSTANDINGS AND AGREEMENTS CONTAINED IN THEIR JOINT ANNOUNCEMENT OF OCTOBER 31, 1986. IN THIS CONNECTION, THEY AGREED TO CONTINUE COOPERATIVE EFFORTS TO STIMULATE GROWTH AND TO REDUCE EXTERNAL IMBALANCES.

SECRETARY BAKER AND MINISTER MIYAZAWA AGREED THAT DEVELOPMENTS IN EXCHANGE MARKETS WARRANT MONITORING. THE MINISTERS EXPRESSED THEIR VIEW THAT DURING MOST OF THE PERIOD SINCE OCTOBER 31, 1986, THE YEN/DOLLAR EXCHANGE RATE HAS BEEN BROADLY CONSISTENT WITH UNDERLYING FUNDAMENTALS, ALTHOUGH THERE WERE RECENT INSTANCES OF TEMPORARY INSTABILITY IN EXCHANGE MARKETS. ACCORDINGLY, THE MINISTERS REAFFIRMED THEIR WILLINGNESS TO COOPERATE ON EXCHANGE MARKET ISSUES.

BOTH MINISTERS AGREED THAT IN ORDER TO PROMOTE GLOBAL GROWTH, REDUCE IMBALANCES AND PROMOTE OPEN MARKETS, CLOSER COORDINATION OF ECONOMIC POLICIES AMONG ALL MAJOR INDUSTRIAL COUNTRIES IS CRITICAL. TOWARD THIS END, THEY AGREED TO INTENSIFY CONSULTATIONS WITH OTHER MAJOR INDUSTRIAL COUNTRIES.

ENDS

3. MIYAZAWA HELD A PRESS CONFERENCE BUT, ACCORDING TO REPORTS, WOULD NOT BE DRAWN ON WHETHER THE TWO GOVERNMENTS HAD AGREED TO INTERVENE JOINTLY IF THE DOLLAR FELL FURTHER. THE STATEMENT ITSELF REFERRED ONLY TO "RECENT INSTANCES OF TEMPORARY INSTABILITY IN EXCHANGE RATES" AND REAFFIRMED US/JAPANESE "WILLINGNESS TO COOPERATE ON EXCHANGE MARKET ISSUES". THE EMPHASIS ON THE NEED FOR FURTHER INTERNATIONAL COOPERATION AND "INTENSIFYING CONSULTATIONS WITH OTHER MAJOR INDUSTRIAL NATIONS" WAS WIDELY INTERPRETED AS A SIGNAL THAT A G5 MEETING IS IMMINENT.

4. US TREASURY OFFICIALS AND THE FED HAVE BEEN TIGHT-LIPPED ABOUT THE IMPLICATIONS OF THE STATEMENT. BUT DALLARA (US

IMMINENT.

4. US TREASURY OFFICIALS AND THE FED HAVE BEEN TIGHT-LIPPED ABOUT THE IMPLICATIONS OF THE STATEMENT. BUT DALLARA (US EXECUTIVE DIRECTOR AT THE IMF) TOLD US THAT THERE WAS "NOT MUCH BEHIND IT" AND THAT SECRETARY BAKER HAD NOT BEEN PREPARED TO DO ANY SERIOUS DEAL WITH MIYAZAWA IN THE ABSENCE OF ACTION BY THE JAPANESE TO STIMULATE THEIR ECONOMY. IN THIS CONNECTION HE DESCRIBED JAPAN'S 1987 BUDGET AS A "REAL DOWNER": IN TREASURY'S VIEW IT AMOUNTED TO FURTHER FISCAL CONSOLIDATION WHICH WAS TOTALLY INAPPROPRIATE IN THE FACE OF THE CONTINUING MASSIVE CURRENT ACCOUNT SURPLUS.

5. THE FOREIGN EXCHANGE MARKET REACTED BADLY TO THE STATEMENT, WITH THE DOLLAR FALLING HEAVILY AGAIN TODAY AGAINST THE YEN AND THE DEUTSCHEMARK. EXPECTATIONS HAD BEEN THAT SOME DEAL--PERHAPS INVOLVING A JAPANESE PLEDGE TO CUT INTEREST RATES AND RELAX FISCAL POLICY IN RETURN FOR A US COMMITMENT TO INTERVENE IN THE MARKETS--WOULD BE STITCHED TOGETHER. THE DOLLAR WAS ALSO AFFECTED BY THE RELEASE OF DISAPPOINTING (PRELIMINARY) GNP FIGURES SHOWING REAL GROWTH IN Q4 OF ONLY 1.7 PER CENT (COMPARED WITH EXPECTATIONS OF 2.5 PER CENT OR HIGHER). FOR 1986 AS A WHOLE, GROWTH IS NOW PUT AT 2.5 PER CENT. THE FIGURES PERPLEXED MANY ANALYSTS BECAUSE, AS COMPARED WITH THE THIRD QUARTER, THEY SHOW AN IMPROVEMENT IN NET EXPORTS AND A DECLINE IN REAL CONSUMER SPENDING, WITH THE MAIN GROWTH AREAS BEING GOVERNMENT SPENDING AND RESIDENTIAL INVESTMENT. THE HUGE MERCHANDISE TRADE DEFICITS IN OCTOBER AND NOVEMBER, WITH SECRETARY BAKER HAVING HINTED THAT THE FIGURE FOR DECEMBER WILL ALSO BE BAD, MAKE THE NET EXPORT IMPROVEMENT LOOK ODD. AND THE DROP IN CONSUMER SPENDING IS A PUZZLE IN VIEW OF THE EVIDENCE THAT CONSUMERS WERE BRINGING FORWARD EXPENDITURE TO OBTAIN SALES TAX DEDUCTION BEFORE THE NEW TAX LAW COMES INTO EFFECT. DOWNWARD REVISION OF THE GNP FIGURE IS A POSSIBILITY, SHOULD THE Q4 TRADE BALANCE TURN OUT TO BE WORSE THAN ASSUMED.

6. THE CUT IN THE GERMAN DISCOUNT RATE SEEMED TO HAVE LITTLE EFFECT THE OTHER WAY, PARTLY BECAUSE OF DOUBTS WHETHER IT REALLY CONSTITUTED ANY GENUINE LOOSENING OF POLICY. (DALLARA ALSO MENTIONED TREASURY'S CONCERN ON THIS ACCOUNT.) IN ADDITION, THE MARKET WAS UNSETTLED BY VOLCKER'S FAILURE TO TAKE A STRONGER LINE ON THE DOLLAR IN TESTIMONY YESTERDAY BEFORE THE SENATE BANKING COMMITTEE. VOLCKER SOUGHT TO SMOOTH OVER RECENT DIFFERENCES BETWEEN HIMSELF AND HIS ADMINISTRATION, REITERATING EARLIER STATEMENTS THAT THE DOLLAR WAS REASONABLY CLOSE TO WHAT HE REGARDS AS A COMPETITIVE LEVEL AND THAT "CONTINUED DEVALUATION CANNOT BE A POLICY IN ITSELF" WITHOUT FURTHER EFFORTS BY THE US (BUDGET DEFICIT) AND OTHER COUNTRIES (FASTER GROWTH) TO ADJUST.

7. FCO PLEASE ADVANCE TO PS/CHANCELLOR, SIR G. LITTLER, H.P. EVANS AND GOODMAN (TREASURY), PS/GOVERNOR AND LOEHNIS (BANK OF ENGLAND), AND RICHARDSON (ERD).

ACLAND

YYYY

ORWBAN 9063

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CN RIM023

231451 :EYSKENS CALLS FOR G-5 MEETING ON DOLLAR

BRUSSELS, Jan 23 - Belgian Finance Minister Mark Eyskens called for Group of Five finance ministers to hold a meeting aimed at controlling what he called the "brutal" fall in the dollar.

In a communique, Eyskens, current president of the European Community's council of finance ministers, proposed the EC should also be represented at the talks.

Eyskens at the same time urged European countries not to follow the lead of West Germany in lowering interest rates, at least for the time being, in order to allow the mark to ease and stabilise.

MORE

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CN RIM051

231516 :EYSKENS CALLS =2 BRUSSELS

A finance ministry spokesman said there had been no official contacts between Eyskens and G-5 finance ministers regarding his call. But the spokesman said it was possible there would be contacts after Sunday's West German elections, depending on how the dollar fared on exchange markets.

Eyskens drew a parallel between the proposed meeting and the 1985 New York Plaza Hotel talks that resulted in a G-5 accord to push down the then-overvalued dollar. "This time the situation is not the same because it would be a question of controlling the brutal fall in the dollar," he said.

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CN RIM055

231517 :EYSKENS CALLS =3 BRUSSELS

He described yesterday's half-point cut in West Germany's discount and Lombard rates as courageous and said it would help reinforce monetary stability within and outside the EC.

But he added he remained convinced that the stability of the European Monetary System depended on the dollar stabilising.

He appealed to other European countries "that they refrain, at least in the near future, from reducing their interest rates with the aim of allowing the mark to evolve downwards and stabilise." Mark strength as investors switched funds out of the falling dollar was one of the factors that forced a three pct revaluation of the German currency in the EMS two weeks ago.

MORE

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CN RIM066

231525 :EYSKENS CALLS =4 BRUSSELS

The finance ministry spokesman said Eyskens saw no contradiction between his call for interest rates to be maintained and a slight reduction in the Belgian National Bank's key three-month treasury certificate rate earlier today.

He quoted Eyskens as saying the 0.15 point reduction in the rate, to 7.75 pct, represented a "normalisation" back to levels seen before the EMS realignment and could not be considered as a cut.

REUTER

Ch
No doubt
egged on
by Delors
AA

CHANCHICOR 12/2
pay ✓

Broadly
unchanged

PPS/CHANCELLOR

12/2

page

231533 :/WEST GERMANY EXPECTS LITTLE FROM ANY G-5 MEETING

BONN, Jan 23 - The West German government would not expect any significant results from a meeting of Finance Ministers from the Group of Five (G-5) countries, a spokesman for the Finance Ministry said.

He was answering questions after Belgian Finance Minister Mark Eyskens called for a G-5 meeting aimed at controlling what he referred to as the "brutal" fall of the dollar.

The spokesman quoted Finance Minister Gerhard Stoltenberg as saying no great expectations should be attached to a G-5 meeting if one were to take place. At the moment, no such G-5 round was planned, he added.

MORE

231535 :/WEST GERMANY EXPECTS =2 BONN

Official sources added West Germany would probably not refuse to take part in any G-5 discussions, despite Bonn's scepticism about whether they would produce concrete results as far as the dollar was concerned.

REUTER

*I agree with Balladur's line - pup
viz that (i) it is essential that Miyazawa & there is a person
(ii) that outcome must be pre-arranged.*

SECRET

From: Sir G.Littler
Date: 23 January 1987

MR ALEX ALLAN

Ch

G5, etc

*Lebegue also rang
Geoff to say Balladur's
line is that it is essential that
Miyazawa is present in person, but
subject to that he is minded
to agree - though he takes
you point that we
need to be
clear & advance
what outcome
shd be -
AA*

c.c. Sir P.Middleton
Mr Lavelle
Mr Evans

Attached is the text of the statement issued by Baker/Miyazawa in the early hours of 22 January. Public comment by the two sides has been very limited and has done nothing to change the disappointing sense of nothingness in the statement. Privately one of the US team told our people in Washington that there was "nothing much behind it".

2. However, Tim Lankester was asked by Dallara (Mulford's aide) to pass on a message to me "that Baker and Miyazawa had agreed that it would be highly desirable, in view of recent exchange rate developments, for the G5 Ministerial to go ahead". I shall try to contact Mulford later today.

3. Your minute of yesterday referred to Japanese references to talks between Japan and FRG and between US and FRG as a way of starting a G3. My reading is that the Japanese are prepared to try any route that might prevent a further rise of the Yen. It is possible that they have calculated that G3 is the best route - it is certainly true that only the three can take substantive action in support. In terms of supporting argument they might well look to France to share the objective of avoiding further depreciation of the US dollar and not count on the UK to be much of an ally.

Geoffrey Littler
(Geoffrey Littler)

BAKER/MIYAZAWA STATEMENT: 22 Jan 1987

The Japanese Minister of Finance, Kiichi Miyazawa, and the US Secretary of the Treasury, James A. Baker III, met today to discuss economic, trade and financial issues of mutual interest to their countries.

Both Ministers stated their continuing support for the understandings and agreements contained in their joint announcement of October 31, 1986. In this connection, they agreed to continue cooperative efforts to stimulate growth and to reduce external imbalances.

Secretary Baker and Minister Miyazawa agreed that developments in exchange markets warrant monitoring. The Ministers expressed their view that during most of the period since October 31, 1986, the Yen/Dollar exchange rate has been broadly consistent with underlying fundamentals, although there were recent instances of temporary instability in exchange markets. Accordingly, the Ministers reaffirmed their willingness to cooperate on exchange market issues.

Both Ministers agreed that in order to promote global growth, reduce imbalances and promote open markets, closer coordination of economic policies among all major industrial countries is critical. Towards this end, they agreed to intensify consultations with other major industrial countries.



Ch

G5 - bad news

Spring 1974.
of Baker -
my wife, I will
my husband
Mon, I
think.
at

Mulford rang Geoff. Mugazawa definitely prepared to come to Europe for a meeting. They want G5 dinner on 7th Feb, G7 lunch on 8th Feb.

Geoff said 7th Feb impossible for you; could just do 8th (but presumably only if G5 - don't want to miss G5, join G7).

Geoff repeated line that meeting pointless ^{or worse} unless we had worthwhile outcome stitched up in advance.

It is possible Baker may try to ring you over the w/e —

though his office have not rung
us tonight to fix anything up.
Do you want ring him? If
so Tony or I (*) will try &
fix it up — or can do it
on Monday.

Geoff is trying to urge
postponement to 14/15 or later
(also on grounds that need too
rushed to get anything agreed
by 7/8).

AA

(* I shall be on — or contactable at
~~0420-23195~~ 0420-23195
most of the weekend).

SECRET

From: Sir G.Littler
Date: 23 January 1987

MR ALEX ALLAN

c.c. Sir P.Middleton
Mr Lavelle
Mr Cassell
Mr Huw Evans

G5, G7, etc

You might find it useful to have a note of my diary over the next fortnight, in relation to possible G5/G7 developments:

- Thursday, 29 January: early morning flight for meeting of G5 deputies beginning 1 p.m. at Dolder Grand, Zurich;
- Friday, 30 January: breakfast meeting before we disperse; I should be back in the office by 2 p.m.;
- Tuesday, 3 February: early afternoon flight for Rome and seeing our Ambassador that night;
- Wednesday, 4 February: meeting of G7 deputies at Grand Hotel, Rome, until about 4-30 p.m. when we all fly on together to Florence;
- Thursday, 5 February: Florence for meeting of sherpas;
- Friday, 6 February: sherpas continue until lunch; I shall not be back in London (home, I hope) until about 8 p.m.

2. Ellen Miller will have my telephone numbers. I shall phone in to you if it seems sensible from Zurich/Rome/Florence, and in any case debrief on return (I assume I should be able to contact your office here after 8 p.m. on 6 February).

3. ECOFIN is scheduled for 9 February and the Chancellor hopes to avoid going. This is fine as far as the agenda is concerned. I have already suggested to Mr Kuczys that you should bear in mind the (I hope remote) possibility that the occasion might be one for Stoltenberg, Balladur and the Chancellor to talk to each other, if there seemed to be good reason.



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CN RIM497

262337 :/BAKER SAYS NO PRESENT PLANS FOR G-5 TO MEET

WASHINGTON; Jan 26 - Treasury Secretary James Baker said there are no present plans for a Group of Five meeting in Paris on February Seven.

Asked on the McNeil-Lehrer News Hour, broadcast on U.S. public television, about reports that such a meeting was likely, Baker replied that the Reagan administration did not comment on reports that a meeting was likely.

"But as we sit here tonight, there are no present plans for such a meeting," Baker said.

REUTER

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CN RIM544

270204 :/MIYAZAWA SAYS G-5 MEETING DATE IS STILL UNCERTAIN

TOKYO, Jan 27 - Japanese Finance Minister Kijichi Miyazawa said a date for a possible meeting of finance ministers from the Group of Five (G-5) is still uncertain.

But he told a press conference Japan has already been negotiating with West Germany to hold such a meeting as he particularly wants to speak with West German officials.

He added that he was not sure how West Germany will respond, as it just held elections on Sunday.

Japanese and U.S. press reports have suggested the G-5 may meet in Paris on February 7.

REUTER

*So much for
his hope
meeting*

CN RIM561

270245 :/G-5 COULD MEET EARLY NEXT MONTH, MONETARY SOURCES

By Peter Torday, Reuters

WASHINGTON, Jan 26 - The Group of Five leading industrial nations could meet early next month to resolve their differences over economic policies and currencies, but monetary sources said a final decision is days away.

"It's a good assumption," said one source when asked if finance ministers and central bankers of the United States, Japan, West Germany, Britain and France would meet soon.

But Treasury Secretary James Baker said in a television interview that there are no plans for such a meeting at present.

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CN RIM562

270246 :/G-5 COULD MEET =2 WASHINGTON

Baker declined to comment on the likelihood of a G-5 agreement to meet, but added, "As we sit here tonight, there are no present plans for such a meeting."

In Tokyo, Japanese Finance Minister Kiichi Miyazawa said a date for a G-5 meeting is still uncertain, but he told reporters that Japan has been talking with West Germany on holding such a meeting as he particularly wants to speak with West German officials.

At issue are near-crisis conditions in foreign exchange markets, where the rapidly falling dollar threatens the economies of Japan and West Germany.

MORE

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CN RIM563

270247 :/G-5 COULD MEET =3 WASHINGTON

Policymakers here also say that a further major decline could hurt the U.S. economy badly. But so large are the differences between the three major economic powers, the U.S., Japan and West Germany, that few sources expect a meeting, if one is called, to have a positive outcome.

"I don't know what they could usefully do," said one source. "It could be bad for the markets, these things have to be prepared carefully," said another.

Baker has expressed public concern about the dollar's continued sharp fall several times in the last few days.

MORE

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CN RIM565

270251 :/G-5 COULD MEET =4 WASHINGTON

Baker said in one television interview: "There can be problems if the dollar falls too fast, and we don't want to see it fall too much because it's counterproductive to achieving growth from our other trading partners."

He said he expects further measures from West Germany, in addition to its recent discount rate cut, and also from Japan. But the U.S. needs to take economic action too, he said, and mentioned redressing the U.S. budget deficit.

A Japanese television report said a G-5 meeting will take place in Paris on February 7. Baker will end a visit to Saudi Arabia on the sixth and could stop off in Paris on his return.

MORE

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CN RIM566

270252 :/G-5 COULD MEET =5 WASHINGTON

But a U.S. Treasury spokesman declined to comment on reports of an imminent G-5 meeting.

For the last two years, the G-5 has met early in the year for the first of three or four meetings a year.

If the G-5 does meet on February 7, it would follow a February 4-6 gathering of top officials in Florence to prepare for June's seven-nation economic summit.

Several G-5 deputies will attend the Florence meeting, where representatives from Italy and Canada join their counterparts from the Five, and it is possible some of the same issues will be raised.

MORE

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CN RIM568

270257 :/G-5 COULD MEET =6 WASHINGTON

But West Germany, whose centre-right coalition has just been returned to power, may not be ready to bring forward planned tax-reform measures, including a 22 billion dlr tax cut, by the time a G-5 meeting takes place.

In the past two weeks the dollar has fallen so sharply that West Germany was forced to act, taking the upward pressure off its already strong currency and stimulating the economy.

Hans Tietmeyer, Secretary of State for Finance, went to Washington to explain the 1/2 point cut to three pct in the German discount rate, monetary sources said.

MORE

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CN RIM569

270259 :/G-5 COULD MEET =7 WASHINGTON

But the normally stimulative move was accompanied by a tightening in German banks' monetary reserves, an action that usually offsets stimulus. Tietmeyer's talks were inconclusive, monetary analysts said.

Similarly, when Japanese Finance Minister Kiichi Miyazawa and Baker discussed the currency crisis, the absence of firm action proved bad for the markets and the dollar fell again.

Several sources said that even if the Five do agree on a meeting in February, it is unlikely to result in action. Instead, rather like last January's G-5 meeting in London, it could prepare the way for later action.

MORE

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CN RIM570

270259 :/G-5 COULD MEET =8 WASHINGTON

The sources said that by the time a scheduled meeting is held in April, ahead of the meeting of the International Monetary Fund, conditions may be ripe for a G-5 agreement.

The U.S. trade deficit may begin to fall, a pact with Congress on reducing the budget deficit may be near and West Germany and Japan may be readier to stimulate their economies, they said.

REUTER

SECRET

mp

From: Sir G.Littler
Date: 26 January 1987

MR ALEX ALLAN

c.c. Sir P.Middleton
Sir T.Burns
Mr Cassell
Mr Lavelle
Mr Huw Evans

G5,etc

Lebegue telephoned me this morning - a little apologetically as he knew from my talk with him last week that his message would not be welcome. Tietmeyer also telephoned a little later.

2. Both said that Baker and Miyazawa are now pressing very hard for a Ministerial meeting as early as possible, are very ready to come to Europe for it, and want the weekend of 7/8 February (the following weekend is apparently very inconvenient for Baker and impossible for Miyazawa). Subject to an important condition Stoltenberg and Balladur are willing to accept 7/8 February (even though the latter would have to postpone a visit to Algeria in order to do so).

3. The condition is that neither will agree to a meeting if they do not have good assurance that there will be a positive and useful outcome. Therefore at present neither is prepared to do more than reserve the date provisionally; both intend to take stock after the meeting of deputies in Zurich on 29/30 January, discuss together and with you in the light of our reports of that meeting and only then make a definite decision.

SECRET

4. However, both Lebegue and Tietmeyer are evidently becoming persuaded in favour of a meeting. The carrot Baker is holding out to them is "Plaza 2" - designed to stabilise exchange rates at the present levels (or at least avoid a further decline of the dollar) and with Baker committing the US to join in intervention to keep these levels.

5. To both I repeated that the Chancellor has a real problem over the date, such that late morning of 8 February would be the earliest he could be in Paris, and that he continues to have great reservations over the risks of an unsuccessful meeting. Lebegue simply noted this and reiterated that Balladur also would not want a meeting unless the prospective outcome was helpful. Tietmeyer said that Stoltenberg could accept a slightly later date, to give more time for preparation and confidence over the outcome. He also talked about 7/8 February timing. Stoltenberg's preference would be for a G5 only - in which case it would suffice to begin at, say, lunch-time on 8 February. But he recognises the problem of seeking an agreement on exchange rates without Italy and Canada, given the history of the argument. He then insists that time be made for a sufficiently full G5 discussion before the other two join in. This forces him to look for an evening and a morning of G5 before a G7 starting perhaps at 3 p.m. on Sunday.

6. I said I would discuss with you and promised both that I would contact them again.



(Geoffrey Littler)

SECRET

*Thanks. I want
intelligence. 13/14
w/ further
w/ suit
w/*

From: Sir G. Littler
Date: 27 January 1987

MR ALEX ALLAN

TELEPHONE CONVERSATION WITH GYOHTEN

My Japanese opposite number telephoned as arranged at 8 a.m. our time today, just before leaving for the airport en route for the meeting of deputies later this week.

2. I explained our two problems over the idea of an early G5 meeting: concern to avoid a meeting with great expectations and an inadequate result; and impossibility for the Chancellor of 7 Feb. Ad hominem on the first point I said that I personally doubted whether the US would offer reliable exchange rate cooperation (if at all) unless they got new substantive economic action from Japan and Germany as part of the package.

3. Three points from Gyohten:

- he said that Miyazawa was keen to have a meeting but strictly on the conditions that others agreed and that it could be of real value; and he wanted to hear how the exchanges among deputies go later this week before any decision is reached;
- he insisted that the press talk about date and venue did not emanate from the Japanese who, he claimed, had been very reticent on the subject (he was very worried about this; it was his first remark and he repeated it later - he could well be right and the source the US Treasury, perhaps mixed up with Baker's plans to visit Riyadh);

SECRET

- on dates Miyazawa's position is constrained by the diet session on the budget, which he cannot escape readily, or without permission from the diet which forces him to make explanations; there could, however, be a window through the combination of days when the diet does not sit (the two Sundays, 8 and 15 Feb, and Weds 11 Feb which happens to be a holiday) and - if it can be arranged - a run of three or four "public hearings" days from which the Minister is exempted and which the MOF are trying to stage in the 8-15 Feb period; Gyohten confirmed that 14/15 Feb are not possible for Miyazawa, but added that 13/14 could be (i.e. dinner on Friday night and finish on Saturday night so Miyazawa could be on deck in Tokyo again by the Monday).

Diary is free.

4. Finally, Gyohten said he would report our talk to his Minister's Secretary before leaving Tokyo (as we knew the Minister is out of town at a funeral). I have not asked the Japanese Embassy here or Gyohten to try again to fix a telephone call for the Chancellor to talk to Miyazawa.



(Geoffrey Littler)

CONFIDENTIAL

GRS 480

CONFIDENTIAL

FM ROME

TO DESKBY 271400Z FC0

TELNO 062

OF 271220Z JANUARY 87

AND TO DESKBY 271400Z HM TRÉASURY

INFO PRIORITY WASHINGTON, TOKYO, PARIS, BONN, OTTAWA,

INFO PRIORITY IMF/IBRD, UKDEL OECD, UKREP BRUSSELS

Prohibit
As you must have
Don't
have a clear
ambition to
Italy/UK
GAP comparison

MY TELNO 772 OF 29 DECEMBER 1986 (NOT TO ALL): G5/G7.

SUMMARY:

1. ITALY EXPRESSES STRONG CONCERN ON THE POSSIBILITY OF A MEETING OF G5 EXCLUDING ITALY AND CANADA IN EARLY FEBRUARY.

DETAIL:

2. THERE HAVE BEEN INTERMITTENT RUMOURS IN THE ITALIAN PRESS THIS MONTH OF A POSSIBLE G5 OR G7 MEETING IN VIEW OF THE CONTINUING DEPRECIATION OF THE DOLLAR, THE EMS REALIGNMENT, THE MEETING IN NEW YORK BETWEEN JAPANESE AND US TREASURY MINISTERS AND THE GERMAN MOVE ON INTEREST RATES. TODAY'S PAPERS CARRY FRONT PAGE STORIES THAT THE JAPANESE MINISTER MIYAZAWA HAS ASKED FOR A G5 MEETING AND THAT, DESPITE OTHER FINANCE MINISTRIES' REFUSAL TO COMMENT, SUCH A MEETING IS LIKELY IN PARIS ON 7 FEBRUARY OR POSSIBLY SHORTLY AFTERWARDS IN NEW YORK.

3. THE CANADIAN PRIME MINISTER MULRONEY WAS YESTERDAY IN ROME ON A VISIT WHICH WAS, ACCORDING TO THE CANADIAN EMBASSY, ARRANGED SOME THREE WEEKS AGO. FOLLOWING HIS DISCUSSIONS WITH CRAXI, CRAXI'S OFFICE YESTERDAY ISSUED BRIEFING TO THE PRESS CONDEMNING ANY MEETING ON EXCHANGE RATE PROBLEMS WHICH EXCLUDES ITALY AND CANADA. CORRIERE DELLA SERA SAYS THE TONE OF THE STATEMENT WAS PARTICULARLY FIRM. CRAXI'S DIPLOMATIC ADVISER BADINI SAID THAT A G5 MEETING WOULD CONSTITUTE A VIOLATION OF THE UNDERTAKINGS ENTERED INTO AT TOKYO SUCH AS TO INVALIDATE THE CREDIBILITY OF THE HEADS OF GOVERNMENT WHO SUBSCRIBED TO IT. ACCORDING TO THE JOINT COMMUNIQUE REPORTED IN THE PRESS CRAXI AND MULRONEY AGREED THAT THE CURRENT SITUATION WAS OF JUST THE KIND WHICH THE TOKYO AGREEMENT ENVISAGED SHOULD OCCASION A MEETING OF THE SEVEN. MULRONEY IS SAID TO HAVE ADDED TO JOURNALISTS THAT THIS DID NOT MEAN PROPOSING THE ABOLITION OF THE GROUP OF 5 WHICH HAS A PARTICULAR AND IMPORTANT ROLE. BUT THE POSITION OF ITALY IS MORE CLEAR CUT. CRAXI WILL PROTEST OFFICIALLY IF ITALY IS EXCLUDED. IL GIORNALE, THE MILAN DAILY, UNEQUIVOCALLY DESCRIBING CANADA AND ITALY AS RESPECTIVELY THE 7TH AND 5TH WESTERN ECONOMIC POWERS, SAYS THAT THE ITALIANS WOULD NOT MIND A MEETING OF THE THREE (UNITED STATES, JAPAN AND GERMANY) SINCE THEY ARE THE MOST DIRECTLY CONCERNED IN CURRENT MONETARY MOVEMENTS BUT THAT THERE IS NO PLACE FOR A MEETING OF

PPP
division
again

CONFIDENTIAL

THE

We clearly must send a line to take to Embassy in Rome - Steve Matthews had already sent copy of briefing to FCO, I have asked her to make sure it gets to Rose as well.

CONFIDENTIAL

THE 5 AS SUCH. LA STAMPA AFFIRMS THIS NEITHER CRAXI'S OFFICE NOR THE TREASURY CAN BELIEVE THERE WILL BE SUCH AN AFFRONT TO ITALY, PARTICULARLY NOW THAT SHE HAS OVERTAKEN BRITAIN AS THE FIFTH INDUSTRIAL POWER.

COMMENT:

4. I DO NOT KNOW WHETHER AN ANSWER HAS BEEN SENT TO THE ITALIAN TREASURY MINISTER GORIA IN REPLY TO HIS MESSAGE TO THE CHANCELLOR OF THE EXCHEQUER OF 23 DECEMBER, TRANSMITTED IN TUR. SEEN FROM HERE, IF IT IS INDEED THE INTENTION TO HOLD A MEETING OF 25 IT WILL BE NECESSARY TO RESPOND QUICKLY TO ITALIAN CONCERN IF THE ATMOSPHERE OF THE FORTHCOMING ANGLO-ITALIAN SUMMIT, AND PERHAPS THE VENICE ECONOMIC SUMMIT LATER THIS YEAR ARE NOT TO BE IMPAIRED.

I HAVE AN APPOINTMENT WITH CRAXI'S DIPLOMATIC ADVISER AT 1600Z ON 28 JANUARY AND WOULD WELCOME ANY GUIDANCE YOU CAN GIVE ME AS I SHALL CERTAINLY BE ASKED ABOUT OUR PLANS.

BRIDGES

YYYY

RFHPAN 4389

LIMITED

ERD

WED

NAD

FED

PLANNING STAFF

PS

PS MRS CHALKER

PS/PUS

MR THOMAS

MR BRAITHWAITE

MR MAUD

MR WATFORD

COPIES TO:

PS. CHANCELLOR } HM
SIR G. LITTLER } TREASURY
MR H EVANS }

CONFIDENTIAL

Ch
You have not sent a reply on Sir GL's advice but Sir GL has spoken to Sarinelli. The French have done much the same
Sir GL has given FCO, by phone, a line to take
AWK

T
TELEX

Trichet rang Geoff this afternoon
29/1/87

This is
not membership,
small
I cannot
do sat
pm @
all.
Pro get
Geoff to
*
Name of.
Now with us
65 was

65

DEAR FRIEND

FOLLOWING INFORMAL PHONE CONVERSATIONS BETWEEN OURSELVES OR OUR DEPUTIES, I WOULD CONSIDER CONVENING OUR SMALL GROUP ON FEBRUARY 7TH AND 8TH, PROVIDED THESE DATES WOULD PROVE TO BE CONVENIENT TO ALL OF US.

OBVIOUSLY, SUCH A MEETING COULD ONLY USEFULLY TAKE PLACE, IF THE PREREQUISITES FOR ITS SUCCESS, I.E THE BASIS FOR AN AGREEMENT, WERE MET AT THE OUTCOME OF OUR DEPUTIES WORKING GROUP ON JANUARY 29TH. I THEREFORE TAKE UP ON MYSELF TO STRESS THE IMPORTANCE OF THIS LATTER MEETING.

SHOULD OUR GATHERING TAKE PLACE, I WOULD SUGGEST THE FOLLOWING TIMETABLE .

- 65 DINNER% SATURDAY EVENING AT 8P.M.
- 65 WORKING SESSION, SUNDAY MORNING, ON THE BASIS OF A REPORT BY OUR DEPUTIES
- 67 LUNCH% SUNDAY
- 67 WORKING SESSION, SUNDAY AT 3 P.M.

I WILL CONTACT YOU AGAIN AFTER OUR DEPUTIES MEETING.

YOURS, FRIENDLY.

EDOUARD BALLADUR

Ch
1pm for 6-7 v early.
AA

| | |
|--------------|--------------------|
| CH/EXCHEQUER | |
| REC. | 28 JAN 1987 ✓ 29/1 |
| ACTION | SIR G. LITTLE OIR |
| COPIES TO | PELEST |
| | MR LUELLE |
| | MR H PEVANS |
| | MR CULPIN |

67

DEAR FRIEND

FOLLOWING INFORMAL CONVERSATIONS I HAD WITH SEVERAL OF OUR COLLEAGUES FROM THE 67 COUNTRIES% I CONSIDER CONVENING OUR SMALL GROUP ON SUNDAY% FEBRUARY 8 TH, 1987, PROVIDED THE TIME SCHEDULE OF ALL OF US PROVES THIS DATE TO BE CONVENIENT.

NATURALLY SUCH A MEETING COULD ONLY USEFULLY TAKE PLACE IF THE CONDITIONS FOR ITS SUCCESS ARE MET, AND IF IT APPEARS THAT IT COULD ALLOW A MAJOR STEP FORWARD IN THE MANAGEMENT OF THE INTERNATIONAL MONETARY SYSTEM.

WERE IT THE CASE, I SUGGEST THAT WE MEET ON SUNDAY% FEBRUARY, 8TH AT 1 P.M., FOR A LUNCH AND CARRY ON OUR SESSION IN THE AFTERNOON.

I INTEND TO CONTACT YOU AGAIN DIRECTLY OR THROUGH OUR DEPUTIES IN THE COMING DAYS.

YOURS, FRIENDLY.

EDOUARD BALLADUR

RT. HON. NIGEL LAWSON, P.C. MP
CHANCELLOR OF THE EXCHEQUER
HM TREASURY - LONDON

by
1pm
Sund.
* but with for
deputies to day to
agree that 7/8 premises,
so to 13/14.

I show your analysis Centre.

FROM: A C S ALLAN
 DATE: 29 January 1987

purp

CHANCELLOR



G5

Geoff finally rang me. The meeting started with the bombshell of Gyohten saying that Miyazawa could not manage 7/8 and wanted 13/14! Tietmeyer and Mulford ganged up on Gyohten and made him agreed to pass a message back Tokyo to say the others were very distressed by this development and urged him to go ahead with 7/8. Geoff did not seem to have supported Gyohten nearly strongly enough, but I said he must take Gyohten aside and say we supported the idea of a postponement very strongly indeed.

2. The pressure for having the meeting early seems primarily to come from Stoltenberg, who is determined to get something in place as quickly as possible. The proposal being put to Miyazawa is that he should arrive at 6 am on Sunday morning and join a meeting starting at 8.30 am. The G7 lunch would be put back a bit - but not by enough to suit us. I stressed to Geoff our objectives must be to get the meeting postponed from 7/8 altogether; a poor second best would be to get it started later on Sunday morning and for the G7 lunch to be much delayed (or preferably cancelled). But it does sound more and more as if this is a G3 affair.

3. On the substance, it appears that Baker's relaxed attitude of offering concerted intervention without any quid pro quo is very far from the one being pursued by Mulford. He seems to be demanding all sorts of countervailing announcements from the others - including pressure on us to make announcements next weekend - Geoff didn't go into the details, but he sounded so outraged I think we can safely rely on him to see that one off. Mulford is also pressing his draft on indicators, with support from the French, and even from the Germans (because the alternatives are less attractive to them). Geoff is fighting hard to get it watered down or, preferably, put off until April.



4. Nor is anything sown up on intervention. Mulford is very firm on the need for agreed ranges. The Germans want a general agreement not to let the dollar fall further. And the French are raising some major issues about what exactly concerted intervention means in terms of who intervenes, when and in what currencies.

5. All in all, this has the makings of a complete fiasco - and I am very nervous about Geoff's attitude of being able to draft round everything, rather than adopting a forthright line of saying that all these problems indicate how impossible it is to have a meeting in ten days time. Geoff will be back about 12.30 tomorrow, and I will make sure you get a chance to see him either immediately before or immediately after lunch.

A C S ALLAN



FROM: A W KUCZYS
DATE: 29 January 1987

Ops A
b/f 10/12 A
(chase progress on 'X')

SIR G LITTLER

cc: PS/Economic Secretary
Mr H P Evans
Mr S Matthews

... The Chancellor has seen the attached telegram from Rome. He has commented that this problem was predictable. We must let the Rome Embassy have a clear answer to the Italy/UK GNP comparison (ie referring to purchasing power parity, etc) and Mr Allan has already spoken to Mr Matthews about this.

(Handwritten initials in a circle)

(Handwritten signature)

A W KUCZYS

Mr Kuczys

This material Mr Matthews prepared was sent to FCS and we have got them to send it to Rome. I shall be staying with the Ambassador tomorrow night and will discuss it with him.

JH 2/2

Good. I have also asked for a written answer to the papers, which I will discuss with Mr...

PS/MST has this in hand
AJK 3/2

CONFIDENTIAL

GRS 430

CONFIDENTIAL

FM ROME

TO DESKBY 271400Z FCO

TELNO 062

OF 271220Z JANUARY 87

AND TO DESKBY 271400Z HM TREASURY

INFO PRIORITY WASHINGTON, TOKYO, PARIS, BONN, OTTAWA,

INFO PRIORITY INF/IBRD, UKDEL OECD, UKREP BRUSSELS

RY TELNO 772 OF 29 DECEMBER 1986 (NOT TO ALL): G5/37.

SUMMARY:

1. ITALY EXPRESSES STRONG CONCERN ON THE POSSIBILITY OF A MEETING OF G5 EXCLUDING ITALY AND CANADA IN EARLY FEBRUARY.

DETAIL:

2. THERE HAVE BEEN INTERMITTENT RUMOURS IN THE ITALIAN PRESS THIS MONTH OF A POSSIBLE G5 OR G7 MEETING IN VIEW OF THE CONTINUING DEPRECIATION OF THE DOLLAR, THE EMS REALIGNMENT, THE MEETING IN NEW YORK BETWEEN JAPANESE AND US TREASURY MINISTERS AND THE GERMAN MOVE ON INTEREST RATES. TODAY'S PAPERS CARRY FRONT PAGE STORIES THAT THE JAPANESE MINISTER MIYAZAWA HAS ASKED FOR A G5 MEETING AND THAT, DESPITE OTHER FINANCE MINISTRIES' REFUSAL TO COMMENT, SUCH A MEETING IS LIKELY IN PARIS ON 7 FEBRUARY OR POSSIBLY SHORTLY AFTERWARDS IN NEW YORK.

3. THE CANADIAN PRIME MINISTER MULRONEY WAS YESTERDAY IN ROME ON A VISIT WHICH WAS, ACCORDING TO THE CANADIAN EMBASSY, ARRANGED SOME THREE WEEKS AGO. FOLLOWING HIS DISCUSSIONS WITH CRAXI, CRAXI'S OFFICE YESTERDAY ISSUED BRIEFING TO THE PRESS CONDEMNING ANY MEETING ON EXCHANGE RATE PROBLEMS WHICH EXCLUDES ITALY AND CANADA. CORRIERE DELLA SERA SAYS THE TONE OF THE STATEMENT WAS PARTICULARLY FIRM. CRAXI'S DIPLOMATIC ADVISER BADINI SAID THAT A G5 MEETING WOULD CONSTITUTE A VIOLATION OF THE UNDERTAKINGS ENTERED INTO AT TOKYO SUCH AS TO INVALIDATE THE CREDIBILITY OF THE HEADS OF GOVERNMENT WHO SUBSCRIBED TO IT. ACCORDING TO THE JOINT COMMUNIQUE REPORTED IN THE PRESS CRAXI AND MULRONEY AGREED THAT THE CURRENT SITUATION WAS OF JUST THE KIND WHICH THE TOKYO AGREEMENT ENVISAGED SHOULD OCCASION A MEETING OF THE SEVEN. MULRONEY IS SAID TO HAVE ADDED TO JOURNALISTS THAT THIS DID NOT MEAN PROPOSING THE ABOLITION OF THE GROUP OF 5 WHICH HAS A PARTICULAR AND IMPORTANT ROLE. BUT THE POSITION OF ITALY IS MORE CLEAR CUT. CRAXI WILL PROTEST OFFICIALLY IF ITALY IS EXCLUDED. IL GIORNALE, THE MILAN DAILY, UNEQUIVOCALLY DESCRIBING CANADA AND ITALY AS RESPECTIVELY THE 7TH AND 5TH WESTERN ECONOMIC POWERS, SAYS THAT THE ITALIANS WOULD NOT MIND A MEETING OF THE THREE (UNITED STATES, JAPAN AND GERMANY) SINCE THEY ARE THE MOST DIRECTLY CONCERNED IN CURRENT MONETARY MOVEMENTS BUT THAT THERE IS NO PLACE FOR A MEETING OF

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THE 5 AS SUCH. LA STAMPA AFFIRMS THIS NEITHER CRAXI'S OFFICE NOR THE TREASURY CAN BELIEVE THERE WILL BE SUCH AN AFFRONT TO ITALY, PARTICULARLY NOW THAT SHE HAS OVERTAKEN BRITAIN AS THE FIFTH INDUSTRIAL POWER.

COMMENT:

4. I DO NOT KNOW WHETHER AN ANSWER HAS BEEN SENT TO THE ITALIAN TREASURY MINISTER GORIA IN REPLY TO HIS MESSAGE TO THE CHANCELLOR OF THE EXCHEQUER OF 23 DECEMBER, TRANSMITTED IN TUR. SEEN FROM HERE, IF IT IS INDEED THE INTENTION TO HOLD A MEETING OF 25 IT WILL BE NECESSARY TO RESPOND QUICKLY TO ITALIAN CONCERN IF THE ATMOSPHERE OF THE FORTHCOMING ANGLO-ITALIAN SUMMIT, AND PERHAPS THE VENICE ECONOMIC SUMMIT LATER THIS YEAR ARE NOT TO BE IMPAIRED. I HAVE AN APPOINTMENT WITH CRAXI'S DIPLOMATIC ADVISER AT 1600Z ON 28 JANUARY AND WOULD WELCOME ANY GUIDANCE YOU CAN GIVE ME AS SHALL CERTAINLY BE ASKED ABOUT OUR PLANS.

BRIDGES

YYYY

RFHPAN 4889

LIMITED

ERD

WED

NAD

FED

PLANNING STAFF

PS

PS MRS CHALTER

PS/PUS

MR THOMAS

MR BRAITHWAITE

MR MAUD

MR RATFORD

COPIES TO:

PS. CHANCELLOR } H.M.
SIR G. LITTLER } TREASURY
MR. H. EVANS }

CONFIDENTIAL

4889



10 DOWNING STREET
LONDON SW1A 2AA

From the Private Secretary

29 January 1987

Dear Alex,

I enclose a copy of a letter to the Prime Minister from Signor Craxi proposing a meeting of G-7 Finance Ministers to discuss developments in the currency markets. I should be grateful for a draft reply.

I am copying this letter and enclosure to Lyn Parker (Foreign and Commonwealth Office).

DRAFT REPLY BY 6.2.87 PLEASE

| | |
|----------------|-----------------|
| CH/EXCHEQUER | |
| REC. | 30 JAN 1987 |
| ACTION | SIR G LITTLE |
| COPIES TO | PS/EST |
| | SIR P MIDDLETON |
| | MR LAVELLE |
| | MR H. EVANS |
| | MR S. MATTHEWS |
| MR WILPIN | |
| MR ROSS GOOSEY | |

Yours sincerely,

Charles Powell

Charles Powell

Alex Allen, Esq.,
H.M. Treasury.

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10
The Italian Ambassador

CC
Italian Embassy
4, Grosvenor Square
London, W. 1.

29th January, 1987

734

My dear Charles,

I take pleasure in forwarding to you, a message addressed to the Prime Minister, The Rt. Hon. Margaret Thatcher, MP., by the President of the Council of Ministers, Onorevole Bettino Craxi, together with a rough translation.

I should be most grateful, therefore, if you could kindly pass on the enclosed message to the Prime Minister.

Sincerely yours



Bruno Bottai

Charles Powell, Esq.,
Private Secretary to the Prime Minister
(Overseas Affairs)
10 Downing Street
LONDON SW1

ROUGH TRANSLATION

"Dear Prime Minister,

The anxiety with which Italy is following developments in the currency markets and the need for a much stricter and more attentive observation of these were recently recalled by the Italian Minister for the Treasury, Signor Giovanni Goria, in a letter which he wrote to his Colleagues in the major industrialised countries, in the spirit of the Tokyo agreements. In the weeks which followed, the relations between the major currencies continued to be subjected to great pressure and the monetary system as a whole remains characterized by a prevailing instability.

The confidential meeting scheduled to take place in Rome on the 4th February, next, at the level of Deputies, certainly provides a most useful opportunity in the search for wider convergences in the analysis of the present situation and, hopefully, in the adoption of the more appropriate measures for the return of more stable conditions in currency markets. We cannot, however, dismiss the fact that the extensive range of the problems to be dealt with may also necessitate a meeting at Ministerial level. In this hypothesis - certainly not a remote one - I think that the premises exist for a meeting to be held between Treasury and Finance Ministers of the "Seven", as established by the Tokyo Economic Declaration. There is in fact no doubt that the subject which would have priority in an eventual meeting concerns the improvement of the international monetary system and the related measures of economic policy.

It seems therefore obvious that a different format would be in blatant contradiction to the spirit and the letter of our agreements in Tokyo.

Certain of the careful consideration which you will give to my letter, please accept my very best wishes.

Bettino Craxi."

TEXT OF MESSAGE

"Signora Primo Ministro,

La preoccupazione con cui l'Italia segue gli sviluppi nei mercati valutari e l'esigenza di una più stretta vigilanza sono state anche recentemente ricordate in una lettera che il Ministro del Tesoro italiano, Giovanni Gorla, ha indirizzato ai suoi colleghi dei Paesi maggiormente industrializzati, nello spirito delle intese di Tokio. Nelle successive settimane, i rapporti fra le maggiori monete hanno continuato ad essere sottoposti a tensioni e il sistema monetario nel suo complesso resta caratterizzato da una prevalente instabilità.

La riunione riservata in programma a Roma il 4 febbraio prossimo, a livello di Deputies, costituisce certamente un'occasione molto utile per la ricerca di più ampie convergenze nell'analisi dell'attuale situazione ed, auspicabilmente, nell'adozione delle misure più appropriate per il ristabilimento di condizioni di maggiore normalità nei mercati valutari. Non possiamo tuttavia escludere che l'ampiezza dei problemi da risolvere renda necessaria anche una riunione a livello ministeriale. In questa ipotesi - non certo remota - penso che ricorrano tutti i presupposti perchè la riunione sia indetta tra i Ministri del Tesoro e delle Finanze dei 'Sette', così come stabilisce la dichiarazione economica di Tokio. Non vi è infatti dubbio che l'oggetto prioritario dell'eventuale riunione da convocare riguardi il miglioramento del sistema monetario internazionale e le connesse misure di politica economica.

Mi pare peraltro evidente che un diverso formato contraddirebbe in maniera stridente lo spirito e la lettera delle nostre intese a Tokio.

Certo della seria considerazione che Ella vorrà riservare a questa mia lettera, Le invio i miei migliori saluti.

Bettino Craxi."

SECRET

From: Sir G.Littler
Date: 30 January 1987

MR ALEX ALLAN

c.c. Sir P.Middleton
Sir T.Burns
Mr Cassell
Mr Lavelle
Mr Huw Evans
Mr Culpin

*Thank.
A clark shark ✓*

MEETING OF G5 DEPUTIES

As you know, the recent meeting in Zurich, which ran from 1 p.m. until after midnight on 29 January and for a couple of hours over breakfast on 30 January, broke up in total confusion and a good deal of bad temper. Here, to fill out what I have reported orally and for the benefit of others, is a summary of the main points. I shall write a more detailed narrative over the weekend.

2. Possible Ministerial Meeting: the plan cooked up between US and Germany (and, we thought, Japan) was to prepare for meetings of Finance Ministers and Central Bank Governors (G5 to be followed immediately by G7) on 7/8 February - inconvenient for the Chancellor but we had contingently explored the idea of his going out to join the meetings from the Sunday morning only. Balladur had unwisely sent out a telex, including Italy and Canada, warning of the likely meeting. All this was overturned at the beginning of our meeting by a Japanese statement, reconfirmed under intense and aggressive German and US pressure, that Miyazawa could not manage that weekend because of his Diet time-table. (I am sure this is genuine; they are having a very difficult time with the Tax Reform legislation and even in danger of losing some of it through Diet delays - I did my best to help Gyohten when our

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German and US colleagues angrily expressed incredulity. Equally I think some of the anger was justified: although Gyöhten hotly denied it, the others were sure that Miyazawa had agreed while in Washington recently to a 7/8 February meeting - he probably said "hai!", the Japanese word for yes which often means no more than that the speaker takes note!).

3. Our German colleague was knocked completely off-balance (and told me privately at the end that Stoltenberg on the phone had been "furiously angry". He refused to contemplate the later weekend of 14/15 February, on the silly ground that the markets would turn disastrously if we waited so long; he tried seriously for a meeting without Miyazawa (which I and others rejected); he tried for a meeting on 1 February, abandoned reluctantly as being impracticable. I suggested that, if there was as much agreement as claimed on substance between US, Germany and Japan, they could perhaps intervene overtly "in continuance of Plaza" or even "in the spirit of Gleneagles"; I thought the others of the G7 would certainly not stand in the way and might well endorse; but a short discussion of this quickly lost focus in renewed attempts by Tietmeyer to find other early dates for meetings.

4. Inevitably, therefore, we ended with no agreement except to report to our Ministers. Tietmeyer and Mulford stayed behind in a huddle.

5. The new December and revised November US trade figures (not known to us in Zurich) may cool things a little and reduce some of

SECRET

the frantic German sense of urgency. My guess is that the most probable conclusion on further reflection will be a meeting on the weekend of 14/15 February. (I have suggested to Lebegue that we should in that event work hard to stop the sense of emergency; and that, if - perhaps inevitably - the fact of a meeting becomes known publicly, we should convey the idea of interim stock-taking with April and doubtless other meetings to follow).

6. Object of Meeting: It was quickly apparent that the US and Germany and Japan were, as we supposed, looking for action and words to arrest the decline of the dollar. We agreed to discuss: intervention; policy action; and draft of possible statement.

7. Intervention: It was agreed in principle that, provided terms and other conditions were satisfactory, there should be a Plaza-type undertaking of concerted intervention. But there were some important comments and reservations:

- Lebegue was very critical of the lack of clarity in the earlier arrangements on methods and divisions of costs and responsibilities; he insisted that such matters must be resolved in good time - the conclusion was that we saw no good way of doing this before a general decision by Ministers but would note it as something to be planned for; the need for some flexibility was mentioned; as also (by me and Lebegue) the need for those whose currencies were causing the trouble to take the burden; and there was some half-baked discussion of choice of intervention currencies which I choked off eventually on the basis

SECRET

that any "rules" must be subject to what was sensible in market terms;

- there was a long argument on "levels" versus "ranges"; this began with Mulford proposing the setting of ranges of values at the limits of which intervention would be required; we were soon in a "target zone" argument, although Mulford denied that he intended that (I heard subsequently and privately from Tietmeyer that in his bilateral visit to Washington last week there had been talk of the US helping stop the dollar fall below 1.7 if Germany would help stop it rising above 2.0, and this may have been behind Mulford's language.

8. Policy Action: It quickly emerged that none of the countries represented envisaged really new policy action, and that any statement would have to make best use of what was already largely known (including perhaps a 0.5% drop in Japanese interest rates and promises of a tax reduction programme from Germany). I urged (here and throughout) that any published statement would be weakened in effect if it substituted rhetoric for action, and I got a good deal of sympathy. We agreed that each of us would consider a few lines on own policies as possible contributions, although with some feeling that it might be better to focus on the three imbalance countries. (I will submit separately on this).

9. Statement: Mulford produced a draft statement. Lebegue produced a rival version. I thought both totally unacceptable.

SECRET

I was successful after a long debate (in which Gyohten from the outset and Tietmeyer after a time supported me) in establishing:

- that we should keep the sheer size of the draft to the minimum;
- that we should not drag in the kitchen sink, but keep to the main issues;
- in particular that we should not publish any elaborate annex or paragraphs (and preferably not anything at all) on the "indicators" exercise.

10. We made progress along these lines until confusion overtook our discussions!



(Geoffrey Littler)

P.S. Top copy only has attached:
- the original Murreford and telegram drafts
- the revised version we cobbled together.

David Drab
Rolford

Draft G-7 Statement

1. Ministers of Finance and Central Bank Governors of seven major industrialized countries met today to conduct multilateral surveillance of their economies pursuant to the Tokyo Economic Declaration of their Heads of State or Government of May 6, 1986. The Ministers and Governors, ^{using a range of economic indicators} reviewed current economic developments and prospects, ~~using a range of economic indicators, with a view toward examining the mutual compatibility of their economic objectives and forecasts and to consider the need for remedial action.~~ The Managing Director of the IMF participated in the discussions.

2. The Ministers and Governors were of the view that ^{farther} ~~important~~ progress had been made since the Tokyo Summit in their efforts to achieve a ^{sustainable} ~~lasting~~, non-inflationary expansion. Our economies are now in the fifth year of expansion, and the prospects are for continued growth this year, although the level of unemployment remains unacceptably high in some countries. A high degree of price stability has been attained, ~~with interest rates at the lowest levels in eight years.~~

3. ^{to be done} Substantial progress is being made in reducing budget deficits in deficit countries, and fundamental reforms ^{of tax reforms} ~~of tax systems are being implemented which will improve incentives, increase the efficiency of our economies, and enhance the prospects of higher growth.~~ Other important structural reforms are also being made in our economies, including deregulation of business to increase efficiency and ^{privatization} ~~denationalization~~ of government enterprises to strengthen reliance on private entrepreneurs and market forces. ~~Renewed efforts are underway in deficit countries to increase competitiveness.~~

4. ~~The substantial exchange rate adjustments that have occurred~~ ^{which} will contribute ~~importantly~~ to the restoration of a more sustainable pattern of current accounts. ~~The positive results of this process should become increasingly visible in the period ahead.~~

5. These positive developments notwithstanding, the Ministers and Governors ~~recognized that problems remain.~~ They were concerned about the large trade imbalances ~~that exist and which they consider economically unsustainable and politically unacceptable.~~ The Ministers and Governors agreed the reduction in these imbalances is a matter of ~~highest~~ ^{highest} priority, and that the achievement of more balanced global growth should play a central role in bringing about such a reduction.

judge broad

concern about the persistence of large trade imbalances, exchange rates and limits of protection

ref to EC/US Agreement

reaffirmed their

over continuing pressures for

6. The Ministers and Governors ~~also expressed concern that the forces of protectionism are growing.~~ They agreed that efforts to deal with economic problems by erecting trade barriers were self-defeating, and pledged to intensify their efforts to resist protectionism and reaffirmed their strong support for the new round of trade negotiations.

In this context they welcomed

7. The Ministers and Governors recognized that the major industrial countries have a special responsibility to follow policies which foster an open, growing world economy in order to support the efforts of debtor countries to restore steady growth and viable balance of payments positions. They noted the progress that had been achieved by many debtor countries toward these ends, but stressed the importance of all participants in the strengthened debt strategy ~~to continue cooperative efforts to resolve international debt problems.~~

continuing their

8. The Ministers and Governors agreed to intensify their economic policy coordination efforts ~~in order to promote more balanced global growth and to reduce existing imbalances.~~ They agreed that remedial actions are necessary in order to achieve these objectives. Surplus countries committed to follow policies designed to stimulate domestic demand and to reduce their external surpluses while maintaining low inflation. Deficit countries committed to follow policies designed to support steady, low-inflation growth while reducing domestic imbalances and their external deficits. To this end, each country has agreed to the undertakings contained in Appendix I to this document.

be in

9. The Ministers and Governors also ^{took note of} ~~agreed to~~ additional refinements to the multilateral surveillance arrangements approved by their Heads of State or Government in the Tokyo Economic Declaration. As part of implementing these arrangements, they will:

Issue for Administration but at time

- Periodically agree on specific medium-term economic objectives that will serve as a basis for assessing national policies and performance;
- Establish interim performance indicators which will be used to examine whether current economic developments and trends are consistent with the agreed objectives. The attached Appendix II provides additional background on these arrangements.

10. The Ministers and Governors noted that a number of newly industrialized countries were playing an increasingly important role in the world economy. These countries have achieved strong economic growth based significantly on their access to open, growing export markets. Recently,

David's appears at X/ in []
2, alternative

some have accumulated trade surpluses which have contributed importantly to the present unsustainable pattern of global imbalances, thus increasing protectionist pressures. The Ministers and Governors urged the newly industrialized developing countries to assume greater responsibility for preserving an open world trading system by reducing trade barriers and pursuing policies that allow their currencies to more fully reflect underlying economic fundamentals.

11. The Ministers and Governors reaffirmed that exchange rates should play a role in adjusting external imbalances, and agreed that the substantial exchange rate changes that have occurred will increasingly contribute to that end. They expressed their understanding that the currency realignment which has taken place has brought their currencies within ranges that are now broadly consistent with underlying economic fundamentals, given the policy commitments outlined herein. In current circumstances, therefore, they stand ready to cooperate closely to reduce the variability of their currencies within broad ranges centered on current rates.

reducing external imbalances

see the 1972 Agreement

to levels

of exch. rates recent
to foster stability & avoid these levels.

~~Further excessive exchange shifts would impair the recovery.~~

conceded
~~[including by intervention] above necessary]~~

among us: currencies

~~Further excessive exchange rate shifts would damage the growth and prospects of the program in all countries.~~

Revised Para - new 10

APPENDIX I

APPENDIX II

Economic Policy Coordination: Next Steps

Agreement has been reached with regard to refinements of the Tokyo arrangements on closer economic policy coordination. A manageable number of indicators has been agreed upon to assess the consistency and mutual compatibility of economic policies and performance. The initial multilateral surveillance exercise based on the indicators in September 1986 has been developed further, both analytically and operationally.

As a result, the economic policy coordination process has been made more effective through: (1) simplification of the indicator mechanism and (2) the provision of greater discipline to the process.

The Establishment of Economic Objectives

Medium-term economic objectives are to be established early in the year in terms of a small group of indicators that measure domestic and external economic performance and policies. Broad objectives will be agreed for each variable for the group as a whole. Objectives are also to be developed for each country. These objectives would depend on each country's own circumstances, but will have to be consistent with the overall objectives for the group. The objectives will in some cases be quantified; in others, they may be more general in nature. Both the collective and individual country objectives are to serve as standards against which to assess country policies and performance. For 1987, the objectives involve the following key variables: growth (GNP), inflation, current account/trade balances, interest rates and exchange rates.

Review Process

The Ministers will meet regularly, three times each year, to review national economic policies and performance and assess current trends and prospects within the context of the agreed objectives. In order to assist in these meetings, the IMF will develop further the approach taken in the initial surveillance exercise by preparing papers for each meeting. Such papers, including tables on the indicators, will examine economic developments and prospects in each country, and assess the progress and problems in achieving the agreed objectives. In this context, an assessment will be made of the possible need for policy action to assure that current and prospective trends are consistent with achievement of the agreed objectives or to modify the objectives.

In order to assist in this assessment, interim performance indicators will be developed. Such indicators can help Ministers in reaching judgments as to whether efforts are on track to achieve the agreed objectives. In selecting the interim

performance indicators, attention will be focused on specific measures from the range of variables referred to in the Tokyo communique. The interim performance indicators will vary from year to year and be selected in light of the agreed medium-term economic objectives.

As part of the review process, the Deputies will prepare a note outlining key issues for Ministerial consideration. Ministers and Governors will meet at least twice a year to review progress and prospects and undertake best efforts to reach understandings regarding appropriate remedial action. On one of those occasions, Ministers and Governors are to approve individual and collective objectives for the coming year. The Managing Director of the Fund would participate in a part of any surveillance discussion of the Ministers and Governors, and will be invited to present a short note in advance of each meeting. When circumstances warrant, a special meeting of Ministers and Governors would be convened.

The Role of Exchange Rates

As indicated above, exchange rates are one of the key variables in outlining economic objectives, and play an important role in fostering progress toward those objectives. Thus it will be important to have informal, confidential understandings among Ministers and Governors on the broad directions, and orders of magnitude, of exchange rate changes which are desired to achieve the agreed objectives. Such understandings are essential to reaching judgments concerning the extent to which imbalances are expected to be reduced through exchange rates or by other adjustment measures (e.g., policies affecting growth).

With agreed objectives for exchange rate developments over the medium term (i.e., the next year or two), it will then be possible to develop a sense of the desired path of exchange rate evolution in the interim. Such a sense will involve the use of ranges which could be seen at any point in time as broadly consistent with the achievement of the ultimate objectives.

The IMF staff will not provide any estimates of "equilibrium" or in any other sense "correct" exchange rates, although the staff and the Managing Director are being invited to express their view about the broad directions of exchange rate movements which might be needed to achieve agreed objectives, and the implications of lack of sufficient movement for other policies. Ministers will seek to reach understandings regarding appropriate exchange rate objectives, as outlined above, as well as regarding interim exchange rate developments. These understandings will normally remain confidential.

Daniel Drouot
Lebegue

DRAFT COMMUNIQUE

1) Ministers of Finances and Central Bank Governors of France, the Federal Republic of Germany, Japan, the United Kingdom and the United States met today in Paris. Along the lines of the multilateral cooperation launched by the Plaza agreement on September 22 1985 and which has received a new impetus from the Heads of State and Government Tokyo Summit on May 6, 1986, they have agreed upon the analysis of the present economic situation and policy measures in order to promote the pursuit of a long lasting non inflationary growth.

Given the unescapable gradualism of a well balanced correction in the present external disequilibria, they strongly reaffirm the deadly effects, particularly for the world economic growth, that resorting to protectionism would entail. They have reviewed the exchange markets recent developments. Although the present parity grid is consistent with the forecasted economic fundamentals they have noted a persistent excessive volatility in exchange rates, reflecting the markets uncertainties. Therefore they have decided to launch a concerted action to promote exchange rates stabilization and to that end, to provide the necessary financial means.

Sustaining growth, reducing external imbalances between industrialized countries, maintaining an open multilateral trading system, stabilizing exchange rates will contribute decisively to solving the debtor countries difficulties.

2) In order to improve their coordination, Ministers and Governors have decided to follow regularly a number of economic indicators, with a special focus on those which reflect interactions among their countries, namely growth, inflation, current account and trade balances, interest rates and exchange rates.

Broad objectives will be agreed for each variable, for the group as a whole as well as for each country. These objectives will serve as standards against which country policies and performance will be assessed. They defined the process through which deviations from the intended paths will automatically trigger consultations among either Ministers and Governors or Deputies.

Ministers and Governors agreed to pay a particular attention to exchange rates which provide a clear indication of the international implications of domestic policies and the interactions among countries. They will assess the evolution of both bilateral and effective exchange rates against a reference range and an intended course on which they would have had informal and confidential common understandings.

They have decided to review their economic situations regularly at least twice a year along these lines, and especially whenever circumstances will warrant such discussions.

3) Short term and medium term prospects are the pursuit of growth without inflation rekindling. In 1986, in most GV countries, including the United States, growth has benefited from the sustained dynamism of domestic demand. In 1987, external demand should be a positive growth component in the U.S, while in Japan and Europe, the pursuit of economic growth will be even more dependent upon the resilience of domestic demand. The warranted substantial correction in exchange rates has taken place ; it has already a strong impact on the real economy ; a reorientation in real trade flows is under way and will accentuate, even if nominal results are lagging behind and do not reflect it as yet. So as to secure optimal conditions for this indispensable adjustment and sustain growth, our countries will intensify their efforts in removing structural rigidities and fostering full employment of human resources and productive capacities.

4) Ministers and Governors stand firmly committed to cooperate toward that end. For the time being, they jointly agreed on the following intentions :

- **the United States Government** will continue its efforts to reduce the fiscal deficit along the lines of the Gramm Rudman Hollings Act, that establishes a 108 billion dollars target for fiscal year 1988 ; the US monetary authorities will maintain a pragmatic monetary policy that would allow for a progressive reduction of real interest rates while paying attention to the external value of the dollar ;

- **the Government of Japan** will expeditiously implement the projected tax reform, aimed at fostering a better balance between savings and consumption and at stimulating capital investment ; furthermore it will accelerate and complete the full realization of the expenditures authorized within the last supplementary budget ; the japanese monetary authorities will flexibly manage monetary policy so as to sustain internal demand, especially through a further reduction of interest rates compatible with inflation prospects in Japan ;

- **the Government of Germany** will pursue its action toward a reduction of the tax burden in order to favour the adjustment and the vitality of the productive sector ; it is committed to take the best advantage of the economic slack that would appear, in order to boost a

full utilisation of the production capacity ; in that respect, the German Government will have implemented its tax reduction program fully by June 1987 and will submit to the Parliament at the earliest the main lines of its projected tax reform ;

- **the Government of France** is committed to contribute to concerted efforts for sustained growth, while progressing further in disinflation and the reduction of the fiscal deficit ; it will pursue its reform program and the structural adjustment aimed at removing rigidities in its markets and at fostering the present pick-up in capital investment ;

- **the United Kingdom Government** is committed, within the Medium-Term Financial Strategy, to improve its control on the evolution of costs, mainly labor costs, and to continue its program for a reduction of structural rigidities.

- **the Italian Government (...)**
- **the Canadian Government**

Ministers and Governors reaffirmed that these measures are designed in a medium-term strategy and that they will maintain a close cooperation to proceed toward that goal.

5) Taking into account these policy measures, Ministers and Governors have discussed the present pattern of their exchange rates and come to the conclusion that at this stage it is consistent with the present fundamental economic data and policy orientations.

The corrections in exchange rates which have materialized since the Plaza agreement have already allowed for a reorientation in real trade flows, although this has not yet surfaced in nominal terms. The present dollar rate vis a vis the currencies of the U.S main industrialized partners grants a good competitiveness level to the U.S economy.

Additional corrections would in fact lead to misalignments. Moreover, to avoid a recession, a better balance in external accounts has to come about slowly. It would be proper for exchange markets to take into full account, in their assessments, the short and medium-term effects of adjustment policies underway.

Ministers and Governors stand ready to undertake concerted interventions as soon as exchange rate variations would tend to produce an overshooting of the dollar rate. To that end, they have set up an extraordinary pool of resources and will maintain a close coordination on its utilization.

6) Ministers and Governors are firmly convinced that protectionist measures if adopted, would greatly jeopardize economic growth and development without fostering a smooth correction of the present external imbalances. The Governments of the five major industrial countries are therefore committed to favouring the starting of the new multilateral trade

negotiations launched last September in Punta del Este ; they invite all the countries which participate in the open system of international trade to contribute to the success of these negotiations.

7) The pursuit of policies in our countries that ensure a balanced and sustained growth and world trade expansion is a basic condition for a solution to the international debt crisis.

It should thus comfort the indispensable efforts of all the involved participants : heavily indebted countries have to remain committed to rigorous macroeconomic and structural adjustment programs ; the multi-lateral institutions and the financial community will have to supply adequate financing for a resumption of development and growth in the developing countries.

Draft G-7 Statement

1. Ministers of Finance and Central Bank Governors of seven major industrialized countries met today to conduct multilateral surveillance of their economies pursuant to the Tokyo Economic Declaration of their Heads of State or Government of May 6, 1986. The Ministers and Governors , using a range of ^{economic} indicators, reviewed current economic developments and prospects. The Managing Director of the IMF participated in the discussions.

2. The Ministers and Governors were of the view that further progress had been made since the Tokyo Summit in their efforts to achieve a sustainable, non-inflationary expansion. Our economies are now in the fifth year of expansion, and the prospects are for continued growth this year, although the level of unemployment remains unacceptably high in some countries. A high degree of price stability has been attained. Exchange rate adjustments have occurred which will contribute importantly in the period ahead to the restoration of a more sustainable pattern of current accounts.

3. Progress is being made in reducing budget deficits in deficit countries, and fundamental tax reforms are being introduced to improve incentives, increase the efficiency of our economies, and enhance the prospects of higher growth. Other important structural reforms are also being made in our economies, including deregulation of business to increase efficiency and privatization of government enterprises to strengthen reliance on private entrepreneurs and market forces.

4. These positive developments notwithstanding, the Ministers and Governors agreed that the reduction of the large trade imbalances is a matter of high priority, and that the achievement of more balanced global growth should play a central role in bringing about such a reduction.

5. The Ministers and Governors reaffirmed their concern over continuing pressures for protectionism. They agreed that efforts to deal with economic problems by erecting trade barriers were self-defeating, and pledged to intensify their efforts to resist protectionism and reaffirmed their strong support for the new round of trade negotiations. [Reference to US/EEC-Agreement]

6. The Ministers and Governors recognized that the major industrial countries have a special responsibility to follow policies which foster an open, growing world economy in order to support the efforts of debtor countries to restore steady growth and viable balance of payments positions. They noted the progress that had been achieved by many debtor countries toward these ends, but stressed the importance of all participants in the strengthened debt strategy continuing their cooperative efforts to resolve international debt problems.

7. The Ministers and Governors agreed to intensify their economic policy coordination efforts in order to promote more balanced global growth and to reduce existing imbalances.

[Country Policy Statements]

8. In order to improve their coordination, Ministers and Governors have decided to follow regularly a number of economic indicators, with a special focus on those which reflect interactions among their countries, namely growth, inflation, current account and trade balances, interest rates and exchange rates.

Broad objectives will be agreed for each variable, for the group as a whole as well as for each country. These objectives will serve as standards against which country policies and performance will be assessed. They defined the process through which deviations from the intended path, will trigger consultations among either Ministers and Governors or Deputies.

Ministers and Governors agreed to pay a particular attention to exchange rates which provide a clear indication of the international implications of domestic policies and the interactions among countries. They will assess the evolution of both bilateral and effective exchange rates against a reference range and an intended course on which they would have had informal and confidential common understandings.

They have decided to review their economic situations regularly at least twice a year along these lines, and especially whenever circumstances will warrant such discussions.

8. The Ministers and Governors also took note of additional refinements in the use of economic indicators for the multilateral surveillance arrangements approved by their Heads of State or Government in the Tokyo Economic Declaration.

9. The Ministers and Governors noted that a number of newly industrialized countries were playing an increasingly important role in the world economy. These countries have achieved strong economic growth based significantly on their access to open, growing export markets. Recently, some have accumulated trade surpluses which have contributed importantly to the present unsustainable pattern of global imbalances, thus increasing protectionist pressures. The Ministers and Governors urged the newly industrialized developing countries to assume greater responsibility for preserving an open world trading system by reducing trade barriers and pursuing policies that allow their currencies to reflect more fully underlying economic fundamentals.

10. The Ministers and Governors agreed that the substantial exchange rate changes since the Plaza Agreement will increasingly contribute to reducing external imbalances and have now brought their currencies [to levels / within ranges] consistent with underlying economic fundamentals, given the policy commitments outlined in this statement. Further excessive exchange rate shifts among their currencies [could / would] damage growth and adjustment prospects in their countries. In current circumstances, therefore, they stand ready to cooperate closely [including by concerted intervention] to foster stability of exchange rates around recent levels.

I agree. We can discuss the handling of the budget. etc.

From: Sir G.Littler
Date: 2 February 1987

MR ALEX ALLAN

c.c. Mr Lavelle
Mr Huw Evans

WASHINGTON MEETINGS: G10 MINISTERIAL

I took the opportunity in the margins of the meeting of G5 deputies last week to take soundings about a G10 Ministerial meeting in Washington in April, in accordance with tradition.

2. I said that our time would probably be under competing claims, that in any case the Chancellor would not want to propose a substantive meeting, and that my question really was whether we needed a meeting at all.

3. The unanimous response was that, while there should be no long or substantive meeting (Ruding had killed that idea by doing it badly!), the interests of diplomacy vis-a-vis G10 members who are not in G5/G7 made it very desirable to have a short meeting, which all wanted to be in the former tradition of not more than an hour before the Interim Committee begins.

4. I think this is the right conclusion. Would the Chancellor agree? If so, I will warn the IMF Secretariat, and set the necessary arrangements in hand. (In case the Chancellor wants to discuss, this can wait until I return from my next absence).



(Geoffrey Littler)

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040820 :/G-7 OFFICIALS LIKELY TO DISCUSS CURRENCY MEETING

By Rich Miller, Reuters

TOKYO, Feb 4 - Senior officials from major industrial nations are likely to discuss informally the possibility of a ministerial meeting on currencies when they get together this week in Florence, government officials and diplomats said.

The officials from the Group of Seven states - Britain, Canada, France, Italy, Japan, the U.S. and West Germany - are meeting to map out strategy for the June economic summit.

Monetary sources in Washington said last month that officials from the group, known as the G-7, would meet in Florence from February 4-6 to prepare for the Venice summit.

MORE

040821 :/G-7 OFFICIALS =2 TOKYO

Deputy finance ministers attending the talks are likely to take the opportunity to discuss informally the possibility of an early meeting of finance ministers from the Group of Five, G-5, which excludes Canada and Italy, and the G-7, officials and diplomats said. One added, however, that deputy finance ministers from all seven countries are unlikely to be there.

The meeting in Florence is also being attended by the personal representatives of the summit leaders, the so-called "sherpas." The formal discussions in Florence are likely to centre on such issues as policy coordination, economic restructuring, trade, Third World debt and agriculture.

MORE

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040821 :/G-7 OFFICIALS =3 TOKYO

Officials and diplomats said Canada's and especially Italy's insistence they be included in any talks on currencies held by the five other nations has increased the chances the G-7 will meet at the same time as the G-5.

Some officials suggested the meetings will be held one after the other, with an informal G-5 get-together preceding a more formal G-7 one.

A senior Japanese official said major nations have been unable to settle on a date to discuss currency stability because of uncertainty over Japanese Finance Minister Kiichi Miyazawa's schedule.

MORE

040822 :/G-7 OFFICIALS =4 TOKYO

With the threat of another boycott of Japan's parliament by the opposition parties, the official said it is unclear whether Miyazawa can attend a G-5/G-7 meeting on February 14, as some local newspapers have suggested.

Officials have already said the idea of holding a G-5 meeting in Paris on February 7 was dropped because Miyazawa would have been unable to attend.

The opposition political parties boycotted parliamentary proceedings last week to protest Prime Minister Yasuhiro Nakasone's failure to mention government plans for a controversial sales tax in his opening speech to the Diet.

MORE

040823 :/G-7 OFFICIALS =5 TOKYO

A senior Japanese official said no G-5 country is strongly opposed to holding an early meeting, although some are skeptical about its chances of achieving much.

But those nations with some reservations are prepared to hold a meeting if a majority of the G-5 are in favour, as seems to be the case, he said. Diplomats said Japan has been pressing hardest for an early G-5 meeting during a recent series of late-night telephone calls among senior officials.

Some analysts have said the recent stability of currency markets has made a G-5 meeting less likely. But the official said a meeting would still be useful to help calm markets.

REUTER

Pub

PPS Chancellor 12/2

091522 :/EC MINISTERS SEE NO NEED FOR EARLY G-5 MEETING

BRUSSELS, Feb 9 - European Community finance ministers believe there is no great need for a Group of Five meeting on world currency stability before talks due to take place at the time of the International Monetary Fund and World Bank meetings in Washington in April, diplomats said.

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"The impression is that there is no great need for a special meeting at the moment, particularly in view of the prospect of a full discussion of the issues at the Washington meetings," said one diplomat.

The diplomats were speaking after EC finance ministers discussed monetary issues over a working lunch here.

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CN RIM974

091527 :EC MINISTERS =2 BRUSSELS

The diplomats said the ministers' talks focussed mainly on the situation within the European Monetary System (EMS) following last month's realignment. They added France will later this week present proposals for technical improvements in the workings of the EMS.

Diplomats said the French ideas would probably focus on greater economic policy coordination within the EC, increased central bank cooperation and the relationship between the ECU and the dollar and yen.

Some diplomats said the French ideas were also expected to cover global monetary stability.

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cc RC; SD; GS; NI
PPS; Long; Miller; McCarroll; Mohr; Kelly; P...

110112 :/BAKER SAYS U.S. WANTS PROGRESS ON TOKYO PACT
WASHINGTON, Feb 10 - Treasury Secretary James Baker said the United States is pursuing development of intensified economic coordination between the major industrial nations.

Baker was asked by reporters after a speech to a university audience to confirm reports that Washington wants to establish currency reference or target ranges with other major industrial countries.

"We support the idea of following through on the Tokyo summit communique of multilateral surveillance exercises by the major industrial nations and we're pursuing that objective," he said.

MORE

110117 :/BAKER AGAIN DECLINES COMMENT ON DOLLAR

WASHINGTON, Feb 10 - Treasury Secretary James Baker again declined to comment on an appropriate level for the dollar.

After a speech to a university audience, Baker was asked whether the U.S. was pursuing a policy of deliberate devaluation. "I refrain from commenting on what we in this government think might or might not be an appropriate level (for the dollar)," he said.

Baker said there have "clearly been benefits" from the dollar's decline but there are also risks like higher inflation and difficult budget deficit financing.

But "we have not seen either of those happening," he said.

REUTER

110128 :/BAKER SAYS U.S. =2 WASHINGTON

The Tokyo summit agreement called for intensified economic cooperation among the seven major industrial nations -- the U.S., Japan, West Germany, Britain, France, Italy and Canada.

It called for the monitoring of forecasts of key economic indicators like growth, trade surpluses and deficits, exchange rates, interest rates, and budget deficits, among others.

When there were significant deviations from the forecasts, the agreement urged the country concerned to take corrective action.

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CN RIM162

110129 :/BAKER SAYS U.S. =3 WASHINGTON

Monetary sources told Reuters yesterday the U.S. has pressed the idea of using reference ranges for the currencies of the five major industrial countries and that the proposal is linked to development of the Tokyo agreement.

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Chancellor

111815 :UK LEADS G-7 IN PRODUCTIVITY GROWTH - TREASURY
LONDON, Feb 11 - Productivity in U.K. manufacturing industries has grown faster in the 1980s than in any other major industrialised country, the British Treasury said in its latest Economic Progress Report.

It said "part of the improvement in productivity performance (in Britain) reflects a shake-out of labour from manufacturing in the early 1980s, as firms were forced to reduce overmanning and increase efficiency"

Manufacturing productivity had grown by more than four pct a year since 1983, it said. It added that employment in the U.K. rose by more than one mln during that period.

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CN RIM746

111824 :/FRENCH MINISTRY SOURCES SAY NO EARLY G-5 MEET
PARIS, Feb 11 - French Finance Ministry sources said today they saw no likelihood of an early meeting of Group of Five Finance Ministers.

"There will be no meeting. Its been discarded, at least for the time being," one source told Reuter, commenting on currency market rumours of a possible G-5 gathering this weekend or early next week.

MORE

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CN RIM747

111828 :FRENCH MINISTRY =2 PARIS
Finance Minister Edouard Balladur said yesterday in a newspaper interview France had been working for several weeks to narrow the policy differences between G-5 members, and he remained hopeful a meeting might be held.

But he added all five countries involved, France, the U.S., Japan, West Germany, and Britain would have to make an effort for such a meeting to be useful.

EC Finance ministers were quoted by diplomats in Brussels on Monday as seeing no need for an early meeting, although West Germany Finance Ministry State Secretary Hans Tietmayer said Germany favoured a meeting if it was well prepared.

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111937 :/BID TO CALL GROUP OF FIVE TALKS CONTINUES

By Peter Torday

WASHINGTON, Feb 11 - Under pressure from volatile currency markets, officials from the five leading industrial democracies are continuing to negotiate for a meeting of their finance ministers, western monetary sources said.

But they also said that crucial compromises by several of the countries have still to be struck and may mean a meeting is delayed until April when the semi-annual meetings of the International Monetary Fund and World Bank are held.

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111939 :/BID TO CALL =2 WASHINGTON

"We share the U.S. position that we should not have a meeting without some policy commitment to stabilize the markets," said a European monetary source.

Pressure for talks intensified after the dollar resumed its sharp fall last month. While markets are calmer today, "as soon as we get more economic news, the markets take off, that's really what's forcing a meeting," one source said.

On the table are U.S. proposals for reference ranges to help bring about currency stability, in addition to American demands for faster economic growth abroad.

REUTER

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CN RIM770

111940 :/BID TO CALL =3 WASHINGTON

So far, however, there are few signs that Japan will enact a genuine economic stimulus plan or that West Germany's finance minister, Gerhard Stoltenberg, will agree to bring forward tax cuts planned for 1988.

Washington has staked a great deal on the argument that only faster economic growth will bring down the huge trade surpluses of Japan and West Germany and correspondingly reduce the massive American trade deficit.

While European monetary sources said West Germany and Britain have grave misgivings about the currency plan, there are signs they may cave in if Washington makes concessions.

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CN RIM947

120254 :/BANK OF JAPAN'S MONETARY POLICY UNCHANGED

TOKYO, Feb 12 - The Bank of Japan's basic stance on monetary policy has not changed, a central bank official said, responding to bond market rumors the Bank will soon cut its three pct discount rate by a half-point.

The official said the bank is still watching developments surrounding a possible meeting of the Group of Five industrialized nations before it cuts the rate.

Bank of Japan officials have previously said the central bank will reduce the discount rate when it has clear signs the group will meet to stabilize currency rates.

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FRS Chancellor

111942 :/BID TO CALL =4 WASHINGTON

Those concessions include, some sources said, action to speed up the reduction of the U.S. budget deficit.

But there is scepticism in Europe that the Reagan administration can deliver promises on the deficit given the apparent impasse with the Democrat-controlled Congress over the issue.

"You know how difficult it is to have the United States reach agreement on the budget deficit. Stoltenberg, on the other hand, is in a position to deliver," said one European source.

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CN RIM775

111945 :/BID TO CALL =5 WASHINGTON

A U.S. monetary source pointed out that the U.S. trade deficit has fostered global growth since 1982 and added that nobody could deny progress has been made on the budget deficit. "There is some adjustment fatigue on our part."

Monetary analysts also believe the United States is being pressed to stabilize and even strengthen the dollar before any talks can be called.

Fed funds -- the rate that banks charge each other for overnight loans to finance their reserve positions -- have been relatively high in the past two days, prompting market speculation of a slightly firmer U.S. monetary policy.

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111949 :/BID TO CALL =6 WASHINGTON

Fed chairman Paul Volcker, who would oversee such a change in U.S. monetary policy, works very closely with Treasury Secretary James Baker, according to officials of both agencies.

Last week, a Reagan administration official said the two men saw "exactly eye-to-eye" on the dollar, a statement that signalled they formed a united front on the main question before the Group of Five -- the United States, Japan, West Germany, Britain and France.

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CN RIM777

111950 :/BID TO CALL =7 WASHINGTON

Several sources say the U.S. plan, which France and Japan support, calls for consultations or even meetings when currencies breach their agreed reference ranges.

Subsequently, currency intervention or more drastically, economic action, would have to keep currencies within ranges.

Such a system would be a major advance on the Tokyo Summit pact for strengthening international economic cooperation.

Last May, the Five joined by Italy and Canada, agreed to measure economic policy goals against actual economic performance. If there was a sharp difference, then the country concerned is urged but not obliged to take corrective action.

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111951 :/BID TO CALL =8 WASHINGTON

When asked about reference ranges yesterday, Baker said, "we support the idea of following through on the Tokyo Summit communique of multilateral surveillance exercises by the major industrial nations and we're pursuing that objective."

At Tokyo it was agreed economies would be measured by indicators like growth, trade and budget deficits and surpluses, inflation, and exchange rates, among others.

But the sources said there is no agreement that these indicators are "objective" in revealing why an economy's direction has changed.

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111954 :/BID TO CALL =9 WASHINGTON

Disagreement over this point is crucial since without objective guidance, the finger cannot fairly be pointed at any particular nation to take corrective action, making agreement on action very difficult once a currency overshoot its range.

The U.S.-Japan economic pact is being used as a rough model for a five-way accord. An administration official said the range in question was between 152 to 161 yen to the dollar.

When the yen tested 150 to the dollar last month, Finance minister Kiichi Miyazawa flew to Washington for talks.

Even the markets played down the talks' importance, fears of intervention prevented the dollar from breaching 150.

REUTER

120958 :/JAPANESE OFFICIAL SAYS G-5 MEETING UNDECIDED ✓ A, B, C, CI
TOKYO, Feb 12 - Finance Minister for International Affairs, Toyoo Gyohten, told a press conference there has been no decision on a Group of Five (G-5) meeting, ministry officials said.

He made the comment to Japanese reporters after briefing Prime Minister Yasuhiro Nakasone about recent speculation of a meeting of finance ministers and central bank governors, they said.
Gyohten told the press conference he told Nakasone he does not know about a timing of a G-5 meeting and that a meeting has not yet been decided, the officials said.
MORE

CN RIM177

121016 :/JAPANESE OFFICIAL =2 TOKYO
In response to a question on whether there is disagreement among the G-5 member countries, Gyohten was quoted as saying it takes time and effort to hold a G-5 meeting, particularly to set a date and place and prepare areas for possible agreement.
The G-5 members are the United States, Japan, West Germany, Britain and France.
Although the G-5 meeting is unofficial, many people are now concerned, so such a meeting cannot be held without adequate preparation, he said.
MORE

121027 :/JAPANESE OFFICIAL =3 TOKYO
Asked about his views on Japanese press reports that Nakasone indicated a delay of a G-5 meeting until next week or later, Gyohten said he was not sure of the Prime Minister's understanding of the situation but that he himself does not know of a date.
He said he told Nakasone the main interest among the countries concerned are the stability of the foreign exchange market and policy coordination.
As to reports that the U.S. may propose "reference ranges" for the currencies of the G-5 nations, the Vice Minister said he has no knowledge such a proposal.
MORE

121032 :/JAPANESE OFFICIAL =4 TOKYO
"Reference ranges are not on the table for discussion", an official quoted Gyohten as saying.
Gyohten said there is international concern about improving the current floating system and change it but there are no detailed proposals.
Countries concered are studying such reference ranges but no result from the study has yet come out, he said.
The agreement between Japanese Finance Minister Kiichi Miyazawa and U.S. Treasury Secretary James Baker on stability of the currency market is in line with the policy coordination agreed at the Tokyo Summit talks last May, he said.
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130544 ://JAPAN OFFICIALS DENY RUMOUR MIYAZAWA WENT TO PARIS
TOKYO, Feb 13 - A Finance Ministry spokesman denied a
widespread rumour in the Japanese bond and currency markets
that Finance Minister Kiichi Miyazawa had left for Paris for
currency talks.

He told Reuters by telephone that Miyazawa is in his
office and will stay in Japan over the weekend.

Neither market appeared to react to the rumour, bond and
currency dealers said, but many dealers contacted Reuters to
ask if it was true.

There has been persistent speculation in the markets here
that the Group of Five may meet soon.

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130047 ://MIYAZAWA SAYS NOTHING NEW ON G-5 MEETING
TOKYO, Feb 13 - Finance Minister Kiichi Miyazawa said
there are no new developments over prospects for a Group of
Five (G-5) meeting.

Asked at a press conference whether anything new had
appeared over a G-5 meeting since yesterday, Miyazawa said,
"Nothing."

Prime Minister Yasuhiro Nakasone also said yesterday a G-5
meeting may not be possible next week.

REUTER



The format is better than
the figs - although it will
be better to have
each of the tables on
individual cards.

The figs - which are
correct -

Growth in domestic demand in
1987 of 4% for Japan &
3 1/2% for Germany looks far
too high

ditto for GDP growth of 3.1%
& 2.9% in 1987 for J & G (look
@ latest estimates for 1985)
1986 figs are slightly suspect, but
for some domestic demand & GDP growth)

Over

UK inflation figure for
1987 is a shade less high,
UK current acc deficit
figure for 1987 is much
less high.

Italian - Canada (1987)
figs for Americas and
growth are exp'd.

Tables A, B & C SLS also
show forecast ~~averages~~
averages for the 3 yrs
1985/6/7 taken together.
M.

P.S. Note: Culprits ~~are~~ also
have some thoughts

CONFIDENTIAL

From : H P Evans

Date : 13 February 1987

CHANCELLOR

Ch
This material will, suitably updated, form part of your briefing for a G5/7 if one takes place.

Any comments on format or coverage?
DWK

cc Sir P Middleton
Sir T Burns
Sir G Littler
Mr Cassell
Mr Peretz
Mr Culpin

POSSIBLE G5/7 MEETING

13/2

Against the possibility of a meeting, we have prepared some material in the form of data and charts on economic developments and forecasts and on financial markets. It can be updated quickly. You may like to glance at this material and let us know where changes would be helpful.

Data and Charts

2. The following tables and charts are attached.

- A - F : international comparisons of nominal income (A), domestic demand (B), GNP (C), inflation (C), current account (D), unit labour costs (D), budget deficits (E) and interest rates (F).
- G - M : charts of dollar exchange rates (G and H), effective exchange rates (I and J), sterling exchange rates (H and L) and yen/DM rates and real dollar effective rates (M).
- N : table of nominal exchange rate changes since the February 1985 peak and since Plaza
- P - R : tables of nominal bilateral £ and \$ (P and Q) and effective rates (R), monthly since 1985.

Comments

3. Most of this material is very familiar. Chart M may not

EVANS
→ CH/EX
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be : it includes real dollar effective indices calculated to include US trading partners outside OECD especially the NICs and the big debtors, whose real exchange rates have not risen against the dollar. (Because many of these countries have high inflation, meaningful series are only possible for real effective rates).

4. The conclusion from the broad version of Chart M - the third one on the page - is that the dollar has fallen enough to regain the 1981-2 level of competitiveness, but is still above the 1976-80 levels : this compares with (Chart G) record or near record lows on the bilateral nominal rates.

5. Table B, on IMF forecasts of growth rates of domestic demand, shows that UK growth rates are broadly comparable with G5 as a whole : faster than the US, slower than in Japan and (perhaps) Germany. ??

6. It is frequently said that reduction of imbalances requires faster growth of domestic demand in Japan and Germany than in the US. This is correct, but it is worth noting that the growth rate of domestic demand in Japan and Germany needs to be at least 1 per cent faster than in the US merely to stop the imbalances getting worse. It is only when the gap is substantially above 1 per cent that the relative growth rates of domestic demand make a significant contribution to reducing the imbalances. (This result is essentially because of the large excess of US imports over exports).

7. All this helps to show why most forecasts of the US current account deficit show such modest improvement by 1988. No doubt this is one factor, along with the perceived reluctance of the US - partly because of worries about their domestic banking system - to contemplate raising interest rates, helping to explain a widespread expectation of further dollar falls.

HPE

H P EVANS

CONFIDENTIAL

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NOMINAL INCOME GROWTH: IMF FORECASTS

| | 1984 | 1985 | 1986 | 1987 | 1988 |
|---|------|------|---------|--------|--------|
| US | 10½ | 6½ | 5½ | 5½ | 6½ |
| Japan | 6½ | 6 | 4½ | 4 | 6 |
| Germany | 5 | 5 | 6 | 4½ | 4 |
| France | 9 | 7½ | 6½ | 5 | 4½ |
| UK | 7 | 10 | 6 | 7 | 7 |
| G5 | 9 | 6½ | 5 | 5 | 6 |
| UK-latest HMT view | | | 7 | 7½ | 7½ |
| UK-MTFS (published FY figures in brackets) | | | 6½ (6½) | 6 (6½) | 6½ (6) |

Notes:

1. Money GDP at market prices.
2. WEP forecasts are generally close to IMF forecasts, except for Japan where WEP sees nominal growth of 3½ and 4½ per cent in 1987 and 1988 respectively.
3. No IMF forecasts yet available for Italy, Canada, and G7.

REAL DOMESTIC DEMAND GROWTH: IMF FORECASTS

| | 1984 | 1985 | 1986 | 1987 | 1988 |
|--------------------|------|------|------|------|------|
| US | 6½ | 2½ | 3½ | 2 | 2½ |
| Japan | 5 | 4½ | 4 | 4 | 4 |
| Germany | 3½ | 2½ | 4 | 3½ | 2½ |
| France | 1½ | 1½ | 3½ | 2½ | 2½ |
| UK | 3 | 3½ | 3½ | 3½ | 2½ |
| G5 | 5 | 3 | 3½ | 2½ | 3 |
| UK-latest HMT view | | | 3½ | 3½ | 2½ |

Notes:

1. Total domestic demand including stockbuilding.
2. WEP forecasts show higher domestic demand growth in Japan and Germany, in part because they assume some relaxation of the present policy stance.
3. No IMF forecasts yet available for Italy, Canada and G7.

INTERNATIONAL COMPARISONS

1. GDP/GNP growth

| | percentage change from year earlier | | |
|----------------|-------------------------------------|--------------------|--------------------|
| | 1985 | 1986 (estimate) | 1987 (forecast) |
| United Kingdom | 3.4 | 3.0 | 3.1 |
| United States | 2.7 | 2.5 | 2.7 |
| Japan | 4.7 | 2.4 | 3.1 |
| Germany | 2.5 | 2.5 | 2.9 |
| France | 1.4 | 2.4 | 2.5 |
| Italy | 2.3 | 2.7 | 3.2 |
| Canada | 4.0 | 3.5 | 2.9 |
| Major seven | 3.0 | 2.6 | 2.8 |
| EEC | 2.5 | 2.5 | 2.8 |

2. Inflation

| | percentage change from year earlier | | | |
|----------------|-------------------------------------|------|------------------|--------------------|
| | 1985 | 1986 | December 1986 | 1987 (forecast) |
| United Kingdom | 6.1 | 3.4 | 3.7 | 4.7 |
| United States | 3.5 | 2.0 | 1.1 | 3.5 |
| Japan | 2.1 | 0.4 | -0.3 | -0.6 |
| Germany | 2.2 | -0.3 | -1.1 | 0.1 |
| France | 5.8 | 2.5 | 2.1 | 2.7 |
| Italy | 9.2 | 6.4 | 4.8 | 4.3 |
| Canada | 4.0 | 4.1 | 4.2 | 2.8 |
| Major seven | 3.8 | 2.0 | 1.3 | 2.5 |
| EEC | 6.4 | 3.4 | 2.9 | 2.8 |

Note: WEP forecasts for 1987 except EEC (OECD forecast)

3. Current account

| | \$ billion (% of GDP) | | |
|----------------|-----------------------|--------------------|--------------------|
| | 1985 | 1986 (estimate) | 1987 (forecast) |
| United Kingdom | 5(1) | 0 (-) | -5(-1) |
| United States | -118(-3) | -141(-3½) | -157(-3½) |
| Japan | 49(½) | 87(4½) | 89(4) |
| Germany | 14(2) | 37(4) | 36(3) |
| France | 1(-) | 4(½) | 3(½) |
| Italy | -4(-1) | 8(1½) | 10(1½) |
| Canada | 0(-) | -7(-2) | -5(-1½) |
| Major seven | -53(-½) | -10(-) | -29(-½) |

Note: WEP forecasts

4. Unit labour costs in manufacturing

| | percentage change from year earlier | | |
|----------------|--|------|-------------|
| | 1984 | 1985 | latest |
| United Kingdom | 3.8 | 6.0 | 3.5 (Sept) |
| United States | -1.8 | 1.8 | -0.1 (Sept) |
| Japan | -5.3 | 1.9 | 1.1 (Sept) |
| Germany | -0.9 | 0.0 | 3.7 (Sept) |
| France | 3.5 | 2.1 | -0.4 (Q2) |
| Italy | 2.8 | 4.5 | -0.8 (Q2) |
| Canada | 1.9 | 2.2 | 4.2 (May) |

Notes: Figures for France and Italy from IMF, others from OECD.
Not adjusted for output relative to trend.

DEFICIT PROJECTIONS FOR MAJOR COUNTRIES

E

| | Deficit | % of GNP/GDP | General government deficit % GNP/GDP |
|--|---------|-----------------|--|
| <u>US Federal govt.</u> (\$ billion) | | | |
| FY1986 | 221 | 5.3 | 3.4 |
| Fy1987 | 173 | 4.4 | |
| <u>Japan central govt.</u> (Yen trillion) | | | |
| FY1986 | 11.5 | 3.4 | 1.5 |
| FY1987 | 10.5 | 3.0 | |
| <u>Germany central govt.</u> | | | |
| FY1986 | 23.0 | 1.2 | 1.0 |
| FY1987 | 22.3 | 1.1 | |
| <u>UK PSBR</u> (£ billion) | | | |
| FY1986 | 7.0 | 1.8 | 3.0 |
| FY1987 | 7.0 | 1.5 | |

Notes:

1. General government deficits shown are HMT estimates for calendar 1986.
2. All central government figures are government estimates. There is widespread doubt in the US about the extent of the reduction in FY1987. We, and most others, think \$190 bn more likely. In the case of Japan the supplementary budget expected in the Autumn could raise the projected deficit for FY1987 above 11 trillion yen.
3. FY1986 figures for the UK are based on the Autumn Statement. FY1987 figures are from last year's MTFs. More recent estimates are available.
4. FY1987 in the US runs from October 1986 to September 1987; in Germany from January to December 1987 and in Japan and the UK from April 1987 to March 1988.

INTEREST RATES IN THE G7

12 February 1987

| | Three Month money | Discount rate* | 10 year government bond yield |
|----------------|----------------------|-------------------|----------------------------------|
| United States | 6.1 | 5.5 | 7.3 |
| Japan | 4.0 | 3.0 | 4.8 |
| Germany | 4.0 | 3.0 | 6.2 |
| France | 8.4 | 8.0 | 8.9 |
| United Kingdom | 11.0 | 10.9 | 10.0 |
| Italy | 11.3 | 12.0 | 9.8 |
| Canada | 7.5 | 7.5 | 8.5 |

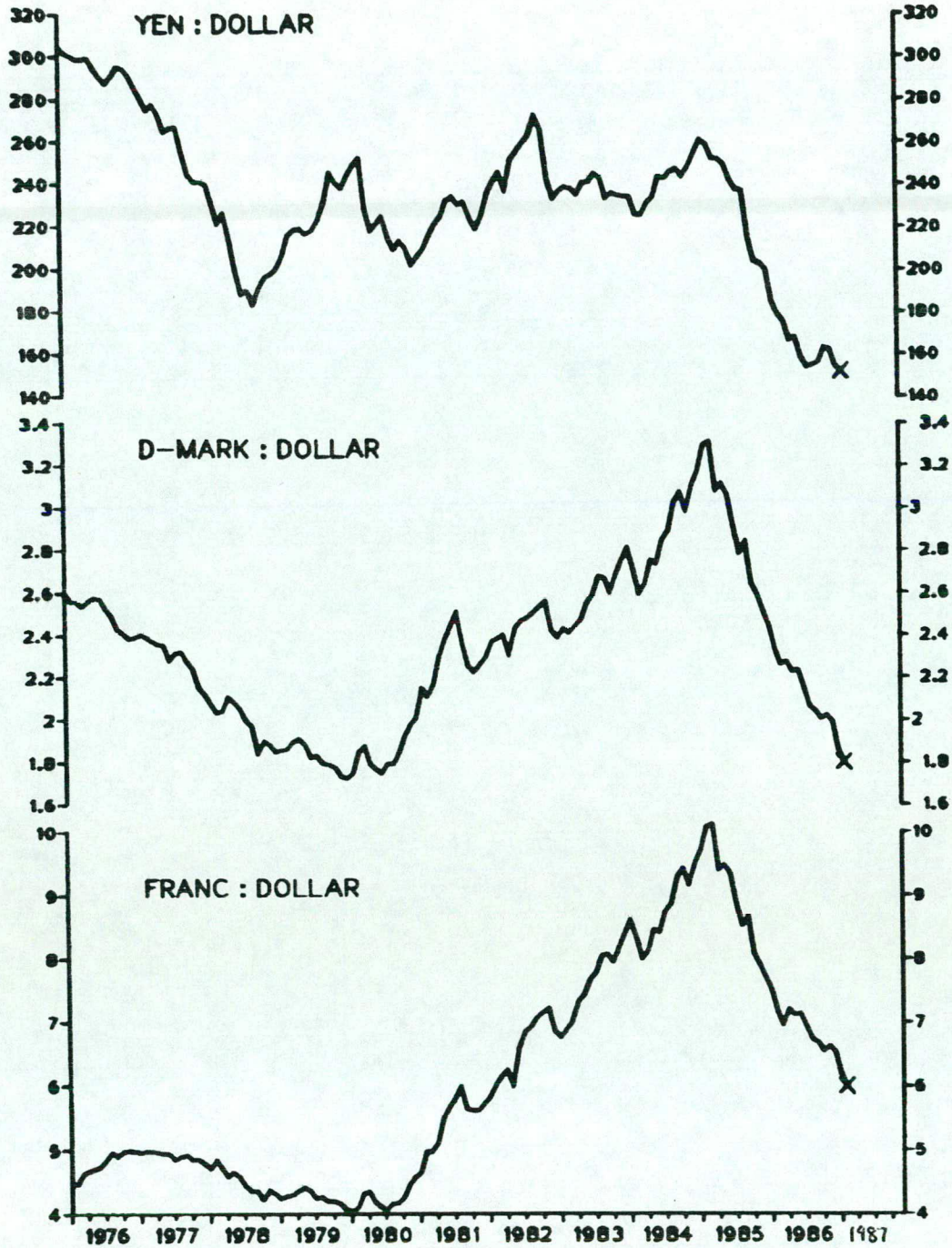
16 September 1985

| | Three Month money | Discount rate* | 10 year government bond yield |
|----------------|----------------------|-------------------|----------------------------------|
| United States | 8.0 | 7.5 | 10.3 |
| Japan | 6.3 | 5.0 | 6.2 |
| Germany | 4.7 | 4.0 | 6.6 |
| France | 9.8 | 9.6 | 10.9 |
| United Kingdom | 11.6 | 11.4 | 10.7 |
| Italy | 14.3 | 15.5 | 14.0 |
| Canada | 9.1 | 9.3 | 10.9 |

* Official lending rate to market. Discount rate in the US, Japan, Germany and Italy; rate at which 1st category paper is purchased by authorities in France; rate at which band one bills are purchased by authorities in the UK; and bank rate in Canada.

G

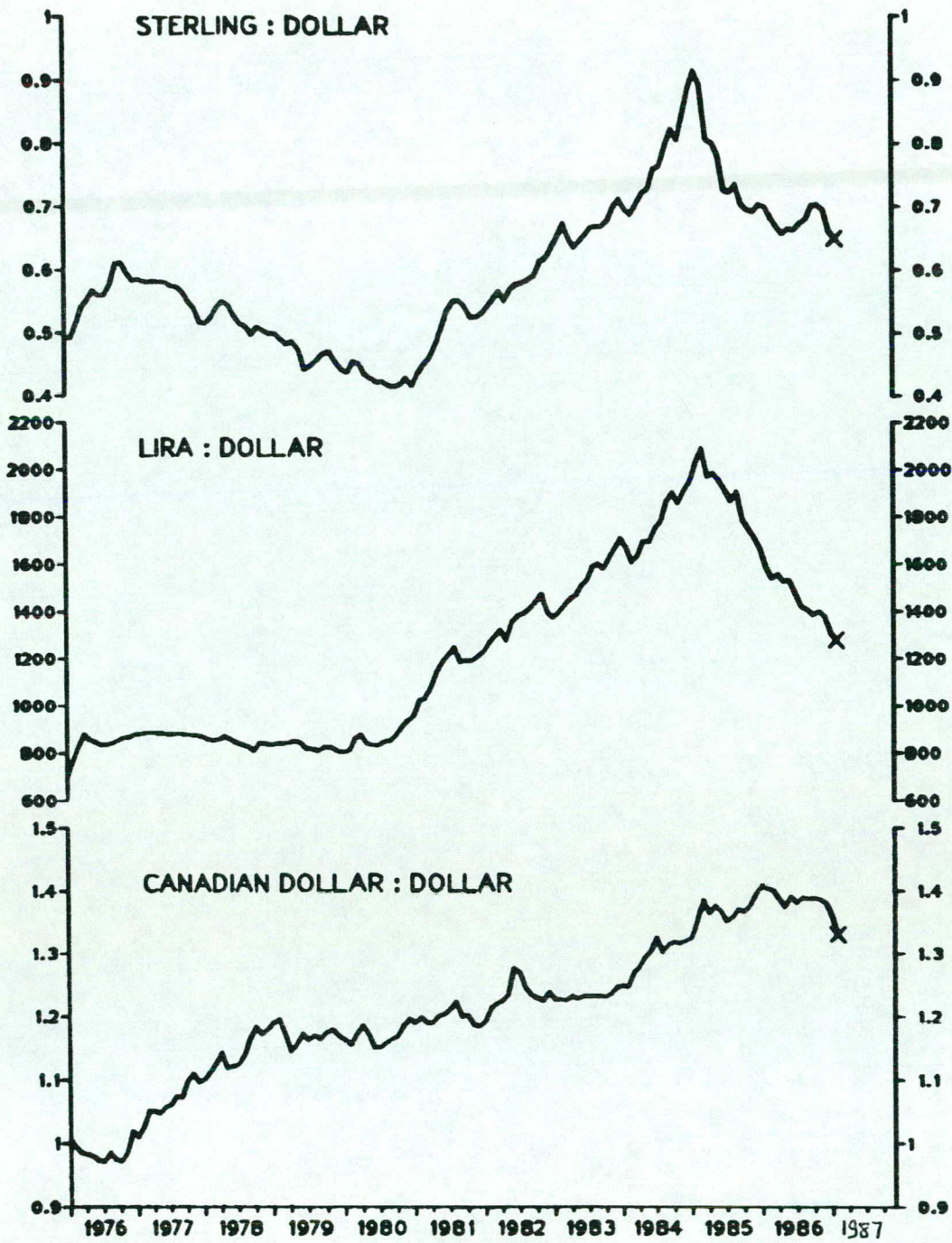
DOLLAR EXCHANGE RATES (MONTHLY AVERAGES)



X = 12th FEBRUARY

H

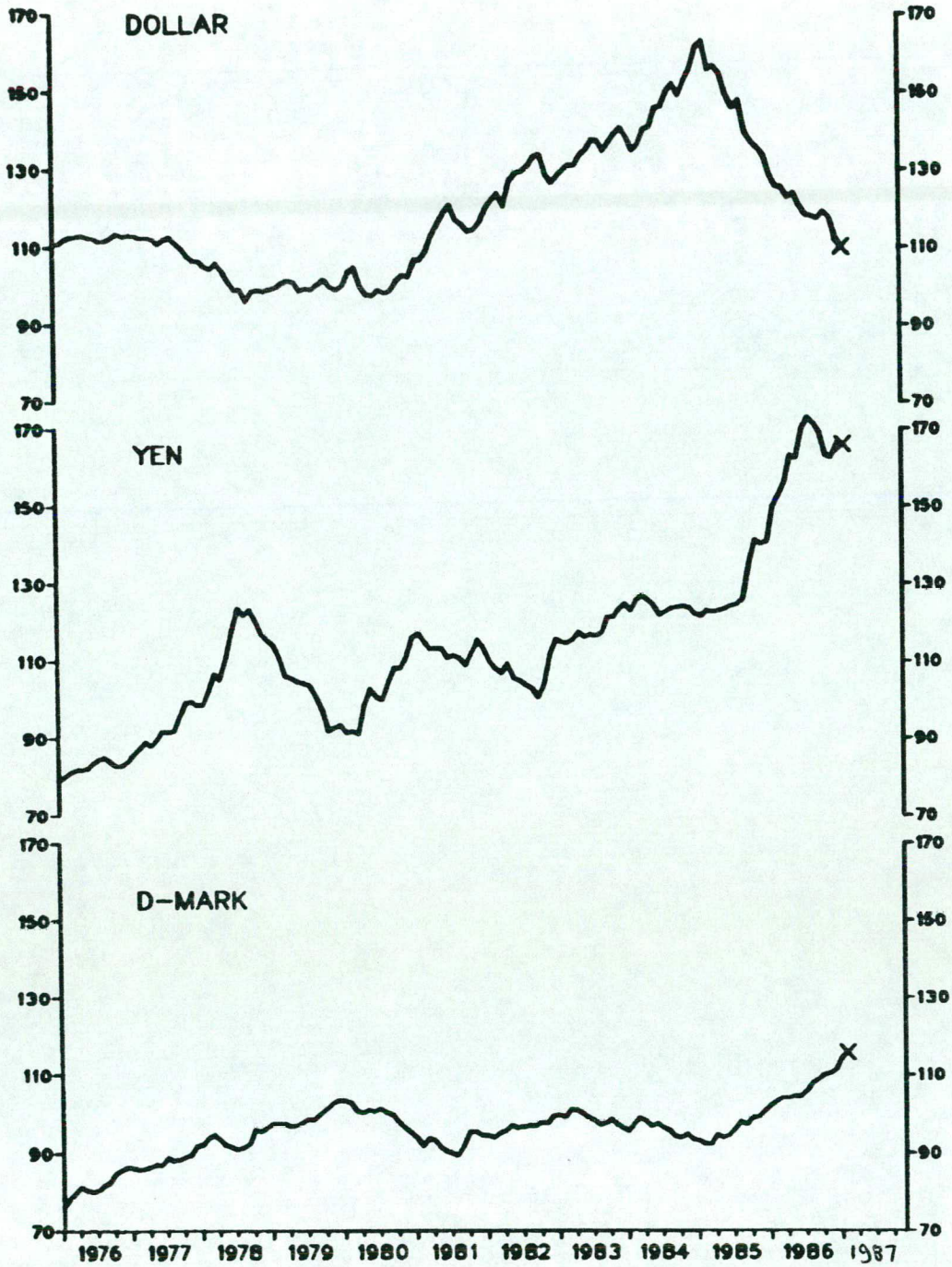
DOLLAR EXCHANGE RATES (MONTHLY AVERAGES)



X = 12th FEBRUARY

I

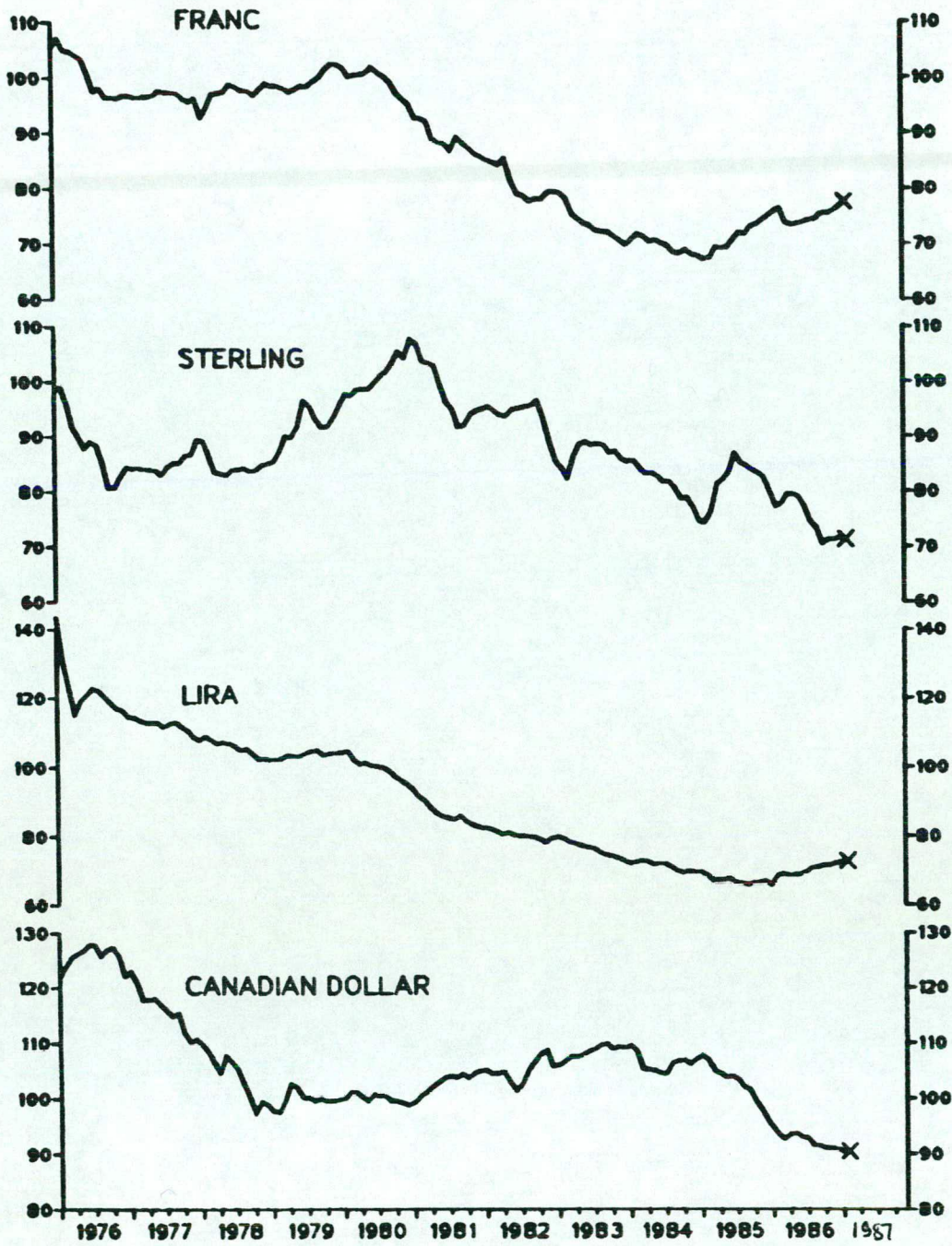
NOMINAL EFFECTIVE EXCHANGE RATES (IMF , 1980=100)



X = 12th FEBRUARY

J

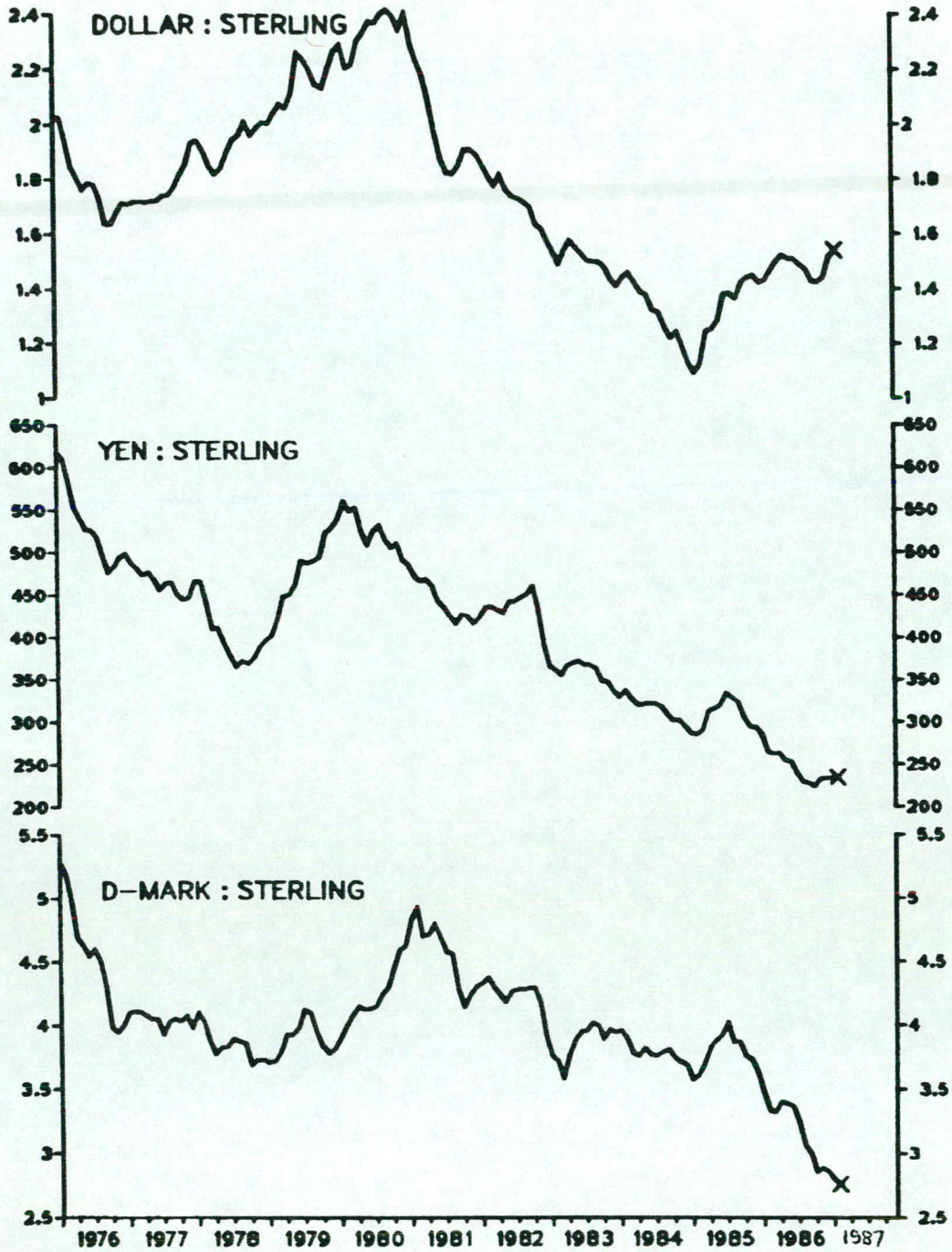
NOMINAL EFFECTIVE EXCHANGE RATES (IMF , 1980=100)



X = 12th FEBRUARY

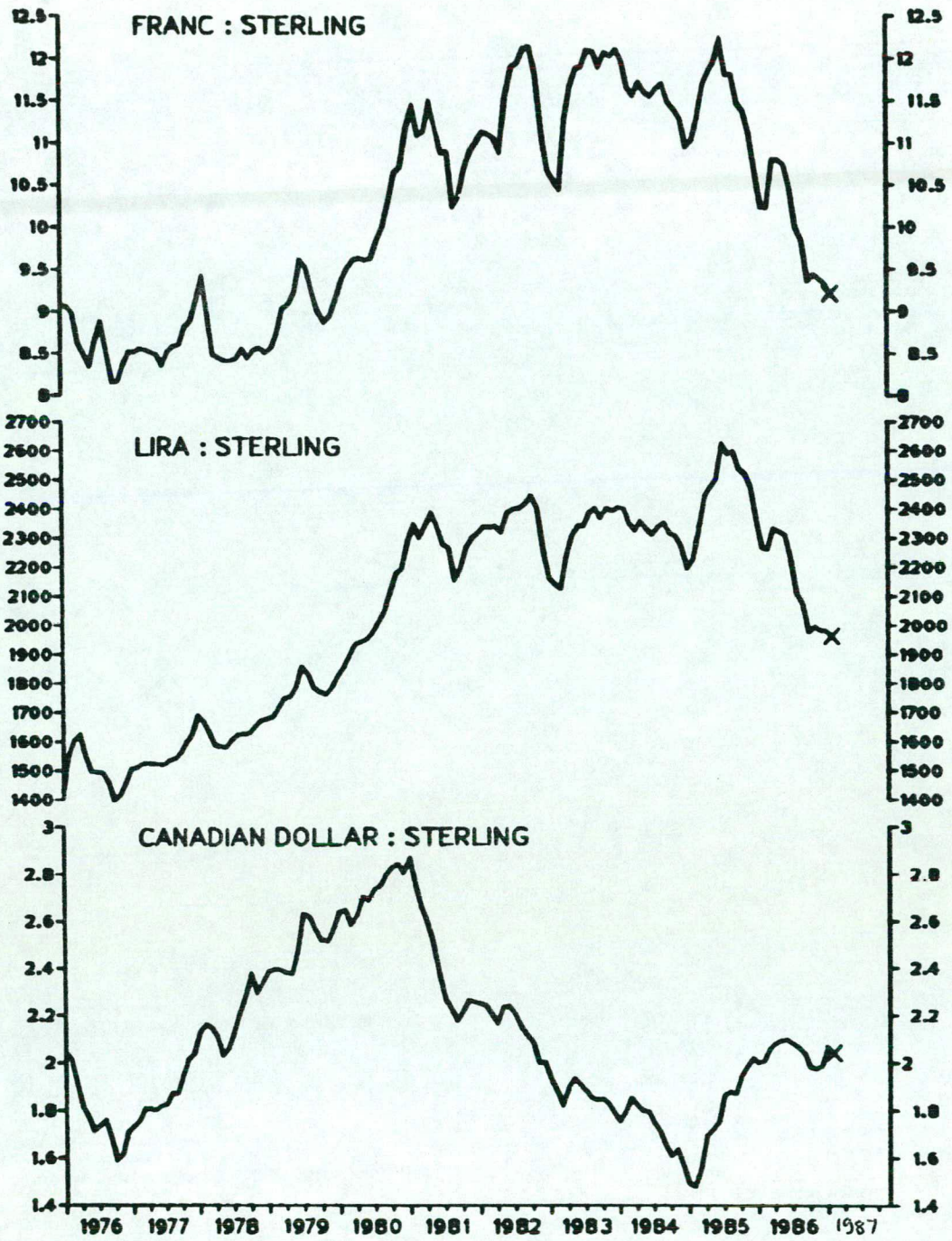
K

STERLING EXCHANGE RATES (MONTHLY AVERAGES)



X = 12th FEBRUARY

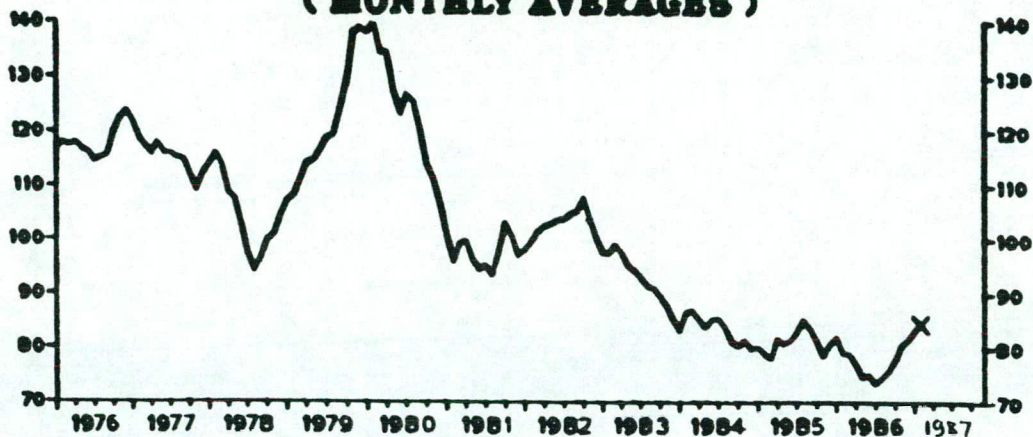
STERLING EXCHANGE RATES (MONTHLY AVERAGES)



X = 12th FEBRUARY

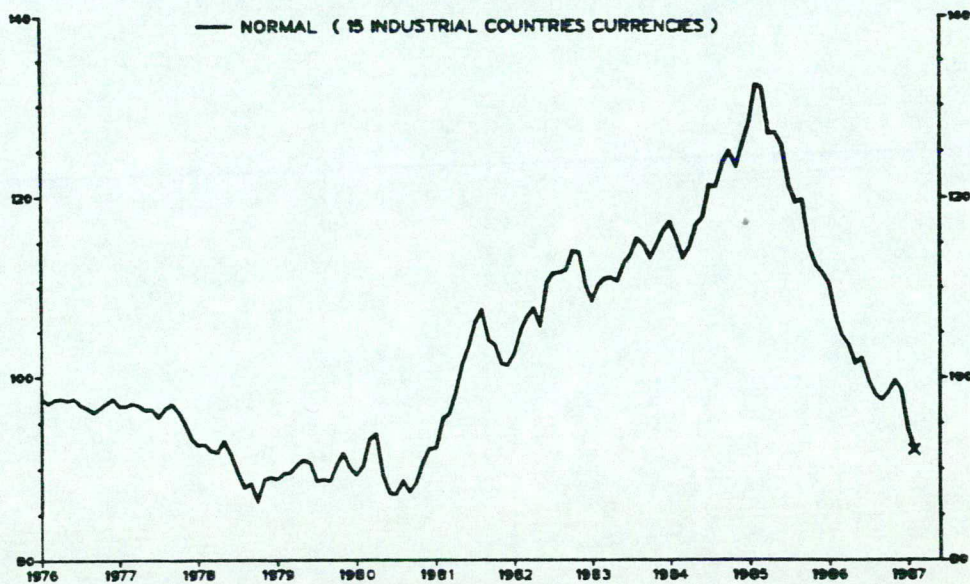
**YEN : D-MARK EXCHANGE RATE
(MONTHLY AVERAGES)**

M



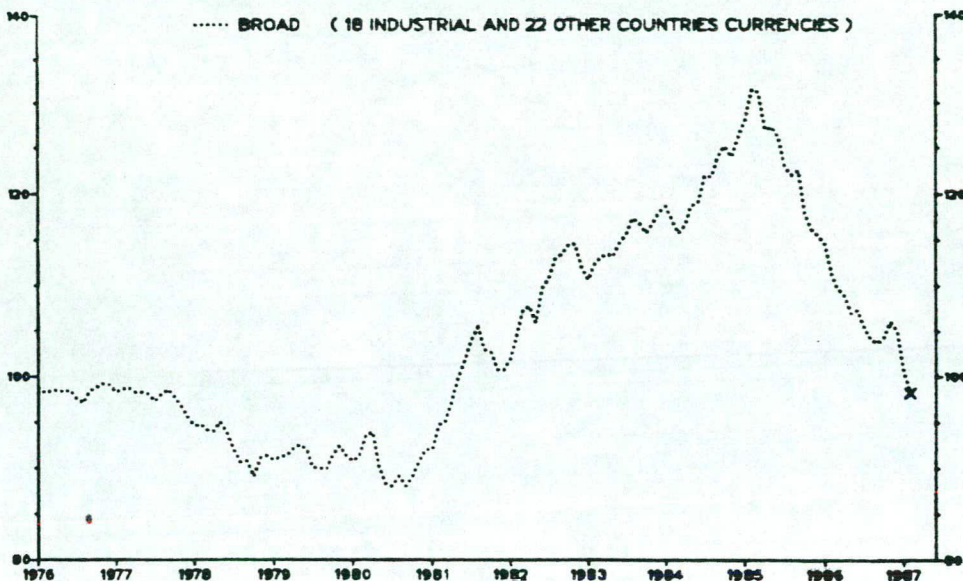
X = 12th FEBRUARY

**REAL DOLLAR EXCHANGE RATE
(MORGAN GUARANTY, 1980=82=100, MONTHLY AVERAGES)**



X = 12th FEBRUARY

**REAL DOLLAR EXCHANGE RATE
(MORGAN GUARANTY, 1980=82=100, MONTHLY AVERAGES)**



X = 12th FEBRUARY

Nominal exchange rate movements to date

| | Latest 12.2.87 | Dollar Peak 26.2.85 | % change to date | Plaza Agreement 20.9.85 | % change to date | 1986 Annual Meetings 30.9.86 | % change to date |
|-------------------------------|-------------------|------------------------|---------------------|----------------------------|---------------------|---------------------------------|---------------------|
| <u>Effective rates</u> | | | | | | | |
| (1975 = 100) | | | | | | | |
| United States | 104.1 | 157.2 | -34 | 139.6 | -25 | 110.2 | -6 |
| Japan | 208.3 | 157.1 | +33 | 156.6 | +33 | 216.7 | -4 |
| Germany | 148.7 | 117.2 | +27 | 125.5 | +18 | 140.9 | +6 |
| France | 72.5 | 62.0 | +17 | 67.2 | +8 | 70.0 | +4 |
| United Kingdom | 68.7 | 70.2 | -2 | 82.0 | -16 | 69.0 | 0 |
| Italy | 48.7 | 45.1 | +8 | 44.0 | +11 | 47.7 | +2 |
| Canada | 77.8 | 88.5 | -12 | 85.5 | -9 | 77.0 | +1 |
| <u>Bilateral rates</u> | | | | | | | |
| Yen/\$ | 154 | 261 | +69 | 240 | +56 | 154 | 0 |
| DM/\$ | 1.83 | 3.43 | +87 | 2.84 | +55 | 2.03 | +11 |
| FFI/\$ | 6.07 | 10.50 | +73 | 8.68 | +43 | 6.64 | +9 |
| £/\$ | .66 | .95 | +44 | .73 | +11 | .69 | +5 |
| Lire/\$ | 1298 | 2166 | +67 | 1922 | +48 | 1402 | +8 |
| C\$/ \$ | 1.35 | 1.41 | +4 | 1.38 | +2 | 1.39 | +3 |
| \$/£ | 1.52 | 1.05 | | 1.37 | | 1.45 | |

Not Changes in bilateral rates show appreciation of currency against dollar

STERLING EXCHANGE RATES

P

| | Dollar | Yen | D-mark | Franc | Lira | C.dollar |
|----------|--------|-----|--------|-------|------|----------|
| 1985 Jan | 1.13 | 287 | 3.58 | 10.9 | 2200 | 1.49 |
| Feb | 1.09 | 285 | 3.61 | 11.0 | 2230 | 1.48 |
| Mar | 1.12 | 290 | 3.70 | 11.3 | 2340 | 1.55 |
| Apr | 1.24 | 312 | 3.83 | 11.7 | 2450 | 1.69 |
| May | 1.25 | 315 | 3.88 | 11.8 | 2480 | 1.72 |
| Jun | 1.28 | 319 | 3.92 | 12.0 | 2500 | 1.75 |
| Jul | 1.37 | 333 | 4.02 | 12.2 | 2620 | 1.86 |
| Aug | 1.38 | 328 | 3.87 | 11.8 | 2590 | 1.88 |
| Sep | 1.37 | 323 | 3.87 | 11.8 | 2600 | 1.87 |
| Oct | 1.42 | 305 | 3.76 | 11.5 | 2540 | 1.94 |
| Nov | 1.44 | 294 | 3.73 | 11.4 | 2520 | 1.98 |
| Dec | 1.45 | 293 | 3.63 | 11.1 | 2480 | 2.02 |
| 1986 Jan | 1.42 | 285 | 3.47 | 10.7 | 2370 | 2.00 |
| Feb | 1.43 | 264 | 3.34 | 10.2 | 2270 | 2.01 |
| Mar | 1.47 | 262 | 3.33 | 10.2 | 2260 | 2.06 |
| Apr | 1.50 | 262 | 3.40 | 10.8 | 2330 | 2.08 |
| May | 1.52 | 254 | 3.39 | 10.8 | 2320 | 2.09 |
| Jun | 1.51 | 253 | 3.37 | 10.7 | 2310 | 2.10 |
| Jul | 1.51 | 239 | 3.25 | 10.5 | 2230 | 2.08 |
| Aug | 1.49 | 229 | 3.07 | 10.0 | 2110 | 2.06 |
| Sep | 1.47 | 228 | 3.00 | 9.8 | 2070 | 2.04 |
| Oct | 1.43 | 223 | 2.86 | 9.4 | 1980 | 1.98 |
| Nov | 1.43 | 232 | 2.88 | 9.4 | 2000 | 1.97 |
| Dec | 1.44 | 233 | 2.86 | 9.4 | 1980 | 1.98 |
| 1987 Jan | 1.51 | 233 | 2.80 | 9.3 | 1980 | 2.06 |
| Feb 12 | 1.52 | 234 | 2.77 | 9.2 | 1970 | 2.05 |

DOLLAR EXCHANGE RATES

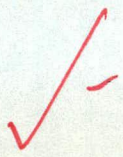
Q

| | Yen | D-mark | Franc | Sterling | Lira | C.dollar |
|----------|-----|--------|-------|----------|------|----------|
| 1985 Jan | 254 | 3.17 | 9.70 | .98 | 1950 | 1.32 |
| Feb | 260 | 3.30 | 10.12 | .94 | 2040 | 1.25 |
| Mar | 258 | 3.30 | 10.09 | .94 | 2080 | 1.37 |
| Apr | 251 | 3.08 | 9.41 | .99 | 1970 | 1.36 |
| May | 252 | 3.11 | 9.47 | .99 | 1980 | 1.38 |
| Jun | 249 | 3.06 | 9.34 | .98 | 1950 | 1.37 |
| Jul | 241 | 2.91 | 8.87 | .93 | 1900 | 1.35 |
| Aug | 237 | 2.79 | 8.54 | .90 | 1880 | 1.36 |
| Sep | 237 | 2.84 | 8.66 | .91 | 1900 | 1.37 |
| Oct | 215 | 2.64 | 8.06 | .85 | 1780 | 1.37 |
| Nov | 204 | 2.59 | 7.90 | .84 | 1750 | 1.38 |
| Dec | 203 | 2.51 | 7.68 | .82 | 1710 | 1.40 |
| 1986 Jan | 200 | 2.44 | 7.49 | .80 | 1660 | 1.41 |
| Feb | 185 | 2.33 | 7.16 | .77 | 1590 | 1.40 |
| Mar | 179 | 2.27 | 6.97 | .75 | 1540 | 1.40 |
| Apr | 175 | 2.27 | 7.20 | .75 | 1560 | 1.39 |
| May | 167 | 2.23 | 7.11 | .73 | 1530 | 1.38 |
| Jun | 168 | 2.23 | 7.12 | .73 | 1530 | 1.39 |
| Jul | 159 | 2.15 | 6.93 | .72 | 1480 | 1.38 |
| Aug | 154 | 2.06 | 6.72 | .74 | 1420 | 1.39 |
| Sep | 155 | 2.04 | 6.68 | .74 | 1410 | 1.39 |
| Oct | 156 | 2.00 | 6.56 | .73 | 1390 | 1.39 |
| Nov | 163 | 2.02 | 6.62 | .74 | 1400 | 1.39 |
| Dec | 162 | 1.99 | 6.53 | .73 | 1380 | 1.38 |
| 1987 Jan | 155 | 1.86 | 6.19 | .69 | 1320 | 1.36 |
| Feb 12 | 154 | 1.83 | 6.07 | .66 | 1300 | 1.35 |

EFFECTIVE EXCHANGE RATES (IMF MEASURE, 1980 = 100)

| | US | Japan | Germany | France | UK | Italy | Canada |
|----------|-------|-------|---------|--------|------|-------|--------|
| 1985 Jan | 155.9 | 122.1 | 93.2 | 67.8 | 74.5 | 69.4 | 107.7 |
| Feb | 161.3 | 121.6 | 92.3 | 67.2 | 74.4 | 68.6 | 106.9 |
| Mar | 162.7 | 122.9 | 92.3 | 67.3 | 76.4 | 66.9 | 104.9 |
| Apr | 155.9 | 122.5 | 94.5 | 69.2 | 81.2 | 67.3 | 104.5 |
| May | 156.5 | 122.9 | 94.0 | 69.1 | 82.0 | 67.2 | 103.8 |
| Jun | 154.8 | 123.3 | 94.0 | 69.3 | 83.3 | 67.5 | 104.0 |
| Jul | 149.2 | 124.1 | 94.4 | 70.7 | 86.8 | 66.4 | 103.5 |
| Aug | 146.0 | 124.5 | 96.0 | 71.9 | 85.1 | 66.1 | 102.1 |
| Sep | 147.7 | 125.8 | 98.0 | 71.6 | 84.6 | 65.7 | 101.6 |
| Oct | 139.6 | 134.7 | 97.3 | 73.0 | 83.8 | 66.3 | 99.5 |
| Nov | 137.1 | 141.0 | 99.1 | 73.4 | 83.3 | 66.4 | 98.1 |
| Dec | 135.6 | 140.2 | 100.8 | 74.2 | 82.5 | 66.7 | 96.2 |
| 1986 Jan | 133.7 | 140.7 | 102.1 | 74.9 | 79.9 | 65.6 | 94.7 |
| Feb | 128.5 | 149.8 | 103.3 | 75.8 | 77.3 | 68.4 | 93.4 |
| Mar | 125.7 | 152.5 | 104.1 | 76.2 | 77.6 | 68.9 | 92.7 |
| Apr | 125.3 | 155.8 | 104.0 | 73.7 | 79.3 | 68.5 | 93.5 |
| May | 122.7 | 162.8 | 104.5 | 73.4 | 79.4 | 68.6 | 93.7 |
| Jun | 123.7 | 162.4 | 104.5 | 73.5 | 79.0 | 68.8 | 93.0 |
| Jul | 120.6 | 169.9 | 105.8 | 73.7 | 77.1 | 69.4 | 92.8 |
| Aug | 118.2 | 172.8 | 107.9 | 74.2 | 74.3 | 70.5 | 91.5 |
| Sep | 117.8 | 171.4 | 108.8 | 74.3 | 73.3 | 70.8 | 91.5 |
| Oct | 117.2 | 169.4 | 110.0 | 75.3 | 70.5 | 71.4 | 91.1 |
| Nov | 118.8 | 163.1 | 110.3 | 75.4 | 71.2 | 71.5 | 91.0 |
| Dec | 117.6 | 162.6 | 111.2 | 75.7 | 71.2 | 72.0 | 90.9 |
| 1987 Jan | 112.6 | 166.1 | 114.3 | 76.6 | 71.6 | 72.3 | 90.5 |
| Feb 12 | 110.0 | 165.5 | 115.7 | 77.3 | 71.4 | 71.4 | 90.4 |

PO



PPS/Chancellor
12/2

AA, BCC,

NNNN

CN RIM703

140433 :/JAPAN SEES PROSPECT FOR G-5 NEXT WEEK, PAPER SAYS
TOKYO, Feb 14 - Japanese government and Bank of Japan
sources, quoted by the Sankei Shimbun newspaper, said there are
prospects for a Group of Five (G-5) meeting next week.
The paper quoted the sources as saying the meeting, to
discuss currency stability, could take place around February
21, or earlier.
Bank of Japan and Finance Ministry officials were
unavailable for comment.
REUTER

pup.

I must tell the Japs
to shut down traps.

Pps. Chancellor
12/2

170051 :/MIYAZAWA SAYS G-5 TRYING TO MEET, NO NEW PROGRESS **AA; BCC; i**
TOKYO, Feb 17 - Finance Minister Kiichi Miyazawa said the Group of Five (G-5) nations was still making efforts to hold a meeting this weekend, though there had been no new progress.
He told a press conference he expected to know in about two days if the G-5 would meet this weekend to discuss currency stability.
Asked if he had heard anything about the possibility of a joint statement by the G-5 without a meeting being held, Miyazawa said he had no knowledge of it.
REUTER

87-02-18 19:50

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262405 TRSY G
ECOFIN 214079F

FROM : E. BALLADUR
MINISTER OF STATE
MINISTER OF ECONOMI, FINANCE AND PRIVATISATION.

TO

HIS EXCELLENCY JAMES BAKER III
SECRETARY OF THE TREASURY
WASHINGTON DC

RT. HON. NIGEL LAWSON, P.C MP
CHANCELLOR OF THE EXCHEQUER
HM TREASURY - LONDON

HIS EXCELLENTY KIICHI MIAZAWA
MINISTER OF FINANCE
TOKYO

HERR DR GERHARD STOLTENBERG
AN DEN BUNDESMINISTER DER FINANZEN
BONN

PERSONAL AND CONFIDENTIAL

| CH/EXCHEQUER | |
|--------------|------------------|
| REC. | 19 FEB 1987 |
| ACTION | SIR G. LITTLE |
| COPIES TO | SIR P. MIDDLETON |
| | MR LAVELLE |
| | MR H. P. EVANS |
| | MR PERETZ |
| | MR CULPIN |

DEAR FRIEND,

FOLLOWING THE RECENT DISCUSSIONS AMONG OUR DEPUTIES AND FURTHER TELEPHONE TALKS BETWEEN P OURSELVES, A MEETING OF OUR SMALL GROUP NOW SEEMS TO BE USEFUL. THUS I HAVE THE PLEASURE TO CONVINCE YOU IN PARIS, FEBRUARY 21ST AND 22 ND, TOGETHER WITH YOUR DEPUTY AND THE GOVERNOR OF YOUR CENTRAL BANK. I WOULD APPRECIATE IF YOU COULD ADVISE THEM.

OUR G5 MEETING WILL OF COURSE REMAIN INFORMAL AND CONFIDENTIAL. THE G5 MEETING COULD BEGIN AT 3 P.M. ON SATURDAY, PROVIDED THAT MR MIYAZAWA MANAGES TO JOIN PARIS IN TIME. WERE IT IMPOSSIBLE, I WOULD CONFIRM THE STARTING HOUR BY TELEX TOMORROW.

THE TIME TABLE AND AGENDA COULD BE AS FOLLOWS :

SATURDAY 3 PM: 65 WORKING SESSION

3-4 MULTINLATERAL SURVEILLANCE
(WITH THE MANAGING DIRECTOR)

4-5.30 COMMUNIQUE

5.30-7 EXCHANGE MARKET AND INTERVENTIO

NS

7 PM : COCKTAILS

7.30 PM :65 WORKING DINNER

PRESS CONFERENCE, 65/67, COORDINATION
AND INDICATORS, NEXT MEETINGS, OTHER
ITEMS

SUNDAY

9.30 AM: 67 WORKING SESSION

9.30-10.30 MULTILATERAL SURVEILLANCE
(WITH THE MANAGING DIRECTOR)

10.30-12.30 COMMUNIQUE, COORDINATION
INDICATORS

12.30 PM : COCKTAILS

12.45 PM :67 WORKING LUNCH

PRESS CONFERENCE, NEXT
MEETING, OTHER ITEMS

2.30 PM : JOINT PRESS CONFERENCE

ALL OUR WORKING MEETINGS, LUNCH AND DINNER WILL
TAKE PLACE IN THE LOUNGE OF MINISTRY 93 RUE DE RIVOLI - PARIS 1ER.

I HAVE ASKED CHIEF CZABINET, M. BENON, (TELEPHONE
47.03.32.72) TO DEAL WITH ALL MATERIAL PROVISIONS. I WOULD BE
GRATEFUL IF YOU COULD DESIGNATE AS SOON POSSIBLE YOUR ASSOCIATE
WHO COULD ACT AS HIS OPPOSITE NUMBER. THE EARLIER CONTACT BETWEEN
THEM WOULD BE THE BETTER.

YOURS FRIENDLY.

SIGNX : EDOUARD BALLADUR.

ROM : E. BALLADUR
MINISTER OF STATE
MINISTER OF ECONOMY, FINANCE AND PRIVATISATION.

TO

HIS EXCELLENCY JAMES BAKER III
SECRETARY OF THE TREASURY
WASHINGTON DC

EX GIOVANNI BORIA
MINISTRO DEL TESORO
ROMA

TR. HON. BIGEL LAWSON P.C. MP
CHANCELLOR OF THE EXCHEQUER
HM TREASURY - LONDON

HIS EXCELLENCY KIICHI MIYAZAWA
MINISTER OF FINANCE
TOKYO

HERR DR GERHARD STOLTENBERG
AN DEN BUNDESMINISTER DER FINANZEN
BONN

HIS EXCELLENCY MICHAEL WILSON
MINISTER OF FINANCE
OTTAWA

DREAR FRIEND,

FOLLOWING THE RECENT DISCUSSIONS AMONG OUR DEPUTIES IN
ROME AND INFORMAL CONVERSATIONS I HAD WITH SEVERAL OF OUR C
COLLEAGUES, A MEETING OF OUR SMALL GROUP NOW SEEMS TO BE USEFUL
THUS I HAVE THE PLEASURE TO CONVENE YOU IN PARIS ON SUNDAY
FEBRUARY, 22 ND

THE TIME TABLE AND AGENDA COULD BE AS FOLLOWS :

SY SUNDAY 9.30 AM : WORKING SESSION
9.30-10.30 MULTILATERAL SURVEILLANCE
(WITH THE MANAGING DIRECTOR)

10.30-12.30 COMMUNIQUE, COORDINATION AND INDICATORS
12.30 PM : COCKTAILS
12.45 PM : WORKING LUNCH
PRESS CONFERENCE, NEXT MEETING
OTHER ITEMS

2.30 PM : JOINT PRESS CONFERENCE

OUR WORKING SESSION AND LUNCH WILL TAKE PLACE IN THE
LOUNGE OF MY MINISTRY, 93 RUE DE RIVOLI - PARIS 1ER.

I HVE ASKED MY CHEF CABINET, M. BENON (TELEPHONE
47.03.32.72) TO DEAL WITH ALL MATERIAL PROVISIONS. I WOULD BE
GRATEFUL IF YOU COULD DESIGNATE AS SOON AS POSSIBLE YOUR
ASSOCIATE WHO COULD ACT AS HIS OPPOSITE NUMBER. THE EARLIER
CONTACT BETWEEN THEM WOULD BE THE BETTER.

YOUR FRIENDLY.

SIGNX : EDOUARD BALLADUR. *

BIG SEVEN IN ECONOMY TALKS

PARIS, THURSDAY - FINANCE MINISTERS AND CENTRAL BANKERS FROM THE SEVEN LARGEST WESTERN INDUSTRIALISED NATIONS WILL MEET SUNDAY IN THE PARIS AREA, FRENCH GOVERNMENT SOURCES SAID.

OFFICIALS SAID CANADA AND ITALY WOULD BE REPRESENTED AT THE MEETING, AS WELL AS THE NATIONS IN THE "GROUP OF FIVE" -- FRANCE, BRITAIN, JAPAN, WEST GERMANY AND THE US.

FRENCH OFFICIALS WOULD NOT COMMENT ON SPECULATION THAT THE SMALLER GROUP, KNOWN AS G-5, WOULD GATHER ON SATURDAY TO DISCUSS WAYS OF CALMING RECENT TURBULENCE IN THE CURRENCY MARKETS.

THEY ALSO WOULD NOT SPECIFY WHERE SUNDAY'S TALKS WOULD TAKE PLACE. HOWEVER, THE WALL STREET JOURNAL, QUOTING UNNAMED MONETARY SOURCES, TODAY REPORTED THAT THE UNITED STATES AND ITS ALLIES HAVE TENTATIVELY AGREED TO TRY TO LIMIT THE DOLLAR'S FLUCTUATIONS IN RETURNED FOR PROMISES BY WEST GERMANY AND JAPAN TO CONSIDER NEW MEASURES TO STIMULATE THEIR ECONOMIES.

THE SOURCES WERE QUOTED AS SAYING THE MONETARY OFFICIALS WOULD ACCEPT THE CURRENT DOLLAR LEVEL, BUT THAT THE ACCORD FALLS SHORT OF ESTABLISHING CEILINGS AND FLOORS FOR THE DOLLAR, THE DEUTSCHMARK AND THE YEN. OFFICIALS HAVE REFUSED TO CONFIRM THE REPORT.

EARLIER, FRENCH FINANCE MINISTER EDOUARD BALLADUR DECLINED TO CONFIRM THE SEVEN NATIONS WOULD MEET. HOWEVER, OFFICIALS IN WEST GERMANY AND JAPAN SAID THE FINANCE MINISTERS AND CENTRAL BANK GOVERNORS WOULD GATHER IN PARIS.

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G5 TALKS SEEM DESIGNED TO END POLICY CLASH BY PETER TORDAY, REUTERS
WASHINGTON, FEBRUARY 19

THIS WEEKEND'S MEETING OF THE FIVE LEADING INDUSTRIAL POWERS IS DESIGNED TO END DAMAGING INTERNATIONAL CLASHES OVER ECONOMIC POLICY BUT MAY FALL SHORT OF HARDER CALLS ON CURRENCIES AND ECONOMIC GROWTH, MONETARY SOURCES FAMILIAR WITH THE NEGOTIATIONS SAY. NEVERTHELESS, AN AGREEMENT TO STABILISE FOREIGN EXCHANGE RATES AND A FIRM COMMITMENT TO BOLSTER GLOBAL GROWTH IS EXPECTED TO BE ISSUED AFTER THEIR MEETINGS IN PARIS. STILL TO BE DECIDED, HOWEVER, IS THE EXTENT TO WHICH MAJOR COUNTRIES, THE UNITED STATES JAPAN, WEST GERMANY, BRITAIN AND FRANCE WILL INTERVENE TO KEEP THEIR CURRENCY STABLE. ALSO UNRESOLVED IS HOW OFTEN AND UNDER WHAT CIRCUMSTANCES THEY WILL CONSULT BEFORE TAKING ACTION, THE SOURCES SAID. AFTER THEIR MEETINGS ON SATURDAY, THE FIVE WILL BE JOINED BY ITALY AND CANADA FOR FORMAL TALKS OF THE GROUP OF 7. THE FIVE WILL BE REPRESENTED BY THEIR FINANCE MINISTERS AND CENTRAL BANKERS AND THE BANKERS MAY ALSO PARTICIPATE IN THE MEETINGS OF THE SEVEN MINISTERS, THE SOURCES SAID. AMERICA'S TWO LEADING ECONOMIC POLICY MAKERS, TREASURY SECRETARY JAMES BAKER AND FEDERAL RESERVE BOARD CHAIRMAN PAUL VOLCKER BOTH URGED JAPAN AND WEST GERMANY TODAY TO FORCE A GLOBAL ECONOMIC UPTURN, AND SO CURB THE HUGE US TRADE DEFICIT AND REDUCE THEIR OWN VERY LARGE TRADE SURPLUSES. "EVERYBODY WILL HAVE SOMETHING" SAID ONE SOURCE WHEN ASKED ABOUT ECONOMIC POLICY COMMITMENTS TO BE MADE BY THE SEVEN

COUNTRIES. BUT NONE WOULD INVOLVE DRASTIC OR CONTROVERSIAL POLICY CHANGES, SEVERAL SOURCES SAID. THEY SAID THAT IN A COMMUNIQUE PREPARED FOR ISSUE AFTER THIS WEEKEND'S MEETING, WEST GERMANY WILL OPT TO STIMULATE IT'S ECONOMY, BRINGING FORWARD PLANNED TAX CUTS ONLY IF THERE ARE SIGNS THAT ECONOMIC GROWTH IS FALTERING. IN SIMILAR CIRCUMSTANCES, THE SOURCES SAID THE JAPANESE GOVERNMENT WOULD UNDERTAKE TO PRESENT A NEW BUDGET TO IT'S PARLIAMENT AND BOOST CONSTRUCTION SPENDING. A FRESH JAPANESE DISCOUNT RATE CUT IS ALSO EXPECTED TO OCCUR AS PART OF TOYKIO'S CONTRIBUTION TO THE AGREEMENT AND THE US WILL UNDERTAKE TO REDOUBLE IT'S EFFORTS TO CUT IT'S HUGE BUDGET DEFICIT, SEEN BY POLICY MAKERS HERE AND ABROAD AS A FUNDAMENTAL CAUSE OF ECONOMIC INSTABILITY. WASHINGTON HAS OBVIOUSLY HAD DIFFICULTY COUNTERING WEST GERMAN ARGUMENTS IT CANNOT DELIVER DEFICIT CUTS WITHOUT CHANGING POLICIES TO SUIT CONGRESS. AND THEREFORE, THE GERMAN POSITION RUNS, WHY SHOULD BONN CHANGE IT'S POLICY SO SHARPLY. "WHAT IS REQUIRED IS COMPLIMENTARY ACTIONS HERE AND ABROAD ON BUDGETS, ON MONETARY POLICIES, AND ON MAINTAINING APPROPRIATE EXCHANGE RATES AND AN OPEN TRADING ORDER" VICKER TOLD CONGRESS IN A PREVIEW OF THE MEETINGS TO CONGRESS TODAY. BUT STILL UNRESOLVED IS HOW THE THREE MIGHTIEST INDUSTRIAL POWERS WILL RESOLVE THEIR DEBATE OVER CURRENCIES. THE SOURCES SAID REFERENCE RANGES—BROAD UPPER AND LOWER LIMITS FOR CURRENCIES THAT COULD BE DEFENDED WITH INTERVENTION—WERE DISCUSSED IN THE NEGOTIATIONS LEADING UP TO THE MEETING. AT ONE POINT, ACCORDING TO SOME SOURCES, RANGES OF 1.70 TO 1.90 MARKS TO THE DOLLAR AND 140 TO 165 YEN TO THE DOLLAR WERE PUT ON THE TABLE. BUT JAPAN IN PARTICULAR HAS RESISTED THE ISSUE,

LARGELY BECAUSE IT FEARS THE RANGE IMPLIES THE YEN MUST RISE TO. THERE IS A BROAD CONSENSUS IN JAPAN THAT 150 YEN TO THE DOLLAR IS THE HIGHEST LEVEL THE COUNTRY'S EXPORT INDUSTRY WILL TOLERATE. MUCH OF THE GENUINE DEBATE, THEREFORE, WILL CENTRE ON WHETHER RANGES CAN BE FORMALLY DISCUSSED AND THE DEGREE TO WHICH THEY WOULD COMPEL ACTION. BOTH BONN AND TOKYO FEAR RIGID COMMITMENTS TO DEFEND CURRENCY RANGES WITH OFFICIAL SALES OR PURCHASES OF CURRENCIES. THERE HAS BEEN SOME DISCUSSIONS OF WHETHER AUTOMATIC CONSULTATIONS ON ECONOMIC POLICY WOULD BE TRIGGERED BY WILDLY FLUCTUATING EXCHANGE RATES. BUT MOST ANALYSTS AGREE WITH VOLCKER'S VIEW REPEATED TODAY THAT REFERENCE RANGES ONLY WORK IF BACKED UP BY APPROPRIATE ECONOMIC POLICY. IT IS GENERALLY ACKNOWLEDGED THAT NO GOVERNMENT IS POWERFUL ENOUGH TO STOP THE CURRENCY MARKETS WHICH HAVE AN ESTIMATED VOLUME OF SOME 150 BILLION DOLLARS A DAY IF IT IS DEFENDING RATES THAT ARE WILDLY OUT OF LINE WITH ECONOMIC REALITY. "THE GERMANS HAVE REAL DIFFICULTIES WITH ANYTHING THAT IS TOO RIGID" ONE SOURCE SAID. AND GOVERNMENT OFFICIALS TOLD REUTERS IN TOKYO THAT MORE TIME WAS NEEDED TO STUDY THE PLAN. THOSE OFFICIALS AND SOURCES HERE, DID SAY A COMMUNIQUE WOULD AT THE LEAST CONTAIN LANGUAGE REAFFIRMING THAT THE CURRENCIES IS OF THE SEVEN BROADLY REFLECT THE UNDERLYING ECONOMIC FUNDAMENTALS. SUCH LANGUAGE WAS USED IN THE SEPTEMBER, 1985 PLAZA COMMUNIQUE WHEN THE GROUP OF FIVE THE UNITED STATES, JAPAN, WEST GERMANY, BRITAIN AND FRANCE AGREED TO DRIVE DOWN THE THEN HIGH-FLYING DOLLAR. IT WAS ALSO IN A RECENT US JAPANESE ACCORD ON CURRENCIES AND INTEREST RATES AND IS GENERALLY RECOGNISED AS HALL-MARK LANGUAGE DEVELOPED BY BAKER'S TREASURY TEAM.

Are they?

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191659 #/BAKER CONFIRMS G-5, G-7 MEETINGS IN PARIS

WASHINGTON, Feb 19 - U.S. Treasury Secretary James Baker confirmed earlier reports that officials of the Group of Five and Group of Seven industrial nations would meet in Paris this weekend but said he wanted to "knock down suggestions" that this round of talks was an emergency.

"It is not. We frequently have mid-winter meetings," Baker told the Senate Finance Committee.

Baker declined to comment on numerous questions about his objectives at the meeting with regard to the value of the dollar in world currency markets or about the economic goals he would suggest for other major industrial nations.

MORE

191706 #/BAKER CONFIRMS #2 WASHINGTON

Baker said normally the existence of the G-5 meeting is kept a secret but Japan could not participate without public notification of the Japanese Diet because it is currently in session.

Baker told the committee "it's no secret we've been seeking stimulative measures" on the part of industrial countries to help the U.S. resolve its trade problem.

Although Baker did not clearly refer to the existence of a G-7 meeting, he did not refute a statement by Senator Bill Bradley that the G-5 meeting on Saturday would be expanded to a G-7 one on Sunday.

REUTER

↳ G7 more secret than G5?

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Pls Chancellor

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191536 :G-5 MEETING SAID RISKY FOR FINANCIAL MARKETS

By Allan Saunderson, Reuters.

FRANKFURT, Feb 19 - The proposed Group of Five meeting is risky for financial markets because participants' diverse interests pose the danger of an inconclusive result that could lead to a precipitous dollar fall, dealers and economists said.

The background is in sharp contrast to the September 22, 1985, meeting in New York's Plaza Hotel, when the dollar was firming and all G-5 participants were agreed on reversing this.

"I find it wrong that a G-5 meeting is taking place at all at the present time," Chris Zwermann, foreign exchange adviser for the Swiss Bank Corp unit here said.

MORE

CN RIM852

191538 :G-5 MEETING SAID =2 FRANKFURT

Zwermann's remarks were echoed by many dealers in share and bond markets, and also by economists.

Though the G-5 meeting has not been officially confirmed, the Japanese chief cabinet secretary said Finance Minister KIICHI Miyazawa would leave for Paris to attend a meeting of the Group of Seven major industrial nations on Sunday.

But news the meeting would be preceded by discussions among various countries on Saturday led monetary analysts to infer that G-5 - excluding Canada and Italy - would meet then.

Currency dealers remained sceptical that the United States was prepared to support the dollar at present levels.

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191542 :G-5 MEETING SAID =3 FRANKFURT

The dollar soared above 1.85 marks on news that the G-5 would meet, but failed to reach initial euphoric predictions of 1.90, and slid again as reports emerged that underscored the national differences of opinion, dealers said.

Economists said German Finance Minister Gerhard Stoltenberg could propose broadening the scope of planned tax reductions but would offer little else.

Prospects of a further leading interest rate cut were slim after the Bundesbank trimmed the discount rate by a half point to three pct last month and brought down market interest rates.

MORE

191544 :G-5 MEETING SAID =4 FRANKFURT

Share prices rose strongly today as the dollar's firmer tone for the moment at least pushed fears over further pressure on export margins into the background, stock dealers said.

But dealers said prices could fall again if the G-5 failed to produce concrete measures to stabilise currencies.

Ernst Pullmann, Deutsche Girozentrale-Deutsche Kommunalbank chief currency dealer said "If nothing comes out of the meeting, the dollar will be down at 1.70 marks in two weeks."

Chase Bank Ag chief dealer Eckhardt Hager said in a screen commentary he was sceptical whether the G-5 meeting would produce an uptrend in the dollar.

MORE

CN RIM870

191545 :G-5 MEETING SAID =5 FRANKFURT

Zwermann added the difference of opinions on the dollar's level between Washington, Bonn and Tokyo were too wide.

"At the end of this meeting they're going to have to stand there with some kind of result to show," he said. The worst thing that could happen would be that this meeting would finish without result. Then it's all over for the dollar."

A level of 1.70 marks was easily in sight if the meeting concluded without any result, he said.

"If they just come out and say the coffee was good, the pie was tasty, and the cigars were too short, then you can forget everything," he added.

MORE

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191609 :G-5 MEETING SAID =6 FRANKFURT

Dealers and economists were also sceptical that the Bundesbank would move to cut leading rates again, even if Japan moves first, due to fears of sparking inflation.

The current rate of 3.0 pct has only once before been undercut, at the end of the 1950s.

Opinion was divided here over whether the U.S. would agree to a dollar level that would be acceptable to West Germany.

Although some dealers said the two nations could agree on a dollar at around 1.90 marks, others said the U.S. would likely prefer a range of 1.50 to 1.60 marks. This would be dangerously low for Germany's export economy, they said.

REUTER

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191333 :DELORS BID TO END EC BUDGET WRANGLES RISKS NEW ROW

By Jonathan Clayton, Reuters

STRASBOURG, Feb 19 - A challenge to European Community member states by EC Commission president Jacques Delors to end the days of constant budget squabbling by radically overhauling EC finances risks attracting the anger of key EC leaders, diplomats said.

Delors' plan, which seeks a large increase in funds by bringing EC contributions more into line with national wealth, could in fact split the community down the middle and spark off exactly the sort of bruising internal debate it was designed to prevent, they said.

MORE

191337 :DELORS BID =2 STRASBOURG

Under the package, outlined to the European Parliament in Strasbourg yesterday, austerity-minded northern states would end up shouldering a larger financial burden to the benefit of poorer southern states.

The plan would be anathema to EC budget hardliners such as British Prime Minister Margaret Thatcher who will not consider any more cash until the EC's surplus-creating farm policies are reformed.

London's stand is that the EC faces an expenditure crisis and not a revenue crisis.

MORE

191340 :DELORS BID =3 STRASBOURG

Diplomats said Britain, France and West Germany, currently the only net contributors to the EC budget, are certain to resist the plans and anger poorer members who see extra cash as essential to achieve the aim of greater European integration.

The Benelux countries would also see a leap in their payments and will want to secure guarantees that they will receive more back in the form of EC handouts before agreeing to any changes.

"There are so many conflicting interests it will take months to work out a deal. Whatever way you turn somebody is offended," one EC diplomat said.

MORE

191342 :DELORS BID =4 STRASBOURG

' Today the parliament finally adopted a revised budget for 1987 of some 36 billion European Currency Units which is expected to fall some five billion Ecus short of needs.

Delors' plan would link a country's budget payments to its gross national product. At present, contributions are calculated on a percentage of Value Added Tax returns.

All countries would pay one pct of their VAT receipts to Brussels. Extra cash would then be raised in line with needs by a levy on the difference between a country's total VAT receipts and its GNP.

MORE

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191344 :DELORS BID =5 STRASBOURG

The commission calculates that under the new formula the budget would rise to 52 billion Ecus by 1992.

"We cannot go on lurching from one crisis to the next," Delors told the Assembly. A new cash injection was needed for the EC's aims of greater cohesion and solidarity to be achieved and that the entire future development of the trading bloc was at stake.

He said the measures would create a leaner, fitter community and allow it to break out of the cycle of financial crises.

EC foreign ministers are due to hold their first debate on the package at a special meeting on Sunday.

REUTER

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191546 :/VOLCKER URGES MORE INTERNATIONAL COORDINATION

WASHINGTON, Feb 19 - Federal Reserve Board Chairman Paul Volcker strongly urged complementary action by the U.S. and its major economic allies on budgets, monetary policies and on maintaining appropriate exchange rates.

In testimony before the Senate Banking Committee, Volcker said "What is required is complementary actions here and abroad -- on budgets, on monetary policies, and on maintaining appropriate exchange rates and an open trading order."

He said that unless dealt with forcibly, global trade imbalances "will impair both growth and price stability" and thus there is no alternative but coordinated action.

REUTER

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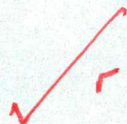
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PARIS MEETING OF FINANCE MINISTERS: BELGIAN VIEWS

SUMMARY

1. IN A PRESS INTERVIEW TODAY THE BELGIAN FINANCE MINISTER EXPRESSED CONFIDENCE THAT THE PARIS MEETING OF FINANCE MINISTERS OF THE ECONOMIC SEVEN WOULD MAKE PROGRESS TOWARDS ACHIEVING GREATER MONETARY STABILITY. HE WOULD HAVE LIKED A GREATER EC PARTICIPATION.

DETAIL

2. IN AN INTERVIEW IN TODAY'S LE SOIR (CENTRE), FINANCE MINISTER EYSKENS SAID THAT THE SEVEN FINANCE MINISTERS WOULD NOT TAKE THE RISK OF MEETING IN PARIS UNLESS THEY WERE REASONABLY CONFIDENT OF A SATISFACTORY OUTCOME. HE EXPECTED THAT THE MEETING WOULD ACHIEVE IMPORTANT AGREEMENTS ON CURRENCY STABILISATION, FOR EXAMPLE THROUGH UNDERTAKINGS ON MARKET INTERVENTION, LOWER INTEREST RATES IN GERMANY AND MEASURES TO STIMULATE GROWTH IN GERMANY AND JAPAN. HE SAID IT WAS IMPORTANT FOR BELGIUM, BEING A SMALL COUNTRY HIGHLY DEPENDENT ON EXTERNAL TRADE, TO HAVE MONETARY STABILITY. THE STABILITY OF THE EMS DEPENDED ON A PEACEFUL RELATIONSHIP BETWEEN THE MARK AND THE DOLLAR. WITHOUT THIS THERE WOULD BE A DANGER OF FURTHER STORMS OVER THE CAP.

3. EYSKENS SAID THERE WOULD BE NO QUESTION OF A SUDDEN RETURN TO BRETTON WOODS AND FIXED PARITIES. CIRCUMSTANCES WERE VERY DIFFERENT. BUT A FEW STEPS TOWARDS A SORT OF SECOND BRETTON WOODS WERE POSSIBLE. HE UNDERSTOOD THE PROBLEMS FACING THE AMERICANS. THE EUROPEANS SHOULD DO MORE THAN JUST WRING THEIR HANDS. BUT THE RELIGION OF FLOATING EXCHANGE RATES INAUGURATED BY NIXON IN THE 1970'S HAD PROVED BAD FOR EVERYONE, INCLUDING THE US ITSELF.

4. EYSKENS SAID THAT AS PRESIDENT OF THE EUROPEAN COUNCIL HE REGRETTED THAT THE COMMUNITY WOULD NOT BE PRESENT IN PARIS OTHER THAN THROUGH THE COMMISSION. HE HAD DONE A ROUND OF HIS PARTNERS ADVOCATING A COMMUNITY PRESENCE, BUT WITHOUT RESULT.

PETRIE

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WGD

CONFIDENTIALFROM: A M DOLPHIN
DATE: 19 February 1987

1. MR EVANS ^{HPE}
2. CHANCELLOR

cc: Sir P Middleton o.r.
Sir T Burns
Sir G Littler
Mr Cassell
Mr Peretz
Mr Sedgwick
Mr Culpin
Mr Matthews**POSSIBLE G5/G7 MEETING**

We have revised the tables provided under cover of Mr Evans' minute of 13 February 1987 along the lines you requested. Updated copies are attached. The charts cannot be updated today because of the failure of both the graphics printers in the Treasury, but exchange rates have moved little during the past week, so the original versions of the charts still offer a fair picture of the present position in relation to trends over the last ten years.

2. The package comprises:

- (i) International comparisons of nominal income growth (A), real domestic demand growth (B), real GNP/GDP growth (C), inflation (D), current balances (E), and unit labour costs growth (F).
- (ii) Indicators of fiscal stance (G) and the level of interest rates (H).
- (iii) Charts showing effective exchange rates (I and J), dollar bilateral exchange rates (K and L), sterling bilateral exchange rates (M and N) and the yen:D-mark rate and real dollar exchange rates (O).
- (iv) Tables showing the exchange rate data underlying the charts for the period since January 1985 (P, Q and R), and movements in nominal exchange rates to date since the dollar's peak, the Plaza Agreement and last year's Annual Meetings (S).

3. Mr Kuczys' minute of 16 February to Mr Evans noted your scepticism about the IMF's latest forecasts, which suggest that real domestic demand will grow by 4 per cent in Japan and $3\frac{1}{2}$ per cent in Germany in 1987.

4. The forecast for Japan is similar to our own assessment, though, unlike the IMF forecast we assume the Japanese Government will come up with the usual supplementary budget designed to meet domestic and international pressure, and which will boost public works a little towards the end of the year. Private forecasters in Japan expect GNP to grow by 2 - 3 per cent in 1987 with domestic demand expected to grow by 3 - 4 per cent. The Government's growth target for GNP in 1987 is $3\frac{1}{2}$ per cent. Even if domestic demand in Japan does grow by 4 per cent, the fall in net exports is likely to be larger than the $\frac{1}{2}$ per cent in the official forecast (our own judgement is that it will be at least 1 per cent) giving overall GNP growth of some 3 per cent: a second year of growth clearly below trend.

5. The IMF forecast of $3\frac{1}{2}$ per cent domestic demand growth in Germany is actually below our own forecast of 4 per cent implicit in what is proposed for the FSBR. Again, our assessment incorporates some relaxation of fiscal policy: this could be worth $\frac{1}{4}$ per cent, not sufficient to explain the difference between the two forecasts. In addition we also have lower inflation, and therefore higher real personal incomes and consumption. Private forecasters in Germany have now revised down their estimates of GNP growth in 1987 to 2 - $2\frac{1}{2}$ per cent, though this would still be consistent with domestic demand growth of about $3\frac{1}{2}$ per cent. The German Government's official view, set out in their Annual Economic Report in January, is that GNP will grow by $2\frac{1}{2}$ per cent or more, with domestic demand expanding by $3\frac{1}{2}$ - 4 per cent.

6. So domestic demand growth of $3\frac{1}{2}$ and 4 per cent in Japan and Germany in 1987, much as in 1984, 1985 and 1986, would not be surprising. But given the shifts out of the balance of payments, a higher growth of domestic demand would be needed to sustained output growth at productive potential.

A.M. Dolph

A M DOLPHIN

NOMINAL INCOME GROWTH

| | 1984 | 1985 | 1986 | 1987 | 1988 | 1985-87 |
|---|------|------|------------|-----------|-----------|---------|
| <u>IMF forecasts</u> | | | | | | |
| US | 10½ | 6½ | 5½ | 5½ | 6½ | 6 |
| Japan | 6½ | 6 | 4½ | 4 | 6 | 5 |
| Germany | 5 | 5 | 6 | 4½ | 4 | 5 |
| France | 9 | 7½ | 6½ | 5 | 4½ | 6½ |
| UK | 7 | 10 | 6 | 7 | 7 | 7½ |
| G5 | 9 | 6½ | 5 | 5 | 6 | 5½ |
| <u>WEP forecasts</u> | | | | | | |
| Italy | 14 | 11 | 11 | 8 | 8 | 10 |
| Canada | 9½ | 7½ | 6½ | 6½ | 6½ | 7 |
| G7 | 9½ | 7 | 5½ | 5 | 6 | 6 |
| <u>UK forecast</u> | | | | | | |
| UK - latest HMT view | | | 6½ | 7½ | 7 | |
| UK - MTFS (published FY figures in brackets) 1986 FSR | | | 6½ (6½) | 6 (6½) | 6½ (6) | |

Notes:

1. Money GDP at market prices.
2. WEP forecasts for the G5 are generally close to IMF forecasts, except for Japan where WEP sees nominal growth of 3½ and 4½ per cent in 1987 and 1988 respectively.
3. No IMF forecasts yet available for Italy, Canada, and G7.

REAL DOMESTIC DEMAND GROWTH

| | 1984 | 1985 | 1986 | 1987 | 1988 | 1985-87 |
|----------------------|------|------|------|------|------|---------|
| <u>IMF forecasts</u> | | | | | | |
| US | 6½ | 2½ | 3½ | 2 | 2½ | 2½ |
| Japan | 5 | 4½ | 4 | 4 | 4 | 4 |
| Germany | 3½ | 2½ | 4 | 3½ | 2½ | 3½ |
| France | 1½ | 1½ | 3½ | 2½ | 2½ | 2½ |
| UK | 3 | 3½ | 3½ | 3½ | 2½ | 3½ |
| G5 | 5 | 3 | 3½ | 2½ | 3 | 3 |
| <u>WEP forecasts</u> | | | | | | |
| Italy | 3½ | 2½ | 3 | 4 | 4 | 3 |
| Canada | 4 | 4½ | 4 | 2½ | 2½ | 3½ |
| G7 | 5 | 3 | 3½ | 2½ | 3 | 3 |
| <u>UK forecast</u> | | | | | | |
| UK - latest HMT view | | | 3½ | 3½ | 2½ | |

Notes:

1. Total domestic demand including stockbuilding.
2. No IMF forecasts yet available for Italy, Canada and G7.

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REAL GNP/GDP GROWTH

| | 1984 | 1985 | 1986 | 1987 | 1988 | 1985-87 |
|----------------------|------|------|------------------|------|------|---------|
| <u>IMF forecasts</u> | | | | | | |
| US | 6.4 | 2.7 | 2.5 | 2.6 | 3.2 | 2.6 |
| Japan | 5.1 | 4.7 | 2.3 | 2.6 | 3.2 | 3.2 |
| Germany | 3.0 | 2.5 | 2.5 | 2.3 | 1.8 | 2.5 |
| France | 1.5 | 1.4 | 2.0 | 1.7 | 2.4 | 1.7 |
| UK | 2.9 | 3.4 | 2.3 | 2.8 | 2.2 | 2.8 |
| G5 | 4.8 | 2.8 | 2.4 | 2.5 | 2.9 | 2.6 |
| <u>WEP forecasts</u> | | | | | | |
| Italy | 2.8 | 2.3 | 2.7 | 3.1 | 2.8 | 2.7 |
| Canada | 5.5 | 4.0 | 3.5 | 2.9 | 3.2 | 3.5 |
| G7 | 4.7 | 2.8 | 2.5 | 2.6 | 2.9 | 2.6 |
| <u>UK forecast</u> | | | | | | |
| UK - latest HMT view | | | 2.6 ² | 3.1 | | |

Notes:

1. No IMF forecasts yet available for Italy, Canada and G7.
2. GDP(O) actual figure.

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INFLATION

| | 1984 | 1985 | 1986 | 1987 | 1988 | 1985-87 |
|----------------------|------|------|------|------|------|---------|
| <u>IMF forecasts</u> | | | | | | |
| US | 4.3 | 3.5 | 1.9 | 3.3 | 3.4 | 2.9 |
| Japan | 2.2 | 2.1 | 0.6 | 0.1 | 2.8 | 0.9 |
| Germany | 2.4 | 2.2 | -0.2 | 1.1 | 2.0 | 1.0 |
| France | 7.4 | 5.8 | 2.5 | 2.3 | 1.6 | 3.5 |
| UK | 5.0 | 6.1 | 3.4 | 4.3 | 4.6 | 4.6 |
| G5 | 4.0 | 3.4 | 1.6 | 2.4 | 3.0 | 2.5 |
| <u>WEP forecasts</u> | | | | | | |
| Italy | 11.1 | 9.4 | 5.8 | 3.9 | 5.0 | 6.3 |
| Canada | 4.4 | 4.1 | 3.8 | 2.7 | 2.6 | 3.5 |
| G7 | 4.5 | 3.8 | 2.0 | 2.5 | 3.1 | 2.8 |
| <u>UK forecast</u> | | | | | | |
| UK - latest HMT view | | | | 4.5 | | |

Notes:

1. No IMF forecast yet available for Italy, Canada and G7.

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CURRENT ACCOUNT (\$ billion, % of GDP in brackets)

| | 1985 | 1986 | 1987 | 1985-1987 |
|----------------------|-----------|------------|-----------|-----------|
| <u>IMF forecasts</u> | | | | |
| US | -118 (-3) | -141 (-3½) | -133 (-3) | -131 (-3) |
| Japan | 49 (3½) | 86 (4½) | 80 (3½) | 72 (4) |
| Germany | 14 (2) | 36 (4) | 33 (3) | 28 (3) |
| France | 1 (-) | 4 (½) | 3 (½) | 2 (½) |
| UK | 5 (1) | 0 (-) | -3 (-½) | 1 (-) |
| G5 | -9 | -15 | -20 | -28 |
| <u>WEP forecasts</u> | | | | |
| Italy | -4 (-1) | 8 (1½) | 10 (1½) | 5 (½) |
| Canada | 0 (-1) | -7 (-2) | -5 (-1½) | -4 (-1) |
| G7 | -53 | -14 | -15 | -27 |
| <u>UK forecast</u> | | | | |
| UK - latest HMT view | | | -3 (-½) | |

Notes:

1. No IMF forecast yet available for Italy, Canada and G7.

F

GROWTH OF UNIT LABOUR COSTS IN MANUFACTURING

| | 1984 | 1985 | 1986Q3 |
|---------|------|------|--------|
| US | -0.6 | 0.6 | -0.5 |
| Japan | -3.9 | 0.9 | 3.9 |
| Germany | 1.0 | 0.8 | 4.7 |
| France | 4.1 | 2.0 | 0.6 |
| UK | 2.6 | 5.8 | 4.3 |
| Italy | 2.8 | 4.6 | -2.0 |
| Canada | -2.2 | 2.7 | 2.8 |

Source: IMF

Notes:

1. Latest UK figure is 3.7 per cent (1986Q4).

DEFICIT PROJECTIONS FOR MAJOR COUNTRIES

9

| | Deficit | % of GNP/GDP | General government deficit % GNP/GDP |
|--|---------|-----------------|--|
| <u>US Federal govt.</u> (\$ billion) | | | |
| FY1986 | 221 | 5.3 | 3.4 |
| FY1987 | 173 | 4.4 | |
| <u>Japan central govt.</u> (Yen trillion) | | | |
| FY1986 | 11.5 | 3.4 | 1.5 |
| FY1987 | 10.5 | 3.0 | |
| <u>Germany central govt.</u> | | | |
| FY1986 | 23.0 | 1.2 | 1.0 |
| FY1987 | 22.3 | 1.1 | |
| <u>UK PSBR</u> (£ billion) | | | |
| FY1986 | 7 | 1.8 | 3.0 |
| FY1987 | 7 | 1.5 | |

Notes:

1. General government deficits shown are HMT estimates for calendar 1986.
2. All central government figures are government estimates. There is widespread doubt in the US about the extent of the reduction in FY1987. We, and most others, think \$190 bn more likely. In the case of Japan the supplementary budget expected in the Autumn could raise the projected deficit for FY1987 above 11 trillion yen.
3. FY1986 figures for the UK are based on the Autumn Statement. FY1987 figures are from last year's MTFS. More recent estimates are available.
4. FY1987 in the US runs from October 1986 to September 1987; in Germany from January to December 1987 and in Japan and the UK from April 1987 to March 1988.

INTEREST RATES IN THE G7

18 February 1987

| | Three Month money | Discount rate* | 10 year government bond yield |
|----------------|----------------------|-------------------|----------------------------------|
| United States | 6.1 | 5.5 | 7.3 |
| Japan | 4.0 | 3.0 | 4.8 |
| Germany | 4.0 | 3.0 | 6.2 |
| France | 8.4 | 8.0 | 8.9 |
| United Kingdom | 10.7 | 10.9 | 10.0 |
| Italy | 11.4 | 12.0 | 9.8 |
| Canada | 7.5 | 7.7 | 8.7 |

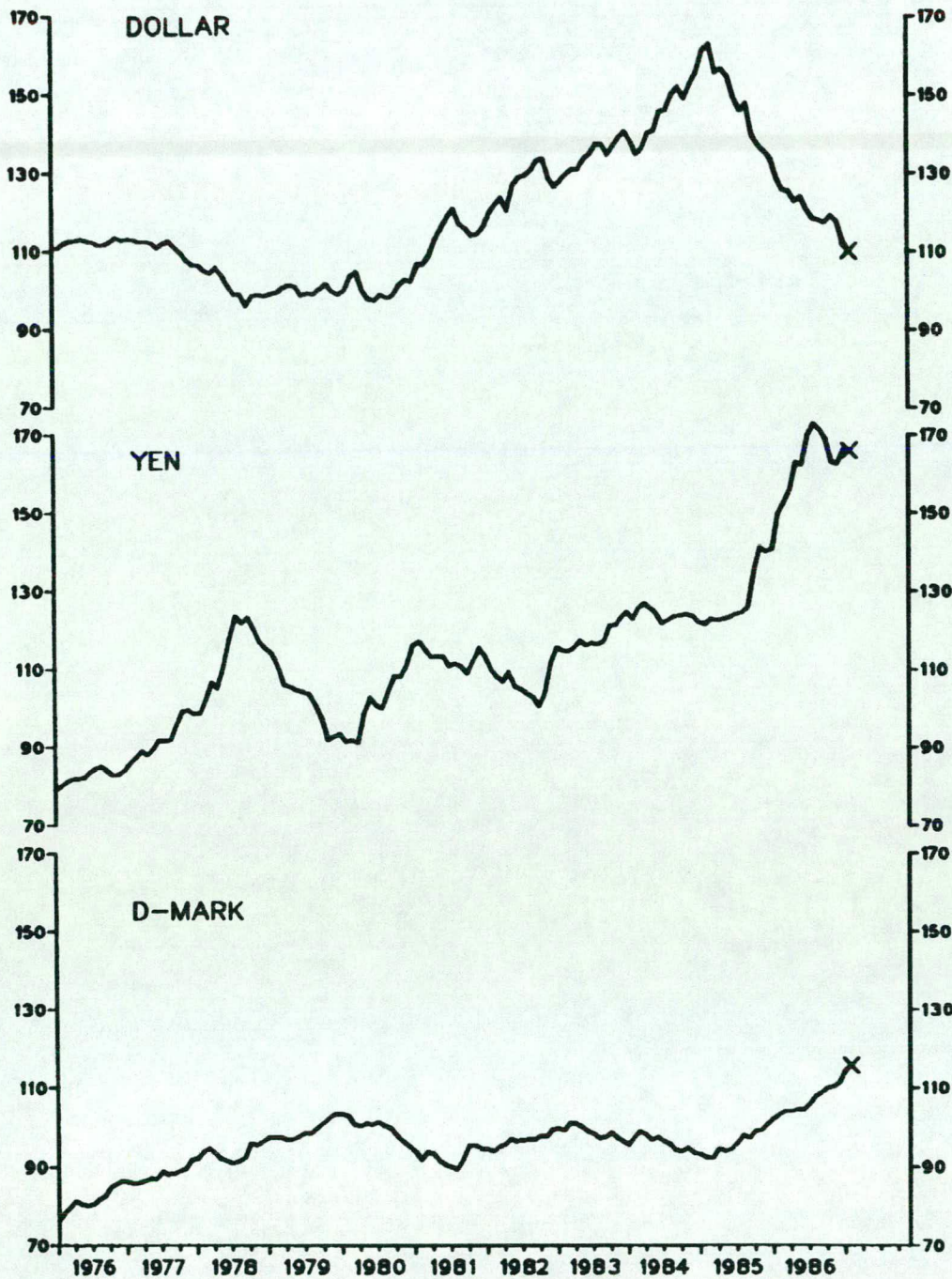
16 September 1985

| | Three Month money | Discount rate* | 10 year government bond yield |
|----------------|----------------------|-------------------|----------------------------------|
| United States | 8.0 | 7.5 | 10.3 |
| Japan | 6.3 | 5.0 | 6.2 |
| Germany | 4.7 | 4.0 | 6.6 |
| France | 9.8 | 9.6 | 10.9 |
| United Kingdom | 11.6 | 11.4 | 10.7 |
| Italy | 14.3 | 15.5 | 14.0 |
| Canada | 9.1 | 9.3 | 10.9 |

* Official lending rate to market. Discount rate in the US, Japan, Germany and Italy; rate at which 1st category paper is purchased by authorities in France; rate at which band one bills are purchased by authorities in the UK; and bank rate in Canada.

I

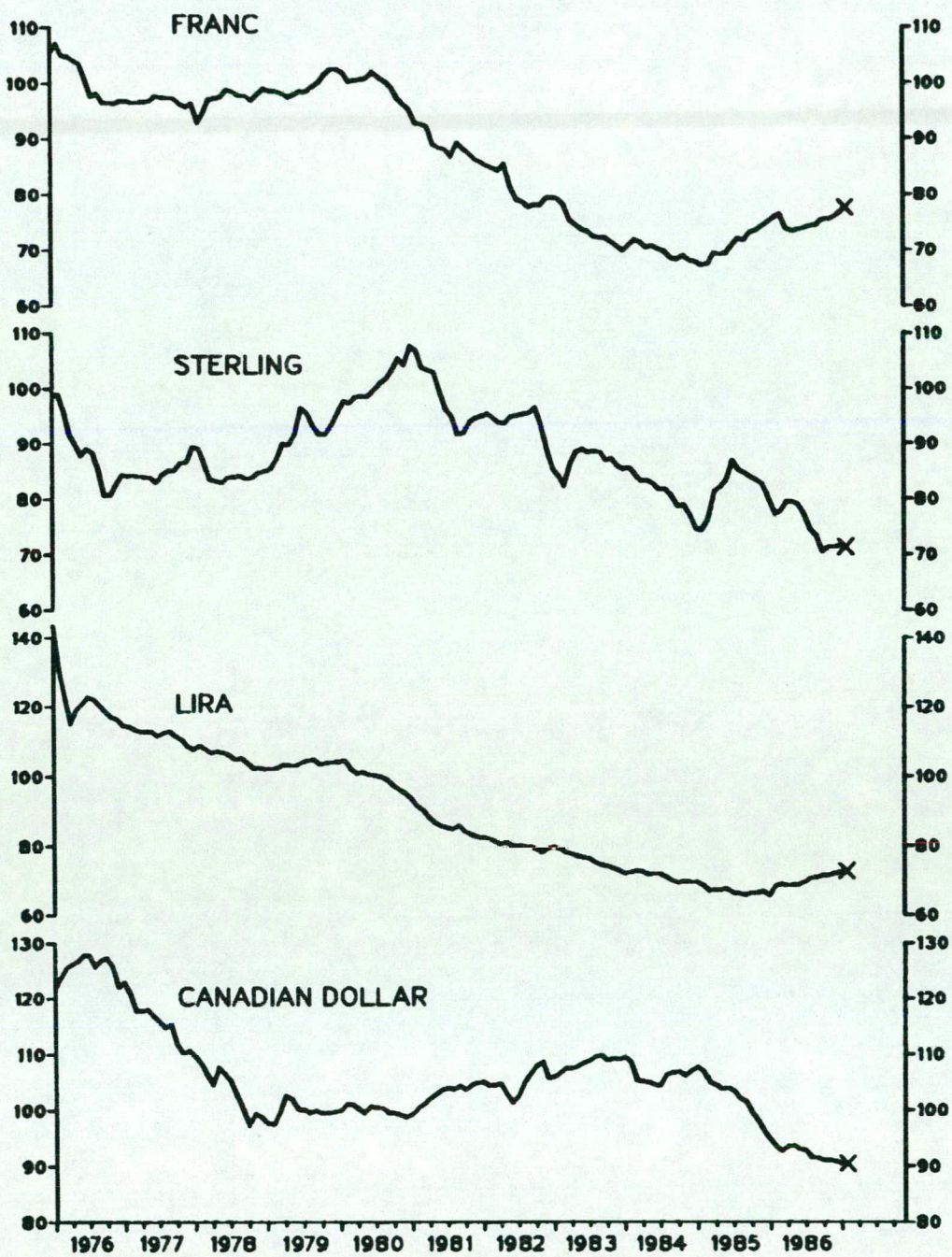
NOMINAL EFFECTIVE EXCHANGE RATES (IMF , 1980=100)



X = 12th FEBRUARY

J

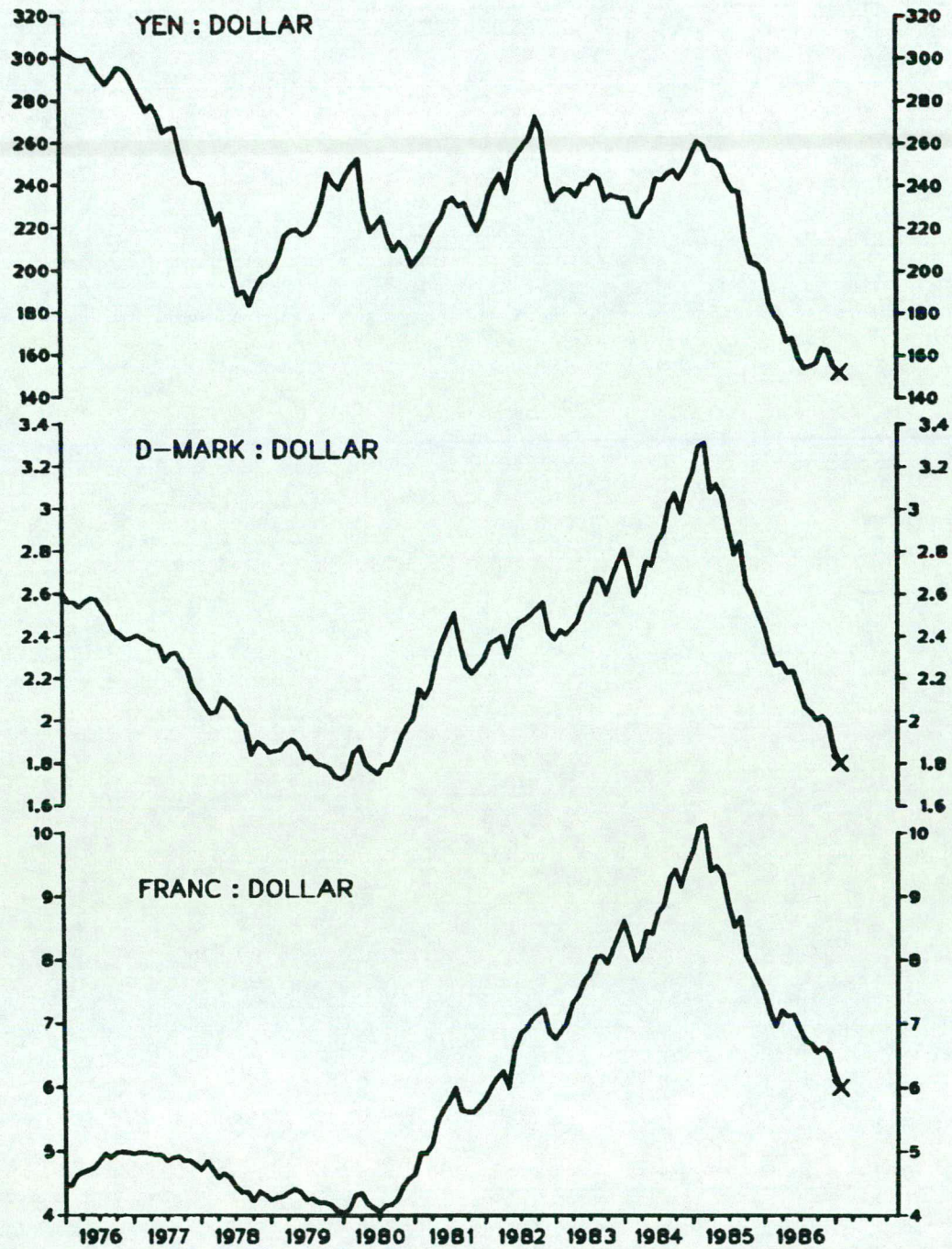
NOMINAL EFFECTIVE EXCHANGE RATES (IMF , 1980=100)



X = 12th FEBRUARY

K

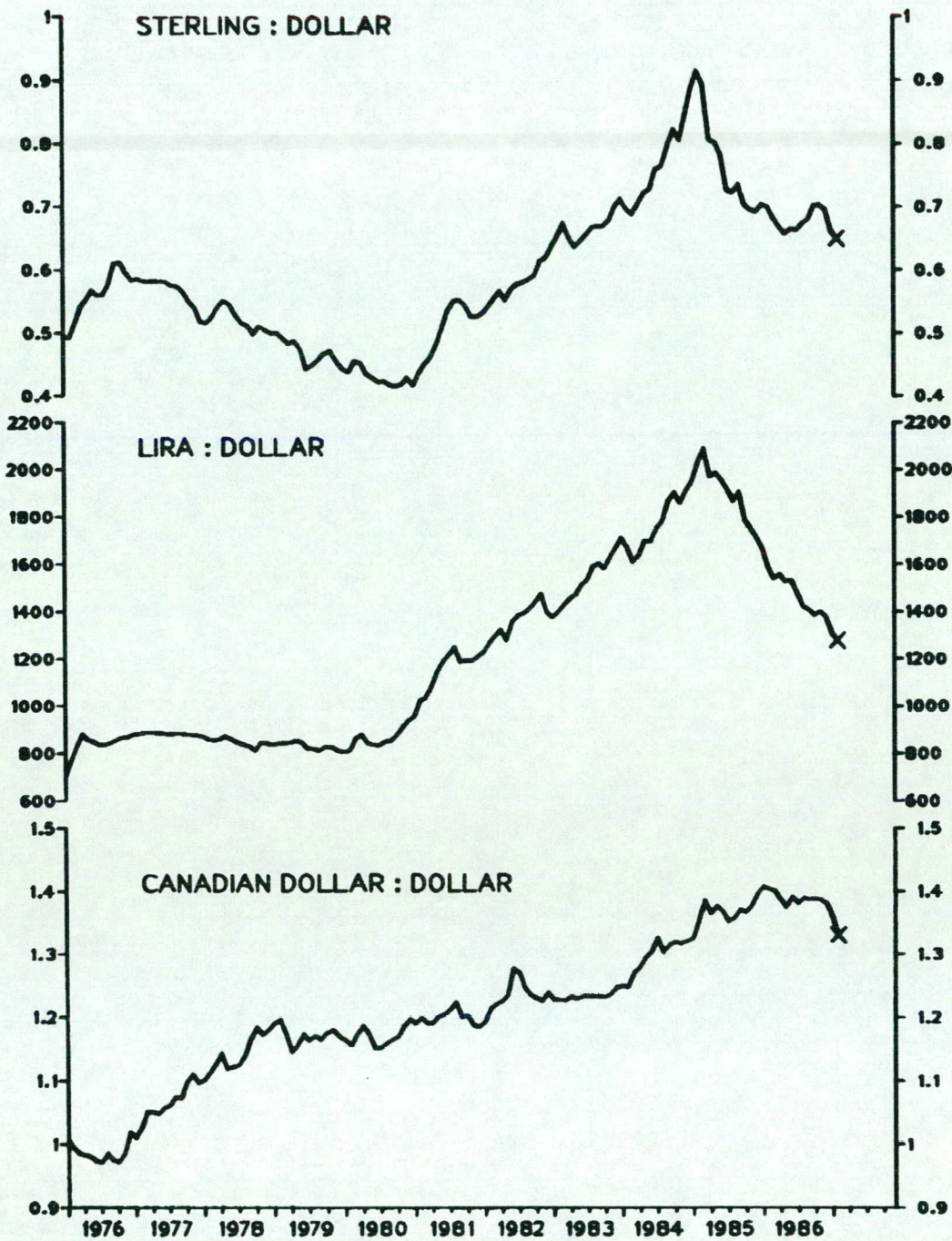
DOLLAR EXCHANGE RATES (MONTHLY AVERAGES)



X = 12th FEBRUARY

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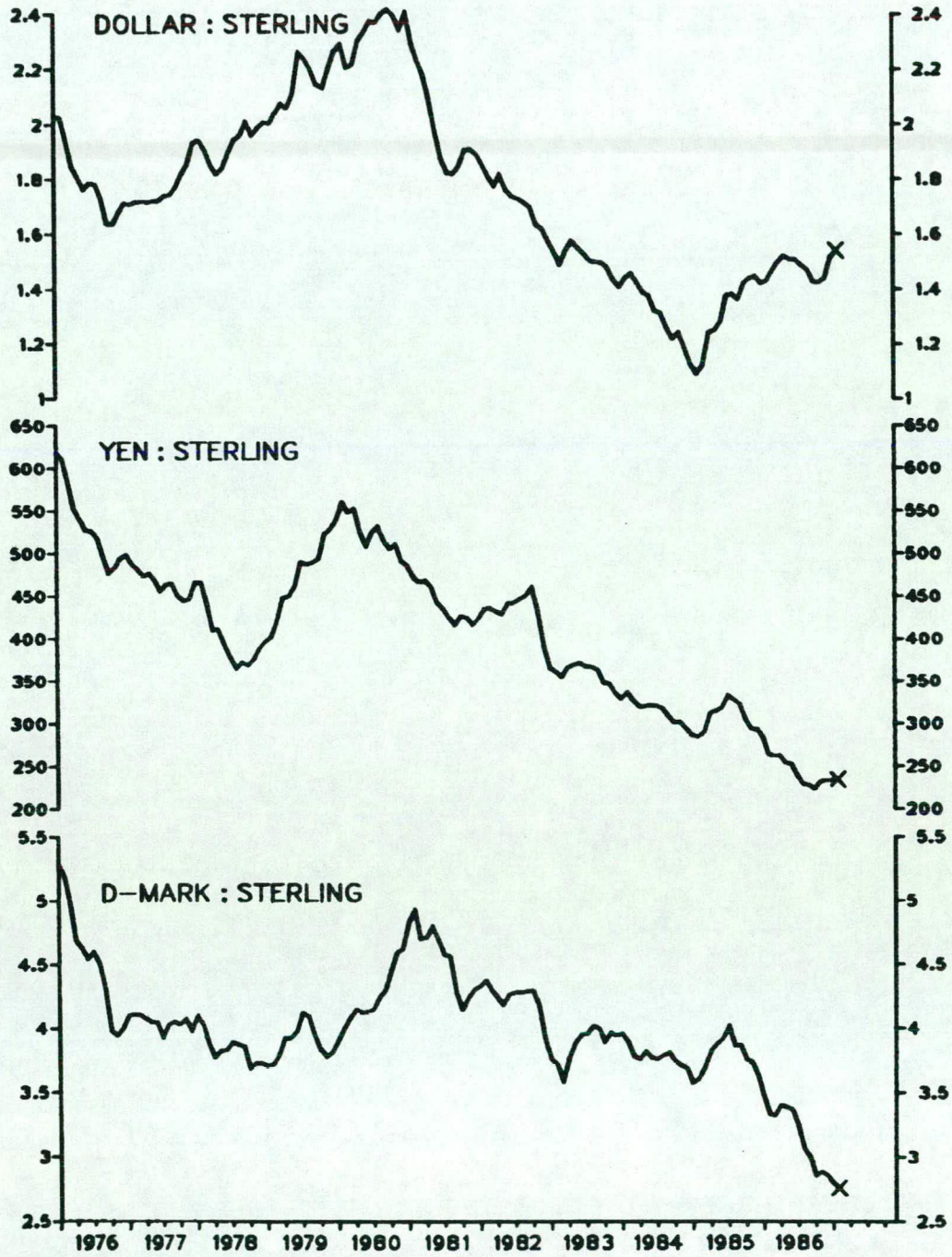
DOLLAR EXCHANGE RATES (MONTHLY AVERAGES)



X = 12th FEBRUARY

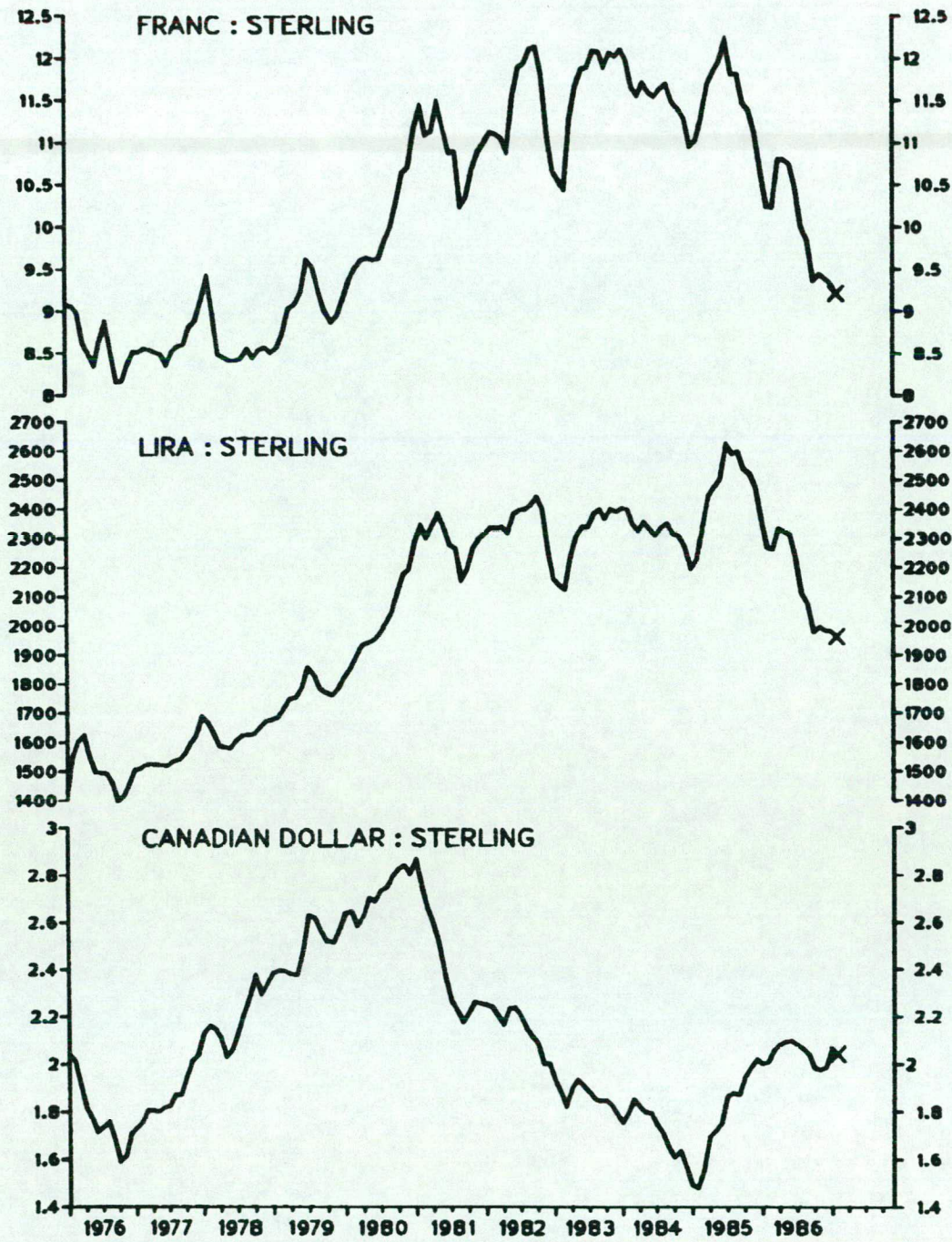
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STERLING EXCHANGE RATES (MONTHLY AVERAGES)



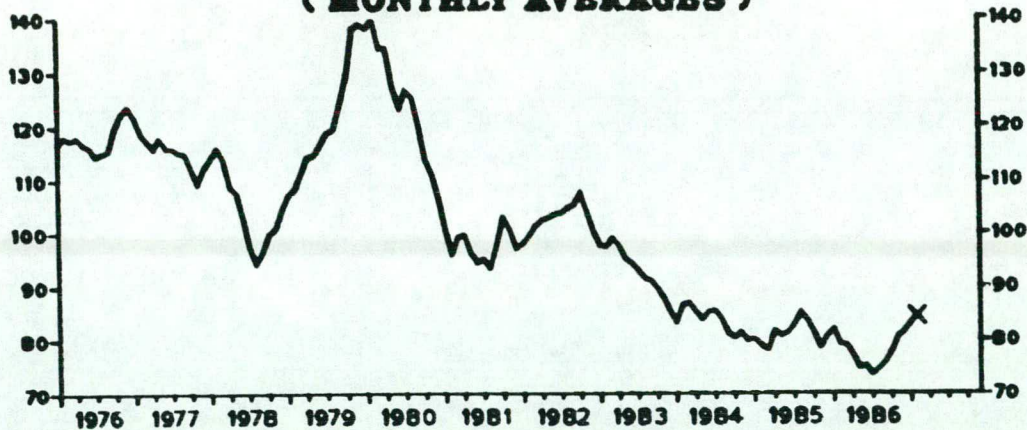
X = 12th FEBRUARY

STERLING EXCHANGE RATES (MONTHLY AVERAGES)



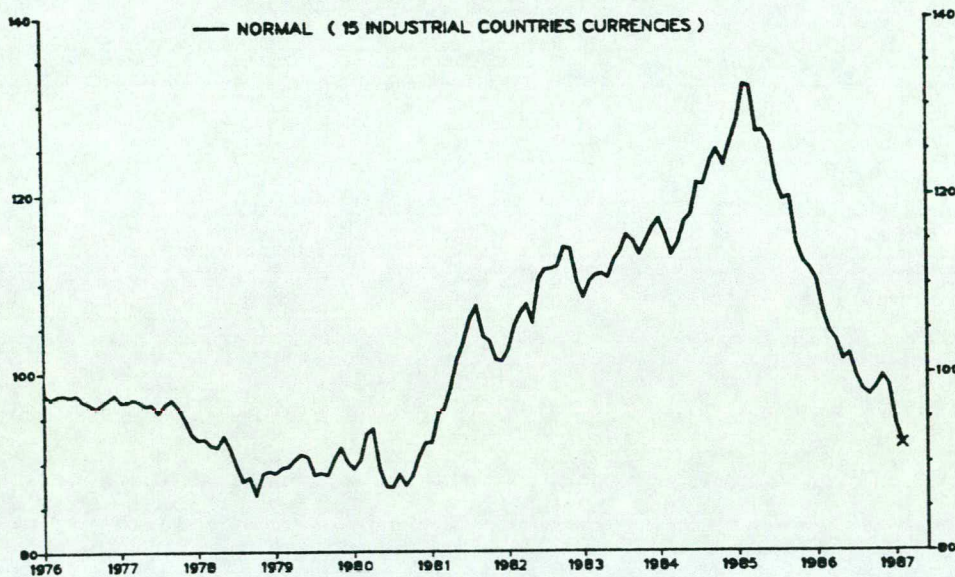
X = 12th FEBRUARY

**YEN : D-MARK EXCHANGE RATE
(MONTHLY AVERAGES)**

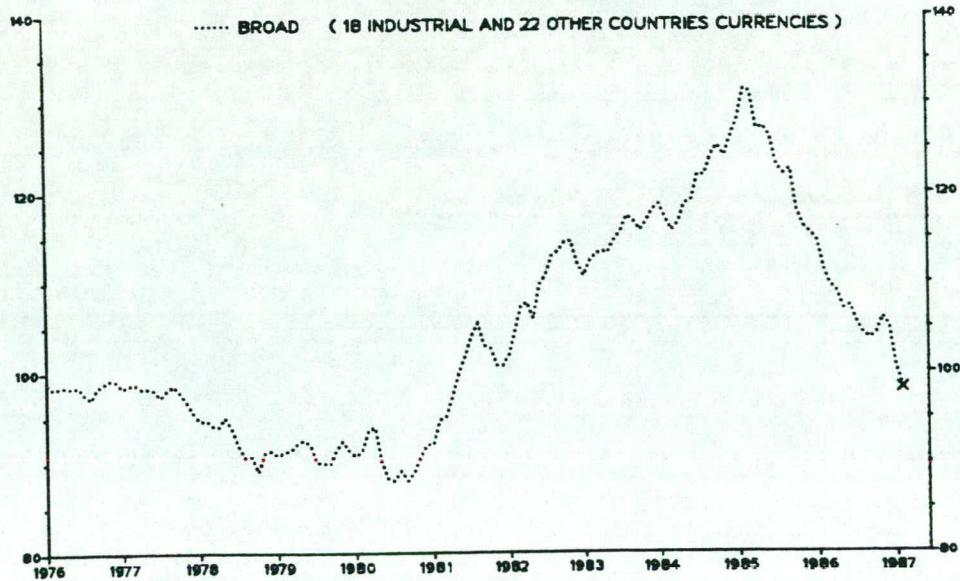


X = 12th FEBRUARY

**REAL DOLLAR EXCHANGE RATE
(MORGAN GUARANTY, 1980=82=100, MONTHLY AVERAGES)**



**REAL DOLLAR EXCHANGE RATE
(MORGAN GUARANTY, 1980=82=100, MONTHLY AVERAGES)**



X = 12th FEBRUARY

EFFECTIVE EXCHANGE RATES (IMF MEASURE, 1980 = 100)

| | US | Japan | Germany | France | UK | Italy | Canada |
|----------|-------|-------|---------|--------|------|-------|--------|
| 1985 Jan | 155.9 | 122.1 | 93.2 | 67.8 | 74.5 | 69.4 | 107.7 |
| Feb | 161.3 | 121.6 | 92.3 | 67.2 | 74.4 | 68.6 | 106.9 |
| Mar | 162.7 | 122.9 | 92.3 | 67.3 | 76.4 | 66.9 | 104.9 |
| Apr | 155.9 | 122.5 | 94.5 | 69.2 | 81.2 | 67.3 | 104.5 |
| May | 156.5 | 122.9 | 94.0 | 69.1 | 82.0 | 67.2 | 103.8 |
| Jun | 154.8 | 123.3 | 94.0 | 69.3 | 83.3 | 67.5 | 104.0 |
| Jul | 149.2 | 124.1 | 94.4 | 70.7 | 86.8 | 66.4 | 103.5 |
| Aug | 146.0 | 124.5 | 96.0 | 71.9 | 85.1 | 66.1 | 102.1 |
| Sep | 147.7 | 125.8 | 98.0 | 71.6 | 84.6 | 65.7 | 101.6 |
| Oct | 139.6 | 134.7 | 97.3 | 73.0 | 83.8 | 66.3 | 99.5 |
| Nov | 137.1 | 141.0 | 99.1 | 73.4 | 83.3 | 66.4 | 98.1 |
| Dec | 135.6 | 140.2 | 100.8 | 74.2 | 82.5 | 66.7 | 96.2 |
| 1986 Jan | 133.7 | 140.7 | 102.1 | 74.9 | 79.9 | 65.6 | 94.7 |
| Feb | 128.5 | 149.8 | 103.3 | 75.8 | 77.3 | 68.4 | 93.4 |
| Mar | 125.7 | 152.5 | 104.1 | 76.2 | 77.6 | 68.9 | 92.7 |
| Apr | 125.3 | 155.8 | 104.0 | 73.7 | 79.3 | 68.5 | 93.5 |
| May | 122.7 | 162.8 | 104.5 | 73.4 | 79.4 | 68.6 | 93.7 |
| Jun | 123.7 | 162.4 | 104.5 | 73.5 | 79.0 | 68.8 | 93.0 |
| Jul | 120.6 | 169.9 | 105.8 | 73.7 | 77.1 | 69.4 | 92.8 |
| Aug | 118.2 | 172.8 | 107.9 | 74.2 | 74.3 | 70.5 | 91.5 |
| Sep | 117.8 | 171.4 | 108.8 | 74.3 | 73.3 | 70.8 | 91.5 |
| Oct | 117.2 | 169.4 | 110.0 | 75.3 | 70.5 | 71.4 | 91.1 |
| Nov | 118.8 | 163.1 | 110.3 | 75.4 | 71.2 | 71.5 | 91.0 |
| Dec | 117.6 | 162.6 | 111.2 | 75.7 | 71.2 | 72.0 | 90.9 |
| 1987 Jan | 112.6 | 166.1 | 114.3 | 76.6 | 71.6 | 72.3 | 90.5 |
| Feb 18 | 111.1 | 166.1 | 114.7 | 77.0 | 72.1 | 72.0 | 90.4 |

DOLLAR EXCHANGE RATES

| | Yen | D-mark | Franc | Sterling | Lira | C.dollar |
|----------|-----|--------|-------|----------|------|----------|
| 1985 Jan | 254 | 3.17 | 9.70 | .98 | 1950 | 1.32 |
| Feb | 260 | 3.30 | 10.12 | .94 | 2040 | 1.25 |
| Mar | 258 | 3.30 | 10.09 | .94 | 2080 | 1.37 |
| Apr | 251 | 3.08 | 9.41 | .99 | 1970 | 1.36 |
| May | 252 | 3.11 | 9.47 | .99 | 1980 | 1.38 |
| Jun | 249 | 3.06 | 9.34 | .98 | 1950 | 1.37 |
| Jul | 241 | 2.91 | 8.87 | .93 | 1900 | 1.35 |
| Aug | 237 | 2.79 | 8.54 | .90 | 1880 | 1.36 |
| Sep | 237 | 2.84 | 8.66 | .91 | 1900 | 1.37 |
| Oct | 215 | 2.64 | 8.06 | .85 | 1780 | 1.37 |
| Nov | 204 | 2.59 | 7.90 | .84 | 1750 | 1.38 |
| Dec | 203 | 2.51 | 7.68 | .82 | 1710 | 1.40 |
| 1986 Jan | 200 | 2.44 | 7.49 | .80 | 1660 | 1.41 |
| Feb | 185 | 2.33 | 7.16 | .77 | 1590 | 1.40 |
| Mar | 179 | 2.27 | 6.97 | .75 | 1540 | 1.40 |
| Apr | 175 | 2.27 | 7.20 | .75 | 1560 | 1.39 |
| May | 167 | 2.23 | 7.11 | .73 | 1530 | 1.38 |
| Jun | 168 | 2.23 | 7.12 | .73 | 1530 | 1.39 |
| Jul | 159 | 2.15 | 6.93 | .72 | 1480 | 1.38 |
| Aug | 154 | 2.06 | 6.72 | .74 | 1420 | 1.39 |
| Sep | 155 | 2.04 | 6.68 | .74 | 1410 | 1.39 |
| Oct | 156 | 2.00 | 6.56 | .73 | 1390 | 1.39 |
| Nov | 163 | 2.02 | 6.62 | .74 | 1400 | 1.39 |
| Dec | 162 | 1.99 | 6.53 | .73 | 1380 | 1.38 |
| 1987 Jan | 155 | 1.86 | 6.19 | .69 | 1320 | 1.36 |
| Feb 18 | 154 | 1.83 | 6.09 | .65 | 1300 | 1.33 |

R

STERLING EXCHANGE RATES

| | Dollar | Yen | D-mark | Franc | Lira | C.dollar |
|----------|--------|-----|--------|-------|------|----------|
| 1985 Jan | 1.13 | 287 | 3.58 | 10.9 | 2200 | 1.49 |
| Feb | 1.09 | 285 | 3.61 | 11.0 | 2230 | 1.48 |
| Mar | 1.12 | 290 | 3.70 | 11.3 | 2340 | 1.55 |
| Apr | 1.24 | 312 | 3.83 | 11.7 | 2450 | 1.69 |
| May | 1.25 | 315 | 3.88 | 11.8 | 2480 | 1.72 |
| Jun | 1.28 | 319 | 3.92 | 12.0 | 2500 | 1.75 |
| Jul | 1.37 | 333 | 4.02 | 12.2 | 2620 | 1.86 |
| Aug | 1.38 | 328 | 3.87 | 11.8 | 2590 | 1.88 |
| Sep | 1.37 | 323 | 3.87 | 11.8 | 2600 | 1.87 |
| Oct | 1.42 | 305 | 3.76 | 11.5 | 2540 | 1.94 |
| Nov | 1.44 | 294 | 3.73 | 11.4 | 2520 | 1.98 |
| Dec | 1.45 | 293 | 3.63 | 11.1 | 2480 | 2.02 |
| 1986 Jan | 1.42 | 285 | 3.47 | 10.7 | 2370 | 2.00 |
| Feb | 1.43 | 264 | 3.34 | 10.2 | 2270 | 2.01 |
| Mar | 1.47 | 262 | 3.33 | 10.2 | 2260 | 2.06 |
| Apr | 1.50 | 262 | 3.40 | 10.8 | 2330 | 2.08 |
| May | 1.52 | 254 | 3.39 | 10.8 | 2320 | 2.09 |
| Jun | 1.51 | 253 | 3.37 | 10.7 | 2310 | 2.10 |
| Jul | 1.51 | 239 | 3.25 | 10.5 | 2230 | 2.08 |
| Aug | 1.49 | 229 | 3.07 | 10.0 | 2110 | 2.06 |
| Sep | 1.47 | 228 | 3.00 | 9.8 | 2070 | 2.04 |
| Oct | 1.43 | 223 | 2.86 | 9.4 | 1980 | 1.98 |
| Nov | 1.43 | 232 | 2.88 | 9.4 | 2000 | 1.97 |
| Dec | 1.44 | 233 | 2.86 | 9.4 | 1980 | 1.98 |
| 1987 Jan | 1.51 | 233 | 2.80 | 9.3 | 1980 | 2.06 |
| Feb 18 | 1.53 | 236 | 2.80 | 9.3 | 2000 | 2.04 |


Nominal exchange rate movements to date

| | Latest 18.2.87 | Dollar Peak 26.2.85 | % change to date | Plaza Agreement 20.9.85 | % change to date | 1986 Annual Meetings 30.9.86 | % change to date |
|--|-------------------|------------------------|---------------------|----------------------------|---------------------|---------------------------------|---------------------|
| <u>Effective rates</u> (1975 = 100) | | | | | | | |
| United States | 104.2 | 157.2 | -34 | 139.6 | -25 | 110.2 | -5 |
| Japan | 209.0 | 157.1 | +33 | 156.6 | +33 | 216.7 | -4 |
| Germany | 148.1 | 117.2 | +26 | 125.5 | +18 | 140.9 | +5 |
| France | 72.2 | 62.0 | +16 | 67.2 | +7 | 70.0 | +3 |
| United Kingdom | 69.3 | 70.2 | -1 | 82.0 | -15 | 69.0 | 0 |
| Italy | 48.5 | 45.1 | +8 | 44.0 | +10 | 47.7 | +2 |
| Canada | 78.6 | 88.5 | -11 | 85.6 | -8 | 77.0 | +2 |

Bilateral rates

| | | | | | | | |
|---------|------|-------|-----|------|-----|------|-----|
| Yen/\$ | 154 | 261 | +69 | 240 | +56 | 154 | 0 |
| DM/\$ | 1.83 | 3.43 | +87 | 2.84 | +55 | 2.03 | +11 |
| FFI/\$ | 6.09 | 10.50 | +72 | 8.68 | +43 | 6.64 | +9 |
| £/\$ | .65 | .95 | +46 | .73 | +12 | .69 | +6 |
| Lire/\$ | 1302 | 2166 | +66 | 1922 | +48 | 1402 | +8 |
| C\$/\$ | 1.33 | 1.41 | +6 | 1.38 | +4 | 1.39 | +5 |
| \$/£ | 1.53 | 1.05 | | 1.37 | | 1.45 | |

Note: Changes in bilateral rates show appreciation of currency against dollar





1 copy
2 copy

Treasury Chambers, Parliament Street, SW1P 3AG
01-270 3000

19 February 1987

David Norgrove Esq
10 Downing Street
LONDON SW1

Dear David

I attach the latest draft of the communique for the G5/G7 meetings this weekend. With the manuscript amendments marked - and new, stronger statements from Germany and Japan - the text is now virtually agreed.

Yours
Alas

A C S ALLAN

SECRETDRAFT STATEMENT

1. Ministers of Finance and Central Bank Governors of seven major industrialized countries met today in Paris to conduct multilateral surveillance of their economies pursuant to the Tokyo Economic Declaration of their Heads of State or Government of May 6, 1986. The Ministers and Governors, using a range of economic indicators, reviewed current economic developments and prospects. The Managing Director of the IMF participated in the discussions.

2. The Ministers and Governors were of the view that further progress had been made since the Tokyo Summit in their efforts to achieve a sustainable, non-inflationary expansion. Our economies are now in the fifth year of expansion, and the prospects are for continued growth this year, although the level of unemployment remains unacceptably high in some countries. A high degree of price stability has been attained, and there have been substantial reductions in interest rates. Exchange rate adjustments have occurred which will contribute importantly in the period ahead to the restoration of a more sustainable pattern of current accounts.

3. Progress is being made in reducing budget deficits in deficit countries, and fundamental tax reforms are being introduced to improve incentives, increase the efficiency of our economies, and enhance the prospects of higher growth. Other important structural reforms are also being made in our economies, including deregulation of business to increase efficiency and privatization of government enterprises to strengthen reliance on private entrepreneurs and market forces.

4. These positive developments notwithstanding, the Ministers and Governors recognize that the large trade and current account imbalances of some countries pose serious economic and political risks. They agreed that the reduction of the large unsustainable trade imbalances is a matter of high priority, and that the achievement of more balanced global growth should play a central role in bringing about such a reduction.

5. The Ministers and Governors reaffirmed their concern over continuing pressures for protectionism. They agreed that efforts to deal with economic problems by erecting trade barriers were self-defeating, and pledged to intensify their efforts to resist protectionism and reaffirmed their strong support for the new round of trade negotiations. They welcomed the progress made in the preparatory work for the new GATT round and the recent positive conclusions of discussions between the US and the EC on bilateral trade issues.

?
- The French Government will reduce the Central Government budget deficit by % of GNP from 1986 to 1988 and in the same period will implement a tax cut program of the same order of magnitude (1 % of GNP) with substantial tax rate cuts for corporations and individuals. It will pursue in 1987 its ambitious privatisation program (with a projected \$ 6 to 7 billions sale of assets) and reinforce the liberalisation of the French economy, especially of labor and financial markets.

?
to be made stronger
- The Government of the Federal Republic of Germany will pursue policies to diminish further the share of public expenditures in the economy and to reduce the tax burden for individuals and corporations with a comprehensive tax reform aimed at reinforcing the incentives for private sector activity and investment. This will be in addition to the substantial tax reductions already enacted for 1988. The Federal Government will emphasize policies that enhance market forces in order to foster structural adjustment and innovation. Monetary policy will be directed at improving the conditions for sustained economic growth while maintaining price stability.

- The Government of Japan will follow monetary and fiscal policies which will help to expand domestic demand and thereby contribute to reducing the external surplus. The comprehensive tax reform, now before the Diet, will give additional stimulus to the vitality of the Japanese economy. Every efforts will be made to get the 1987 budget approved by the Diet so that its early implementation^{can} be ensured.

← The Bank of Japan has announced that it will reduce its discount rate by % on (date...)

see revised version attached
[The UK Government will continue to work to reduce inflation further by following a prudent monetary policy ; to reduce the share of public expenditure in the economy thus enabling lower taxes to be combined with a declining path for the budget deficit as a percentage of GDP ; to strengthen the supply performance of the economy and maintain the improvement in the growth of productivity ; to promote in the future the steady growth of output and GDP achieved over the past five years ; and will seek to maintain broad balance on external account over the medium term.]

?
- The United States Government will pursue policies to reduce the budget deficit with a view to achieving a \$65 billion reduction in fiscal 1988, to 2.3 percent of GNP. For this purpose, the growth in Government expenditures will be held to less than 1 percent in fiscal 1988. As part of the continuing program to reduce the share of Government in GNP from its current level of 23 percent the United States will introduce a wide range of policies to improve its competitiveness and to enhance the strength and flexibility of its economy. Monetary policy will be directed toward permitting the economy to expand at a sustainable non-inflationary pace.

6. The Ministers and Governors recognized that the major industrial countries have a special responsibility to follow policies which foster an open, growing world economy in order to support the efforts of debtor countries to restore steady growth and viable balance of payments positions. They noted the progress that had been achieved by many debtor countries toward these ends, but stressed the importance of all participants in the strengthened debt strategy reinforcing their cooperative efforts to resolve international debt problems.

7. The Ministers and Governors agreed to intensify their economic policy coordination efforts in order to promote more balanced global growth and to reduce existing imbalances. Surplus countries committed themselves to follow policies designed to strengthen domestic demand and to reduce their external surpluses while maintaining price stability. Deficit countries committed themselves to follow policies designed to encourage steady, low inflation growth while reducing their domestic imbalances and external deficits. To this end, each country has agreed to the following undertakings.

Insert para 8 here.

8. The Ministers and Governors also agreed to additional refinements in the use of economic indicators for the multilateral surveillance arrangements approved by their head of State of Government in the Tokyo Economic Declaration. As part of these refinements, they will :

- Periodically ^{review} ~~discuss/seek~~ a common understanding ~~on/develop~~ medium term economic objectives and projections involving domestic and external variables. The medium term objectives ~~are~~ to be mutually consistent and will serve as a basis for assessing national policies and performance.

- Regularly examine, using performance indicators, whether current economic developments and trends are consistent with the medium term objectives and projections and consider the need for remedial action.

^{initially,}
For ~~1987~~ the objectives and projections will involve the following key variables :
growth, inflation, current accounts/trade balances, monetary conditions budget performance,
~~interest rates and~~ ^{and} exchange rates.>

? insert "and projections"

Now to alter para 6

9. The Ministers and Governors noted that a number of newly industrialized countries were playing an increasingly important role in the world economy. These countries have achieved strong economic growth based significantly on their access to open, growing export markets. Recently, some have accumulated trade surpluses which have contributed importantly to the present unsustainable pattern of global imbalances, thus increasing protectionist pressures. The Ministers and Governors considered ^{that} it is important that the newly industrialized developing countries should assume greater responsibility for preserving an open world trading system by reducing trade barriers and pursuing policies that allow their currencies to reflect more fully underlying economic fundamentals.

10. The Ministers and Governors agreed that the substantial exchange rate changes since the Plaza Agreement will increasingly contribute to reducing external imbalances, and have now brought their currencies within ranges broadly consistent with underlying economic fundamentals, given the policy commitments summarized in this statement. Further <substantial/excessive> exchange rate shifts among their currencies <could/would> damage growth and adjustment prospects in their countries. In current circumstances, therefore, they agreed to cooperate closely to foster stability of exchange rates <within recent ranges/~~around recent levels~~>

either

REVISED PARAGRAPH ON UNITED KINGDOM

The United Kingdom Government will maintain conditions for continuing the steady growth of GDP of the past five years and will continue to work to reduce inflation by following a prudent monetary policy. On external account the aim will be broad balance over the medium term. The share of public expenditure in the economy will continue to fall and the burden of taxation will be reduced, while public sector borrowing is maintained at a low level. These and other measures to strengthen the supply performance of the economy will reinforce improvements over recent years in the growth of productivity.

REVISED PARAGRAPH ON UNITED KINGDOM

OK: delete words in square brackets & make no other changes - I have written!

The United Kingdom Government will maintain conditions for continuing the steady growth of GDP of the past five years and will continue to work to reduce inflation by following a prudent monetary policy. On external account the aim will be broad balance over the medium term. The share of public expenditure in the economy will continue to fall and ~~tax reform will be carried further and the total~~ burden of taxation ^{the} ~~will be~~ reduced, while public sector borrowing is maintained at a low level. These and other measures to strengthen the supply performance of the economy will reinforce improvements over recent years in the growth of productivity.

X |

Y |

Ch

Despite 'X', David Nargrove wondered if 'Y' wd be misinterpreted as a hint about your 1987 Budget*. Do you think there is a problem?

David
19/2

Ch

This concern is about the square bracketed words.

- (a) stimulates expectation of tax-reforming Budget - which will be disappointed
 - (b) could be taken as further fuel for "income tax slashed, VAT doubled" etc.
- I'm inclined to agree. AA

purp

S E C R E T

FROM: DAVID PERETZ
20 February 1987

PRINCIPAL PRIVATE SECRETARY

cc Sir P Middleton
Sir T Burns
Sir G Littler
Mr Cassell
Mr Lavelle
Mr Evans
Mr Kelly
Mr Culpin
Mr Pickford
Mr Towers*Y
=
r* *α* *\$Cam*

G7

May I feed in a few thoughts from Mr Kelly and myself on the briefing attached to Mr Culpin's minute of 19 February. There are not many.

2. In general, we thought it might be possible to be a little bit more robust on both of the two main lines of attack that Robert Culpin identifies. On the first I would hope we can say fairly robustly that the agreement means what it says: it is a judgement about current circumstances, not some prescription about target zones for the future. And on the second I do not see why we should not accept that in current circumstances we would prefer there not to be substantial movements either upwards or downwards in sterling. We certainly do not want to leave it looking as if sterling is excluded from the agreement: that is the way to get currency markets to switch their attention to us.

do with you

3. On the draft answers, we have the following suggestions:-

What sort of ranges do you have in mind?

✓ Delete "wait and see". It suggests that there are specific ranges for sterling which people will find out in due course.

4. Then I would suggest replacing the second, third and fourth answers to "Questions on Britain" by the following:-

Have you or have you not a collective agreement to support sterling at present levels?

Agreement applies to all seven currencies. Says that we are broadly agreed on the present pattern of exchange rates, and have agreed to "co-operate closely to foster stability".

Have you a range in mind for sterling?

Agreement means what it says. Chancellor has on a number of occasions made it clear that he does not want to see the pound fall any further; but by the same token has no wish in present circumstances to see a substantial rise. (This was the line the Chancellor himself suggested earlier on.)

5. Finally, I think we need a little more on interest rates. The difficult question is about what we would do on interest rates if sterling were to rise substantially. I suggest replacing the last question and answer with the following:-

Does the agreement mean a fall in sterling interest rates?

Interest rates not part of the agreement.
~~No plans to reduce interest rates [at present].~~ Will continue to set these at whatever levels are needed to maintain downward pressure on inflation.

What will happen to interest rates if there were a substantial rise in sterling?

A substantial rise in sterling would obviously be an important factor to be taken into account in assessing monetary conditions and decisions on interest rates.

DLCP

D L C PERETZ