PO-CH/NL/0093 PT A

Part: A.

SECRET

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Begins: 9/4/87.
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PO -CH /NL/0093

PART A

PO -CH /NL/0093
PART A

Chancellor's (Lawson) Papers;

GROUP OF FIVE SEVEN AND
TEN MEETINGS WASHINGTON
SEPTEMBER 1987

Disposal Directions: 25 Years

1/8/95.

G5
8/4/87

CONFIDENTIAL

For Washington

NOTE FOR THE RECORD

9/4/87

cc: Chancellor
Sir P. Middleton
Sir T. Burns
Mr. Cassell
Mr. Peretz
Mr. Kelly

Governor
Mr. Loehnis

MEETING OF G5

A meeting of the Group of Five Finance Ministers and Central Bank Governors was held in the United States Treasury from 11.00am until just after 2.00pm on Wednesday, 8 April 1987. (Press and television were aware of the meeting and witnessed arrivals and departures, but cordoned off to avoid direct contact with participants).

2. The attendance was the full normal complement of three per country, plus Camdessus (Managing Director of the IMF) for the first part of the discussion.

3. Opening the discussion Camdessus reviewed the estimates and forecasts he had circulated, which incorporated assumptions based on the Louvre Accord. He drew attention to the disappointingly weaker domestic demand growth forecasts, some half per cent less than projections of last September which had been described as "satisfactory, but only barely so". All G5 countries except the United Kingdom were expanding at below potential. Prospects for inflation were not worrying. Current account imbalances showed a very slight improvement, mainly due to assumptions of slower domestic growth in the United States, but left grave doubts about sustainability.

4. In conclusion, he said that:

- there had been impressive support for the Louvre Accord: Executive Directors of several countries who were not participants had asked him to convey their warm welcome of this initiative;

- market reactions to the Accord had been interesting: apparent endorsement of the dollar rate against European currencies, but doubts about the dollar/yen relationship;

- there was a growing worry over trade issues and prospective conflicts and he begged that all should try to prevent these from escalating;

- in the trade-off between growth and inflation, he felt that the risks lay rather in the threat of inadequate growth than in the threat of excessive inflation.

5. Baker (United States) drew the broad conclusion that things looked worse since the Paris meeting, rather than better, with some clear danger signals on world growth. There had to be general agreement that not enough corrective action had yet been taken. As far as the United States economy was concerned, he thought they were on track for 1987 on the reduction of the fiscal deficit to around $175 - 180 billion (3.9% of GDP). The aim would be to carry this forward with a further reduction to about 2.9% of GDP in fiscal 1988. The general run of economic statistics so far this year was reasonably satisfactory, with growth sustained and unemployment actually reduced. The latest estimates of GDP growth, fourth quarter on fourth quarter, were 3.2% up to end 1987 and 3.7% to end 1988. But there would be a modest reduction only in current account imbalances, by no more than $15 billion in 1987, and prospective figures beyond 1987 were sobering. It was not surprising that the protectionist threat had grown stronger.

6. Stoltenberg (FRG) acknowledged that the growth projections were disappointing and would give rise to concern during Interim Committee discussion. Germany was one of the countries over which disappointment was being expressed. He felt that the figures were by no means so bad as represented. There had undoubtedly been a slackening of growth. Part of the problem was to convince the German public, trade unions and managers, of the need to adjust to new prices and conditions. But he was confident that the German external surplus would decline faster than the IMF forecasts suggested.

7. Balladur (France) spoke briefly of the French position, not significantly different from the IMF figures. He said he was confident that the policies embodied in the Louvre Accord were the only route to sustained non-inflationary growth. He noted that some countries plainly had more room for manoeuvre than others - largely because of the success of good policies in the past - and suggested that they should use that room for manoeuvre now.

8. The Chancellor began with a request to the Managing Director to carry forward the IMF staff work on the world current account deficit, and attempt roughly to assign it among countries and groups of countries, which might be helpful in giving a better picture for some countries. He then spoke briefly of the recent UK Budget, in which he had reduced both public sector borrowing and taxation, and noted that his estimates for it were based on an oil price of $15 per barrel - a higher price would tend to improve UK government revenues and current account balance.

9. On the world prospect, he accepted the downward revision of forecasts of world growth. There was an element here of the unavoidable cost of adjustment, which involved not only political difficulties, but frictional costs in the form of poorer economic performance in the short-term. We should not be surprised: much the same had happened in 1986 as a result of the shock of large price reductions in oil and many other commodities. The problem of making the adjustment process more efficient took us into the micro-economic field. He agreed with Stoltenberg that it was vital to get managers and unions to understand changed conditions and work with them. This was particularly true in Japan, given the scale of the adjustment needed from a traditionally export-based economy. He recalled the Plaza Communique

in which Japan had undertaken - as the first in a series of important policy directions - to open up its domestic markets to foreign goods and services. He had to say that he was not satisfied that the commitment had been honoured - and it must be. Protectionist pressures were building up now in the United Kingdom and other countries as well as the United States.

10. Miyazawa (Japan) spoke of the current budget situation in Japan due to difficulties in the Diet. He described the new package of measures decided the day before by the Liberal Democratic Party. (He explained that the Japanese Government had been unable to present such an agreement because it was constitutionally impossible for them to suggest a supplementary budget until Parliament had cleared the main budget: that was why agreement had been reached in the Party, but under the Chairmanship of the Prime Minister). The package involved accelerating public works and other expenditures, but also a later supplementary budget so that the higher level of expenditure could be maintained throughout the year. The total additional stimulus could be of the order of $35 billion (worked out on the spot as being 1.5% of GDP). He wanted to emphasise that there was a real break-through in Japanese thinking reflected in a decision by the Liberal Democratic Party of this kind, to abandon the broad austerity approach of previous budgets, and go for expansion. He concluded by thanking colleagues warmly for the cooperative help they had given in stabilising the yen/dollar rate.

11. Baker said that others might be interested to know that the United States had talked bilaterally with Taiwan and South Korea recently about their exchange rates. They intended also to talk with the Hong Kong authorities. The Chancellor briefly rehearsed the special position of Hong Kong, arguing also that the total freedom of trade in Hong Kong distinguished the colony from the other newly-industrialised Asian countries. Baker suggested that others would not be prepared to move unless Hong Kong did, but the Chancellor crisply rejected this as an unsatisfactory excuse. At this point Camdessus left the meeting.

12. Introducing a discussion of the Louvre Accord, and after recapitulating developments since it took place, Baker said that he would be willing to extend the arrangement, in the form of a G7 agreement, on three conditions, all relating to the yen which had proved the most vulnerable part of the arrangement:

- he would want a public statement containing an adequate expression of the expansionary measures agreed by the Liberal Democratic Party

- the central point of the yen in understandings about cross-rates must be rebased

- there must be European undertakings actively to support the dollar/yen relationship as well as the relationship between the dollar and European currencies.

On that basis, he would be prepared to increase the US commitment (in terms of total intervention). He thought it would be right to aim to hold the position until the OECD meeting, rather than committing ourselves now to go as far as the Summit.

13. Balladur said that the Louvre Accord had worked well. German announcements and the UK Budget in the intervening period had both been important steps in the direction of implementing policy undertakings. The problem lay with the yen, where the market had undoubtedly tested the agreement and there was need for signs of a strengthening of Japanese policy. But he wanted to see the agreement continue, and wondered whether there might be advantage in strengthening the scale of resources available to participants to support it. He differed from Secretary Baker on the idea of an extension only until May. If the original agreement came to be reviewed very frequently, it would begin to take on the form of a continual negotiation. We should as a minimum agree to extend until the Venice Summit. (In a brief exchange with Secretary Baker, Balladur accepted that the agreement might be kept under regular review, but insisted that this must not be on the basis of revising the agreement every time, or having ministerial review meetings).

14. Stoltenberg expressed strong agreement. It was important to present at the Venice Summit evidence of improved international economic cooperation. It would be a bad failure to give up the Louvre Accord now. There was indeed a special problem over the yen, but we must find ways of coping with that. He could go along with the conditions suggested by Baker. He added that he thought it particularly important to keep under control the problem of trade disputes. Japan must understand the attitudes of other countries, which had been given pledges in various forms (in the Plaza Communique, at the Tokyo Summit, in the Maekawa Report, etc.) which they felt there was little evidence of Japan fulfilling. What was needed was some early decisions and actions which would give a real signal of more open markets.

15. Discussion continued over lunch. The Chancellor said that all seemed to agree with the objective of maintaining the Louvre Accord, and he certainly shared with European colleagues a desire to extend it until the Venice Summit and beyond. He would like to follow the thought in Secretary Baker's three conditions with slight modifications following what Stoltenberg had said. Certainly the yen would have to be rebased. If that was done, he thought there would be no problem of principle in European support, and the technical problems should be left to technicians to resolve. On the important first condition, he welcomed Miyazawa's account of the Liberal Democratic Party intentions but he would like also to emphasise the importance of a contribution on more open trade in goods and services. He saw this as being important in economic terms, in political terms and in terms of impact on markets. He very much hoped that an appropriate sentence could be included in the public statement - indeed failure to make some mention of this problem would have an odd appearance in present circumstances. Finally, he offered the general thought that, if we wanted stability of exchange rates, all - particularly including the largest countries - must be prepared occasionally to subordinate domestic policies to external needs. This meant using interest rates, not merely intervention.

16. Miyazawa indicated acceptance of the conditions proposed by Secretary Baker, and of the additional point on trade suggested by the Chancellor. Summing up this part of the discussion, Secretary Baker suggested that there should be - for discussion among the G7 - a short statement reaffirming the Louvre Accord, referring to the two points of Japanese policy (supplementary fiscal measures and opening up markets) and repeating the aim of stabilising exchange rates.

17. Further discussion on intervention is recorded in a separate note with limited circulation.

Sir G. Littler
9 April, 1987

SECRET

NOTE FOR THE RECORD

c.c. Mr Peretz
Mr Kelly
Mr Loehnis (B/E)

MEETING OF G5

This is a supplementary, with very limited circulation, to the record I wrote on 9 April of the G5 meeting in Washington on the previous day. It covers: the new central rates, and intervention.

Rates

2. I included in the previous record the fact that Baker and others had demanded, and Miyazawa had agreed, that the yen should be "rebased" in a continuation of the Louvre Accord. I did not mention figures. In fact the US suggestion, which was agreed without detailed debate, was simply that the "current levels" which had been agreed in Paris should be amended in just the one respect, that instead of Yen 153.50 = $1, we should substitute, based on the previous day's approximate rate, Yen 146 = $1. The operating 'margins' for intervention would be the same ratios as agreed in Paris.

Intervention

3. There was an appalling discussion over lunch in the G5 about sharing the burdens of intervention. It began with Baker offering to raise the limits of US intervention from $4 billion to $5 billion provided Japan and Europe would match this with what he described as "honest-to-gosh" intervention. Poehl said he did not understand: apart from the fact that we should take some account of what had already happened, there were problems about mounting intervention between currencies which did not include one's own. Baker said he could not commit the US unless all others committed themselves. Larosiere and others urged that calculations on any precise basis were pointless. There was a lot of talk about the value and feasibility of yen/dollar intervention by others (some of it - especially by the US Treasury - very ignorant!). Mulford tried various splits of dollar/yen and dollar/DM reserves to meet Poehl's point that he was not going to spend anything on holding the yen if, when the DM then came under strain, the US were going to plead that they had spent their all on the yen and could do no more. His arithmetic was not well received.

Comment & currency reserves

4. There was no agreement. Stoltenberg suggested that central bankers could be left to sort things out, and we would have to consult again if limits were reached, whatever they were. The Chancellor rounded off the discussion by suggesting that, since we plainly all agreed we could now end the meeting!

5. I understand that there was some subsequent (and rather more sensible) discussion among central bank representatives.

(Geoffrey Littler)
H.M.Treasury
15 April 1987.

for Washington Tky

SECRET

2 pages

Attached is a detailed note of the weekend meetings of Finance Ministers and Central Bank Governors in Paris, together with a copy of the published Communique and a "non-paper" on the broad arrangements for intervention.

Please note that the details of the intervention arrangements are particularly sensitive. Any necessary discussion of them should be kept to those directly concerned in operations.

(Geoffrey Littler)

Copies:-

Chancellor
Sir P.Middleton
Sir T.Burns
Mr Cassell
Mr Lavelle
Mr Peretz
Mr Huw Evans
Mr C W Kelly
Mr Culpin

Governor (B/E)
Mr Loehnis (B/E)
Mr George (B/E)
Mr Gill (B/E)

Ch
You asked to see this.

Thanks AA

(psc nc my papers for Washington)

'NON-MEETING'
21-22/2/87

SECRET

Note for the Record

MEETINGS OF FINANCE MINISTERS AND CENTRAL BANK GOVERNORS IN PARIS ON 21-22 FEBRUARY 1987

G5

A "non-meeting" of G5 (see below) was held in the French Ministry of Finance on 21 February, attended by the Finance Ministers, Central Bank Governors and Deputies of the G5, as follows:

- France: Balladur (Chair), Larosiere, Lebegue
- U.S.: Baker, Volcker, Darman
- Germany: Stoltenberg, Poehl, Tietmeyer
- Japan: Miyazawa, Sumita, Gyohten
- U.K.: Chancellor, Governor, Littler

Camdessus (IMF Managing Director) attended for the first two hours. Mulford (U.S. Deputy) and Trichet (Chef de Cabinet to Balladur) were extras at the dinner. There was an English/French translator present throughout.

2. The meeting began just after 3 p.m. on 21 February. (The U.K. party arrived just before 4 p.m. - due to Air France delays). It ended at 10 p.m. - when Balladur had an appointment to meet the Italian Finance Minister. The agenda circulated in advance was followed fairly closely.

Multilateral Surveillance

3. Camdessus gave his view of the position and prospects of G5 countries and the world economy based on figures circulated in advance (and not challenged other than marginally). He also referred to debt problems, and particularly Brazil. Shortly after the U.K. party arrived he reached his conclusions, which he summarised as follows:

- strong adjustments would be needed to establish robustly stable exchange rates; possibilities of such adjustments in the immediate future might be constrained, in which case more would be required later;
- there was no reason to suppose the same adjustment was needed in the DM/$ and Yen/$ cases;
- there was certainly a good argument at present for a pause, to allow effects of past changes to work through and make an assessment of them;
- the G7 must not put their own credibility at risk;
- therefore they must make sufficiently strong commitments and be prepared to carry them out for a sufficient time;
- good intervention arrangements would be needed, although that did not mean they would be sufficient alone;
- markets would have the last word - which reinforced the importance of the G5/7 being seen to act in unison.

4.   Baker noted that the IMF projections showed only modest reductions of the major current account imbalances by 1988. There was a need for measures to stimulate demand in surplus countries. He acknowledged the timing constraints on public announcements now, but these should have gone by April. He was therefore thinking in terms of an agreement to stabilise exchange rates up to the April meetings, at which the situation could be reviewed.

5.   Miyazawa said that his experts thought the IMF were being too pessimistic, but he was personally inclined to agree with the IMF. The political problem in the Diet tied his hands at present. But when that was out of the way, he intended, assuming he was still Finance Minister, to present a supplementary budget with new capital expenditure and other measures, and to tackle the next year's budget preparation on a different basis (he thought he might prove to be the first Japanese Finance Minister to deliver on such promises!). In answer to interjected questions he said he thought April or May for the supplementary budget (because the Diet was delaying the main budget); and the sales tax might be somewhat modified or postponed - it could not be dropped without grave loss of credibility by the Government.

6.   Stoltenberg made three main points. First, the nominal dollar statistics masked the extent of the impact of exchange rate changes which was already being felt and reflected in volume changes in German trade. Secondly, the German fiscal balance was being significantly worsened by lower tax receipts from companies suffering cuts in profit as a result of DM appreciation. Thirdly, he would nevertheless be announcing substantial increases in tax reductions for 1988 and a big further programme of both reform and reduction of taxation (which however he could not specify before conclusion of the coalition negotiations).

7.   The Chancellor said that he broadly accepted the IMF figures but would present the U.K.'s own latest figures in his forthcoming budget. Meanwhile he had two general comments. First on policies: the three countries which were in major imbalance were pursuing the right policies; but markets were not convinced that they would carry them through adequately, with appropriate reinforcement if necessary; the problem was to speak and act with the necessary conviction. Secondly on exchange rates: following the massive changes which had taken place, whose effects were not yet visible, there was a strong case for a period of stability; but if we wanted stability, we must talk the language of stability and not confuse markets with other language which might suggest conflicts and uncertainties.

8.   This provoked comment. Most others strongly agreed, but Volcker said it was all very well to talk of stability but the IMF figures suggested no basis for it without further policy measures. After some scrappy debate, Darman found a formula which commanded general assent: that it was right now to go for a period of stability on the assumption of present policies and vigorous pursuit of policy intentions, but it would also be right to take stock in April to see whether that assumption was valid.

9. In answer to a question by Stoltenberg, Baker said that the Congress was indeed leaning to more moderate views on trade protectionism, but the risk remained that their leaders could be driven into courses they themselves would dislike, if refusal to cooperate on the part of other countries led them to think that was the only way to bring effective pressure to bear.

10. Balladur, summing up, noted several positive features in the world economic scene; but expansion was too slow to help solve unemployment problems or problems of major debtors. He earnestly hoped that protectionism would not gain ground, and that further substantial exchange rate changes could be avoided. He warmly thanked the IMF Managing Director, who then left the meeting.

The Italian Problem

11. Balladur reported frenzied diplomatic activity on the part of the Italians, incensed by rumours of a prior G5 meeting which they and the Canadians would merely be allowed to endorse. He proposed a form of words for all to use in answer to questions. After minor changes, the agreed version was: that there had been only informal consultations and a private dinner today, and that the only formal meeting was that of G7 tomorrow.

Draft Statement/Communique

12. The text of the draft Communique was then circulated. The points of interest, apart from a long argument on the last phrase of the text, were two remarks by Volcker: first, unsuccessfully, he tried a couple of times to insert a reference to the recent slow-down in growth; secondly, during brief discussion of the paragraph referring in passing to debt, he argued that debtor countries were doing their part but the commercial banks were uncooperative players - this drew protests from several others.

13. On the last three words of paragraph 10 at the end of the draft communique, there had been a history of argument between the alternatives "within recent ranges" and "around recent levels". The U.S. and France had insisted on the former; the U.K. and, as we thought, others had eventually all acquiesced. However, the discussion at the meeting was opened by Volcker asking that "around present levels" should be adopted instead of "around recent levels". The Japanese saw this as an attack on their wish to go for a range of 150-165 Yen to the dollar (which it was) and argued for a long time in favour of the word "recent". In half an hour of discussion the "ranges" version was never mentioned. The argument was eventually resolved following two comments by the Chancellor: first, he suggested that the object of stability would be much better reflected in the clear "present" than the more ambiguous "recent"; and secondly (on Miyazawa's appeal for an alternative English word) he suggested "around current levels" which was received with unanimous acclamation!

SECRET

Exchange Rate Management

14. Baker presented what he described as a secret 'non-paper' covering various "Understandings on intervention". There was much scepticism and disagreement (Larosiere said it was altogether a bizarre paper) - the main difficulty was over the attempt to deal with shares in the total of intervention - but in an effort to keep the spirit of U.S. cooperation the text was eventually endorsed with various amendments such as insertion of "as a general rule" to reduce the rigidity of the original. This non-paper did not in either initial or final version contain any figures for intervention points. (In various bilateral talks in the margins of the meetings it was agreed that arrangements within Europe would be flexible, and the question of precisely how the various possible transactions would 'count' in shares relative to U.S. and Japan was left vague - partly because the U.S. concepts were ill-thought-out. At no time were special demands made of the U.K. and sterling, beyond consistent behaviour; but Poehl hoped and expected that actual U.K. interventions would be helpful in the 'count'! - e.g. if the U.K. continued to recoup some earlier dollar losses). Poehl said that he hoped to bring in Switzerland as well as other ERM countries as extra collaborators, which was welcomed.

15. Before the meeting broke for dinner, the Chancellor took the opportunity of emphasising the two conditions which he thought indispensable to a credible operation. First, action by the U.S. must be visible and unambiguous. Secondly, everybody should adopt a policy of silence vis-a-vis the press: statements over the last few weeks had done a great deal of damage and that practice should cease. Both points were strongly endorsed, except that the U.S. representatives quibbled about the meaning of visibility of their action, and the Japanese stayed silent!

Miscellaneous Items

16. Over dinner, some miscellaneous points were disposed of:

- Press Conference: it was agreed that Balladur would be flanked by all Ministers, and that all would make short statements.

- Future of G7: Balladur reported that the Italians were pressing two points: that Central Bank Governors should be included in all G7 meetings (except any at Summits); and that there should be two meetings of G7 deputies per year. The first point was agreed. On the second it was agreed that G7 deputies would in practice meet in the course of Summit preparation meetings and no further arrangements should be made.

- "Indicators" Exercise: Lebegue offered to circulate a paper, but the Chancellor refused this, on the grounds that the subject was for the April meeting, not for this one. Lebeque said that the problem was that the deputies needed guidance for continuing the work. The Chancellor explained his reasons for wanting to avoid discussion of the subject now: it could lead to disagreement and this in turn allow the press to speak of 'disarray'; and the draft he had seen included exchange rate material which could be seen as inconsistent and confusing in relation to this weekend's meetings. Stoltenberg agreed and it was left that the subject would be reconsidered in April.

- Balladur warned that the EC Commission would seek again to be allowed to join G7 meetings, and that France would not oppose. Baker assured his colleagues that the U.S. would remain unalterably opposed, and would simply not attend meetings if the Commission were present.

Intervention Points

17. After some preliminary skirmishing among the bankers it was established that the "current levels" must be interpreted as the official rates at the close of business on the previous day, which for present purposes were agreed (? European close) to be:
DM 1.825 = 1 dollar Yen 153.5 = 1 dollar

18. There followed a long argument, essentially Japan against all others, as to whether the margins around these rates should be symmetrical or not. The Japanese were particularly anxious to get agreement of the U.S. to help prevent the Yen appreciating above 150 and wanted a range of 150-165, heavily skewed compared with the "current level". The Chancellor supported the efforts of others to shift the Japanese by arguing that "stability" would be better served by a symmetrical arrangement, which left only the amplitude of variation for discussion. Larosiere effectively took over the chair (acting very much as Managing Director) and gently and skilfully led all, including the Japanese, to agree on:

- "current level" DM/$ and Yen/$ rates as stated above;
- a limit of some 2.5% around these rates (both ways) as marking the points at which concerted intervention would be appropriate (giving the Japanese their 150 figure);
- a sense of some wider limit, perhaps twice the width, at which - if markets were still pressing in spite of the actions taken by the authorities to stabilise rates, it could be appropriate to take stock again.

Subject to insistence by Poehl and others that the arrangements must not be interpreted rigidly (and that central bank operators must concert together from day to day), this was agreed.

19. There was passing reference to the French franc/dollar rate which had to be consistent with the DM/dollar and the ERM. No particular rates were agreed for sterling or other currencies, and it was explicitly assumed that Canada would not be participating on the same basis as others.

SUNDAY MEETINGS

20. The formal meeting of G7 Ministers and Central Bank Governors was due to begin at 9.30 a.m. on 22 February. It did so without any Italian representatives. Those present the previous day were therefore supplemented by the three Canadians only.

21. Opening the meeting, Balladur said that he had talked with the Italian Finance Minister as planned the previous evening. Goria had complained about the G5 dinner, claiming that it had been a working dinner and that this was a breach of understandings between them. Balladur had tried to show him reasons why he should accept the situation and join in the important work of today's meeting. But Goria had refused: he maintained that the Saturday meetings were a violation of the Tokyo Summit agreement and a betrayal of assurances he had been given "at a high level" (Balladur said: "c'est a dire moi, je suppose!"). Italy would refuse to attend today's meetings, therefore, and the whole matter would be raised at the Venice Summit. Balladur added that he had just learned that Goria would be giving a press conference in Paris at 11 a.m. today. (During the ensuing brief discussion he received and read out a report of an Italian official statement, repeating what Goria had said to him).

22. Concluding his opening remarks Balladur said that in his view we now needed a clear understanding: either there was no G5, or there was no G7, or there were both and both were acceptable. He thought it could be useful to agree a common line of comment on the Italian position and would present later a short drsft. There was general agreement, followed by some inconclusive discussion of the nature of the present session in the circumstances - left to be defined in settling the terms of the Communique.

23. Camdessus was then invited to make his presentation. He gave a somewhat briefer version of what he had said the previous day. Comments also followed the lines of discussion previously, picking out main points partly for the benefit of the Canadians. Wilson focussed on the problems of commanding credibility and confidence in markets, which in his view required not only signs of immediate joint action but also a sense of continuity of the cooperation between the major countries.

24. At this point the IMF Managing Director left the meeting; news of Goria's proposed press conference arrived; and Balladur circulated his draft guidance on the Italian problem. It was agreed to play the whole incident down if possible: in answer to questions - not otherwise - it would be right to say that the Tokyo Summit declaration envisaged continuance of G5 as well as establishment of G7, that Saturday's meetings had not been in conflict with that arrangement, and that Goria and Wilson had been both warned and included in the series of bilateral discussions; and finally that the others regretted the Italian decision and hoped to see Italy at future G7 meetings.

25. The draft Communique was then discussed and agreed, after incorporating a number of minor amendments. The most awkward problem arose over the definition of the group issuing it, as finally resolved in the wording of paragraph 1. This reflects both the fact of six nations only being involved, and the context of the Tokyo Summit Declaration (which alone validated Canadian presence and was understandably a point to which Wilson attached great importance). The text of the Communique in its final form is attached.

26. Balladur then asked Larosiere to spell out for Wilson's benefit the proposed intervention arrangements. He did so in the form of seven points of agreement, mentioning no figures:

- given existing and intended policies and actions, the present structure of exchange rates was broadly right in relation to fundamental economic conditions;
- further substantial exchange rate shifts could do damage;
- the SDR currency countries (G5) had therefore agreed to cooperate to foster stability of their rates around current levels;
- they would cooperate on a pragmatic basis with close and regular contact between central banks;
- they would treat variations from current levels on a symmetrical basis, i.e. seeking similar restraint against unwelcome movements in both directions;
- intervention, where appropriate, would be visible, even where not officially confirmed;
- they recognised that overall policy convergence remained critically important.

27. At this point the meeting suffered the last interruption on account of Italy. With some astonishment, Balladur read out news he had just received of an official Italian statement that, if they were not offered a satisfactory solution to the problem of which they complained, they would cancel the Venice Summit! He suggested that in response to this high drama it would be right for all present to adopt a low profile and simply carry on with the important immediate business, and this was agreed.

28. Reverting to the proposed intervention arrangements Wilson noted that the agreement had been described as applying only to the SDR currencies. Baker said that he envisaged not imposing on Canada some of the specific obligations which would rest on the G5, but hoped that Canada would be able to operate in the spirit of the agreement, on lines which the two of them had discussed together. Wilson said that Canada's policy was, and he thought could consistently with what Baker had said remain unchanged, to moderate excessive movements of the Canadian dollar against the U.S. dollar, a policy which should be conducive to the stability being sought. Others found this acceptable.

29. Over lunch there was brief discussion of arrangements for various future meetings:

- the Chancellor said that, as current Chairman, he was arranging for a very short G10 meeting in Washington in the early part of the morning on which the meeting of the Interim Committee would be held;

- it was agreed that a G5/7 meeting would be held, probably on the previous day (the format would have to await any developments over Italy); the agenda should include any necessary preparation for the other Washington meetings, debt, progress towards a report for the Venice Summit and the "indicators" exercise;
- G7 deputies could find an opportunity to meet before then in response to Wilson's urging and the probable need to prepare for G7 discussion.

30. Finally there was a brief exchange on debt problems. This was confined to remarks by Baker and Larosiere about the renewed risks of widespread rebellion by Latin American debtors and the consequent advantage of picking off and settling some (Mexico, Chile, Ecuador, perhaps Venezuela and even Philippines) ahead of possible major difficulties with Brazil and Argentina. Trichet, (Chairman of Paris Club although present as Balladur's Chef de Cabinet) took the opportunity of emphasising the major contribution of official creditors in Paris Club reschedulings over the last four years.

31. Before the end of lunch, Stoltenberg congratulated Balladur on his excellent hosting and chairmanship of the meetings and there was general acclamation.

Press Conference

32. A press conference was held at 2 p.m. Balladur made a general statement and each of the other five Ministers spoke briefly and supportively. Details are recorded separately.

(Geoffrey Littler)
H.M.Treasury
23 February 1987.

UNDERSTANDINGS ON INTERVENTION *SECRET*

1. BASIC STRATEGY

To promote greater exchange rate stability by seeking to maintain exchange rates around current levels for the time being. These understandings will be reviewed in a normal way at a meeting in early april in conjunction with the spring meeting of the Interim Committee. There would be no bias toward dollar purchases as opposed to dollar sales.

2. TACTICS

Participants will seek to avoid predictability in intervention activity. Intervention may occur when there is large and/or volatile movement of exchange rates, and would be expected as exchange rates deviate substantially from current levels. Levels and amounts of intervention would be discussed among participants on a day-to-day basis in light of market conditions.

3. SCALE

Total net intervention (dollar market only) would be maximum of $12 billion during the period until the next meeting. Daily amounts would vary, but would not ordinarily exceed $300 million for either the United States, Europe and Japan.

4. CURRENCY

As a general rule : for the United States, yen/$, DM/$; for others (except EMS interventions), dollars against national currency.

5. PROPORTIONATE SHARES

United States, Europe and Japan would have approximately equal shares over time. (Dollar sales or purchases offset through other EMS transactions would not be included in totals.) Participants would endeavour not to intervene in directions inconsistent with the basic purpose of the exercise without prior consultation.

6. VISIBILITY

Operations will be conducted without attempting to disguise them, and on occasion with the intention that they become known in the market. However, no official confirmation of intervention except in accordance with established subsequent publication policies.

7. LOCUS OF OPERATIONS

Presumption that each participant would have responsability for its own market and would not be expected to intervene in another market, although it could do so after consultation.

8. COORDINATION

Central banks continue to maintain close contacts on intervention operations pursuant to established channels. Finance ministries intensify their bilateral channels of communication.

FINAL

STATEMENT

1. Ministers of Finance and Central Bank Governors of six major industrialized countries met today in Paris to conduct multilateral surveillance of their economies in the framework of the Tokyo Economic Declaration of May 6, 1986 pursuant to which the group of seven Finance Ministers was formed. 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. Their national 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 economies, and enhance the prospects of higher growth. Other important structural reforms are also being carried forward, 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 United States and the European Community on bilateral trade issues.

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 developing countries, especially debtor countries, to restore steady growth and viable balance of payments positions. They noted that the progress achieved by many debtor countries toward these ends have not solved all the problems and stressed the importance of all participants in the strengthened debt strategy reinforcing their cooperative efforts.

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.

The Government of Canada's policy is designed to sustain the current economic expansion through its fifth year and beyond. In the budget for 1987/88, the Government has cut the fiscal deficit for the third consecutive year and remains committed to further progressive reduction. Canada will propose shortly an extensive reform of its tax system. It will continue with its policies of regulatory reform, privatization and liberalization of domestic markets. It will vigorously pursue trade liberalization bilaterally with the United States and multilaterally within the Uruguay round. Monetary policies will continue to aim at the reduction of inflation and be consistent with orderly exchange markets.

The Government of France will reduce the central government budget deficit by 1 percent of GNP from 1986 to 1988 and in the same period will implement a tax cut program of the same order of magnitude (1 percent of GNP) with substantial tax rate cuts for corporations and individuals. It will pursue in 1987 its privatization program (with a projected $6 to $7 billions sale of assets) and reinforce the liberalization of the French economy, especially of labor and financial markets.

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. In addition, the Government will propose to increase the size of the tax reductions already enacted for 1988. The Federal Government will emphasize policies that enhance market forces in order to foster structural adjustment and innovation. Short-term interest rates, although already at a very low level in international comparison, have further dropped substantially during the last few weeks. 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 effort will be made to get the 1987 budget approved by the Diet so that its early implementation be ensured. A comprehensive economic program will be prepared after the approval of the 1987 budget by the Diet, so as to stimulate domestic demand, with the prevailing economic situation duly taken into account. The Bank of Japan announced that it will reduce its discount rate by one half percent on February 23.

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 low level. These and other measures to strengthen the supply performance of the economy, such as the privatization programme, will reinforce improvement over recent years in the growth of productivity.

The **United States** Government will pursue policies with a view to reducing the fiscal 1988 deficit to 2.3 % of GNP from its estimated level of 3.9 % in fiscal 1987. 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 consistent with economic expansion at a sustainable non-inflationary pace.

8. The Ministers and Governors noted that a number of newly industrialized economies were playing an increasingly important role in world trade. These economies have achieved strong 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 economies 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.

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

- periodically review medium-term economic objectives and projections involving domestic and external variables. The medium-term objectives and projections 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, the objectives and projections will involve the following key variables : growth, inflation, current accounts/trade balances, budget performance, monetary conditions and exchange rates.

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 exchange rate shifts among their currencies could damage growth and adjustment prospects in their countries. In current circumstances, therefore, they agreed to cooperate closely to foster stability of exchange rates around current levels.

Paris, February 22, 1987

000707 G10

TREASURER

PARLIAMENT HOUSE
CANBERRA 2600

4 August 1987

ORIG: TRE
CC: MD
DMD
~~MR. LANKESTER~~
MR. RYE
ASD
ETR
EUR
WHD
MR.R.BROWN

Mr Michel Camdessus
Managing Director
International Monetary Fund
WASHINGTON DC 20431
USA

Dear Mr Camdessus

I have today written to the Chairman of the Group of Ten to request that consideration be given to admitting Australia to the Group.

A copy of my letter to the G10 Chairman, which has also been sent to the Finance Minister of each G10 country, is attached for your information.

In the past, a concomitant of G10 membership has been participation in the General Arrangements to Borrow. Australia is prepared to fulfil its obligation in that respect and I should appreciate your support for Australia's request to be admitted as a GAB participant and a member of the G10.

With kind regards

Your sincerely

P.J. KEATING
Treasurer of the Commonwealth of Australia

GAB

4 August 1987

The Rt Hon Nigel Lawson, MP
Chancellor of the Exchequer
11 Downing Street
London SW1
United Kingdom

My dear Chancellor

I am writing to you in your capacity as Chairman of the G10.

As you know, Australia has expressed interest on several occasions in becoming a participant in the general arrangements to borrow and a member of the G10. I now do again, not only on the basis of the benefits which membership might brir to Australia but also to the group as a whole, having regard to the extent that Australia and the $A are now integrated into the international financial system.

When the G10 last considered the issue of an expansion of its membership, it decided to defer substantive consideration until the next review of the GAB, which is to take place shortly. Australia wishes to be considered in the context of those processes for inclusion as a participant in the GAB and a member of the G10. I believe that Australia has exceptionally strong claims to these positions, particularly given the major policy changes which have occurred since 1983 when the GAB were last reviewed. These policy actions have completely transformed Austrlia's financial system, and the way it interacts with the international financial system.

In the period since 1983 Australia has floated its exchange rate and abolished exchange controls on private transactions. Similarly, there are now no controls of any kind on interest rates on official paper and bank interest rates have been virtually deregulated. Australia's professional money markets and its foreign exchange markets are therefore fully functioning free markets and have deepened rapidly. Sixteen foreign banks have been permitted to establish subsidiaries in Australia and entry to the merchant banking sector derestricted. Restrictions on investments at interest in Australia by official foreign monetary institutions have been removed. Australia's foreign investment policy also has been liberalised substantially, so that there are now very few impediments to overseas investment in Australia.

As a result of these policy decisions, Australia now has one of the most open financial systems in the world. There are now very well-developed and efficient on-shore and off-shore foreign exchange markets for the Australian dollar, with significant trading on a 24 hour basis around the world. Other major currencies are actively traded in Australia.

The Australian foreign exchange market is now among the top six or seven in the world in terms of turnover, and the Australian dollar is estimated to be the sixth or seventh most traded currency. Australia's position in global time zones makes our market an important link between New York, Tokyo and London. Trading in the Australian market has become increasingly important to conditions in the major markets. The Australian dollar is currently among the top five currency denominations used in the Eurobond market. Commercial banks from G10 countries have established banking and/or merchant banking operations in Australia, and Australian banks have taken on an increasingly global orientation. Foreign central banks and international institutions have begun to include Australian dollars in their reserve holdings. Such $A holdings presently total $US1.5 billion and have been growing quickly since the removal of restrictions on such investments.

Australian dollars

In short, Australia is now fully integrated into the international financial system and the Australian dollar has assumed an important international role. As a result, developments in Australian financial markets, together with Australian government policy attitudes, are of increased relevance to G10 countries. In these respects, in particular, I believe that Australia's claims to membership of the G10 surpass those of any other prospective members.

Another important consideration, in my view, is the fact that Australia has much in common with G10 countries in terms of its approach to economic policy. In policy terms we have seen responsible domestic economic management aimed at containing inflation and structural adjustment as being essential to sustaining acceptable rates of growth in output and employment in the longer run.

Australia has always taken a detailed and responsible interest in international monetary and financial matters. This is reflected in our active role in the IMF and IBRD, where we lead substantial constituencies. It also explains our keenness to be able to participate in G10 discussions on these matters.

The Australian economy is larger than those of four countries which are presently G10 members. Based on OECD GDP data, Australia is the ninth largest OECD economy. I also observe that the present G10 membership has a very limited non-atlantic representation. Australia, while very much identifying with the industrial countries, would be able to increase the group's awareness of relevant developments in the dynamic Asian Pacific region.

You have my assurance that the Australian government is prepared to provide a GAB credit line to the IMF that is fully in accordance with the relative size of the Australian economy and Australia's external position. We are also ready to provide the necessary high level representation to enable us to play a responsible role in the G10. In the light of these assurances and the developments outlined in this letter, I should be most grateful if you and the other G10 Finance

Ministers would give favourable consideration to the Australian government's request to be included as a participant in the GAB and a member of the G10. With a view to facilitating consideration of that request, I am forwarding a copy of this letter to the Finance Minister of each of the G10 countries.

Kind regards.

Yours sincerely,

P.J. KEATING
Treasurer of the Commonwealth of Australia

August 28, 1987
(Revised September 3, 1987)

Economic Prospects and Policies in the Major Industrial Countries

Note by the Fund Staff

The attached tables A to D bring together information submitted by the major industrial countries for key economic variables for the period 1987-90. (For convenience, Tables AA to DD provide the corresponding estimates from the Fund staff's World Economic Outlook.) Tables E and F provide historical data for interest rates and exchange rates. The following notes are based on data submitted by national authorities. In some cases, especially where national authorities' data are not available, Fund staff estimates are employed.

I. Main Features of the Indicators

(a) Growth of output and demand

GNP growth is projected to continue at a moderate pace in 1988 and beyond in all seven major industrial countries. Domestic demand is expected to grow rather faster than final output in Europe and Japan, and more slowly in North America. The average rate of growth of GNP for the seven countries as a group is somewhat higher in national authorities' projections than in those made by the Fund staff. National authorities' estimates are for aggregate GNP growth in the seven countries, taken together, of about 3 1/4 percent from 1988 onwards. Fund staff estimates put the average growth rate at about 2 3/4 percent, which would probably not be sufficient to bring about a significant easing in either the unemployment problem or in the international debt situation.

(b) Unemployment

Unemployment rates in all the major countries are expected to remain close to recent levels. Some increase is expected in France and Italy, and some decline in the other countries in the group. Only in the United States would the projected decline, to under 5 1/2 percent in 1990, imply labor market tightness.

(c) Inflation

No major change from current inflation rates is expected. Underlying rates of price increase are expected to settle in the 1-2 percent range in Japan; 2-3 percent in France and Germany; and 3-4 percent in the other countries.

(d) Trade and current account balances

Significant adjustments in real trade balances are under way, partly masked by terms of trade factors. By 1990, the adjustments to recent exchange rate changes should largely have been felt. In that year the U.S. current account deficit is projected by the U.S. authorities to fall to around 2 percent of GNP. The German authorities' figure for their surplus would be around 1 1/2 percent of GNP; no official estimate is available for Japan. According to Fund staff estimates, the imbalances for Germany and the U.S. would be somewhat greater than in the national projections or objectives. Fund staff estimates put the Japanese surplus at 2 3/4 percent of GNP in 1990.

(e) Fiscal positions

The U.S. authorities expect further reductions in the federal fiscal deficit, bringing it to about 1.5 percent of GNP in 1990. A continued strengthening in the fiscal position is also forecast by Canada, France, and Italy. Little change is expected in the budgetary position for the U.K., and a slight increase in the deficit is foreseen for Germany. In Japan, a slight increase in the deficit is expected in FY 1987, as a result of the supplementary budget. Fund staff estimates for the United States, which are based on current services and therefore do not take account of possible deficit-cutting measures, put the federal deficit at 3-3 1/2 percent of GNP in 1990. Staff projections of the fiscal deficit in other countries also tend to be somewhat higher than in the figures submitted by the authorities.

(f) Monetary conditions

Stable or declining monetary growth rates are projected in those countries that have made such projections (Canada, U.S., U.K.). In those countries that have supplied assumptions or projections for interest rates (Canada, France, U.S.) a moderate downward movement is expected over the period to 1990.

II. Implications for Other Countries

The rate of growth of output and demand being projected by the large industrial countries implies a modest acceleration in growth from the pace achieved in 1985-87. This should be favorable for countries outside the G-7. The projections or assumptions for current account balances of the G-7 countries in 1990 are incomplete; therefore no clear implications emerge for the rest of the world. The combined current account of the four countries that have submitted data for 1990 (Canada, U.S., Germany, and France) shows a strengthening of some $25-30 billion over the expected position in 1987. Assuming that a part of this would be offset by a reduction in the surplus of Japan, the implied weakening in the aggregate payments position of the rest of the world would be relatively moderate.

The lower interest rates assumed on U.S. dollar instruments would, if they materialized, facilitate the task of servicing external debt. However, questions could be raised about the likelihood of the assumed decline in interest rates, especially if economic growth in the United States were, as officially projected, to exceed the growth of productive potential. Moreover, the persistence of large current account imbalances carry risks for interest rates and activity levels. If the persistence of financial imbalances led, directly or indirectly, to higher interest rates and an interruption of the present expansion, the consequences for indebted countries could be severe.

III. "Tensions" and Policy Issues

As just noted, a central source of uncertainty in the projections is the expected continuation of large payments imbalances among the three largest industrial countries. The imbalances are, if anything, somewhat larger in the staff's estimates than in those of the authorities. Since there is agreement that such imbalances cannot be considered sustainable in the medium and longer term, a series of inter-related policy questions arises:

(i) How much can differential rates of domestic demand growth contribute to the process of adjustment? Is the pace of domestic demand and GDP growth projected in individual countries appropriate to facilitate the required adjustment in the external accounts? In the United States, domestic demand growth is expected to accelerate gradually to 3 percent in 1990 with GDP growth being maintained at about 3 1/2 percent. In Germany, the medium-term rate of growth of domestic demand is also 3 percent. No official estimate is available for Japan, but the Fund staff projection is for domestic demand growth of 4 1/2 percent.

(ii) Since monetary policy will have to be directed at sustaining the progress that has been made in curbing inflation and inflationary expectations, what are the roles of fiscal policies and structural measures in achieving the desired rate of growth of domestic demand? What specific budgetary actions can be envisaged that would be consistent with the medium-term fiscal strategy and would also contribute to the desired redistribution of demand growth in the major countries? And what kind of structural policies are presently contemplated that would strengthen competitiveness in the United States and increase absorption relative to output in surplus countries?

(iii) In designing a policy strategy to facilitate adjustment, how can account be taken of the need to maintain an adequate flow of resources to capital-importing countries?

(iv) Finally, and despite the increased stability of exchange rates over the past six months, there is the question of whether feasible adjustments in the pace of domestic demand and GNP growth inthe major countries will reduce payments imbalances sufficiently to achieve a sustainable outcome. To the extent they cannot, further downward pressure on the dollar would be likely to develop at some stage, and the issue of how to respond to such pressure would arise. What would be the relative advantages of yielding to such pressure and resisting it from the viewpoint of the effective working of the international monetary system. If it were felt desirable to offer resistance to exchange market pressures, how could this be achieved?

NATIONAL AUTHORITIES DATA

6

DATE :SEPTEMBER 2, 1987

A. OUTPUT AND EMPLOYMENT
(CHANGES, IN PERCENT, EXCEPT IF OTHERWISE NOTED)

	1987	1988	1989	1990
REAL GNP/GDP				
CANADA	2.8	3.0	3.3	2.8
UNITED STATES	2.6	3.3	3.4	3.4
JAPAN	3.5	...	...	...
GERMANY, FED. REP. OF	2.5	2.5	2.5	2.5
FRANCE	1.5	2.2	2.3	2.7
ITALY	3.0	2.5	...	...
UNITED KINGDOM	3.0	2.5	2.5	2.5
OTHER INDUSTRIAL COUNTRIES	2.0	1.8	...	...
DEVELOPING COUNTRIES	3.3	4.3	...	...
REAL TOTAL DOMESTIC DEMAND				
CANADA	2.0	2.8	3.4	2.6
UNITED STATES	2.0	2.4	2.8	3.0
JAPAN	4.1	...	...	...
GERMANY, FED. REP. OF	3.0	3.5	3.0	3.0
FRANCE	2.4	1.9	2.6	3.0
ITALY	4.1	3.1	...	...
UNITED KINGDOM	3.5	2.5	...	...
OTHER INDUSTRIAL COUNTRIES	2.2	1.8	...	...
DEVELOPING COUNTRIES	2.2	3.3	...	...
GROWTH OF EMPLOYMENT				
CANADA	2.3	2.1	2.3	2.3
UNITED STATES	...	...	...	...
JAPAN	1.5	...	...	...
GERMANY, FED. REP. OF	1.0	1.0	1.0	1.0
FRANCE	...	...	...	...
ITALY	0.8	0.9	...	...
UNITED KINGDOM	...	...	...	...
UNEMPLOYMENT RATE (IN PERCENT)				
CANADA	9.3	9.0	8.6	8.2
UNITED STATES	6.2	5.9	5.6	5.4
JAPAN	2.9	...	...	...
GERMANY, FED. REP. OF	...	...	...	...
FRANCE	...	...	...	...
ITALY	11.6	11.8	...	...
UNITED KINGDOM	...	...	...	...

NOTE: THE ESTIMATES SHOWN HERE REFLECT DIFFERING NATIONAL PRACTICES. FOR CHARACTERIZATIONS OF NATIONAL ESTIMATES, SEE THE ATTACHED GENERAL AND TABLE-SPECIFIC NOTES. THE SAME DEGREE OF PRECISION IS APPLIED FOR ALL COUNTRIES SOLELY AS A MATTER OF CONVENIENCE. IT IS NOT INTENDED TO CONVEY ANY CONNOTATION REGARDING THE DEGREE OF ACCURACY ATTACHING TO THESE ESTIMATES AND PROJECTIONS.

NATIONAL AUTHORITIES DATA

DATE :SEPTEMBER 2, 1987

B. INFLATION
(CHANGES, IN PERCENT)

	1987	1988	1989	1990
GNP/GDP DEFLATOR				
CANADA	3.5	3.7	3.3	3.0
UNITED STATES	4.2	4.0	3.8	3.5
JAPAN	1.1	...	...	...
GERMANY, FED. REP. OF	2.0	2.0	2.0	2.0
FRANCE	3.3	2.5	2.5	2.5
ITALY	5.3	4.8	...	...
UNITED KINGDOM	4.0	4.0	3.5	3.0
CONSUMER PRICES				
CANADA	3.9	3.8	3.0	2.9
UNITED STATES	...	...	...	...
JAPAN	1.6	...	...	...
GERMANY, FED. REP. OF	...	...	...	...
FRANCE	3.3	2.5	2.5	2.5
ITALY	4.7	5.0	...	...
UNITED KINGDOM	4.0	4.0	...	...

NOTE: THE ESTIMATES SHOWN HERE REFLECT DIFFERING NATIONAL PRACTICES. FOR CHARACTERIZATIONS OF NATIONAL ESTIMATES, SEE THE ATTACHED GENERAL AND TABLE-SPECIFIC NOTES. THE SAME DEGREE OF PRECISION IS APPLIED FOR ALL COUNTRIES SOLELY AS A MATTER OF CONVENIENCE. IT IS NOT INTENDED TO CONVEY ANY CONNOTATION REGARDING THE DEGREE OF ACCURACY ATTACHING TO THESE ESTIMATES AND PROJECTIONS.

NATIONAL AUTHORITIES DATA

NATIONAL AUTHORITIES DATA

C. TRADE AND CURRENT ACCOUNT BALANCES

DATE :SEPTEMBER 2, 1987

7

	1987	1988	1989	1990
CURRENT ACCOUNT (IN BILLIONS OF U.S. DOLLARS)				
CANADA	-6	-6	-6	-5
UNITED STATES	-154	-144	-110 TO -125	-100 TO -115
JAPAN	77	...	...	...
GERMANY, FED. REP. OF	40	30	25	20
FRANCE	-1	—	—	—
ITALY	2	-1	...	...
UNITED KINGDOM	-4	-2	...	...
OTHER INDUSTRIAL COUNTRIES	-2	—	...	...
DEVELOPING COUNTRIES	-22	-16	...	...
CURRENT ACCOUNT (IN PERCENT OF GNP/GDP)				
CANADA	-1.4	-1.4	-1.3	-1.0
UNITED STATES	-3.4	-3.0	-2.1 TO -2.4	-1.8 TO -2.1
JAPAN	3.6	...	...	...
GERMANY, FED. REP. OF	3.5	2.5	2.0	1.5
FRANCE	-0.1	—	—	—
ITALY	0.3	-0.1	...	...
UNITED KINGDOM	-0.6	-0.3	...	...
OTHER INDUSTRIAL COUNTRIES	-0.1	—	...	...
DEVELOPING COUNTRIES	-0.7	-0.5	...	...
TRADE BALANCE (FOB/FOB)(IN BILLIONS OF U.S. DOLLARS)				
CANADA	10	10	12	13
UNITED STATES	...	...	...	...
JAPAN	81	...	...	...
GERMANY, FED. REP. OF	57	54	51	47
FRANCE	-5	-4	-4	-4
ITALY	—	-3	...	...
UNITED KINGDOM	...	...	...	...
OTHER INDUSTRIAL COUNTRIES	-7	-9	...	...
DEVELOPING COUNTRIES	30	41	...	...
TRADE BALANCE (IN PERCENT OF GNP/GDP)				
CANADA	2.4	2.4	2.6	2.8
UNITED STATES	...	...	...	...
JAPAN	3.8	...	...	...
GERMANY, FED. REP. OF	5.0	4.5	4.0	3.5
FRANCE	-0.6	-0.5	-0.5	-0.5
ITALY	—	-0.4	...	...
UNITED KINGDOM	...	...	...	...
OTHER INDUSTRIAL COUNTRIES	-0.4	-0.5	...	...
DEVELOPING COUNTRIES	1.0	1.2	...	...

NOTE: THE ESTIMATES SHOWN HERE REFLECT DIFFERING NATIONAL PRACTICES. FOR CHARACTERIZATIONS OF NATIONAL ESTIMATES, SEE THE ATTACHED GENERAL AND TABLE-SPECIFIC NOTES. THE SAME DEGREE OF PRECISION IS APPLIED FOR ALL COUNTRIES SOLELY AS A MATTER OF CONVENIENCE. IT IS NOT INTENDED TO CONVEY ANY CONNOTATION REGARDING THE DEGREE OF ACCURACY ATTACHING TO THESE ESTIMATES AND PROJECTIONS.

NATIONAL AUTHORITIES DATA

NATIONAL AUTHORITIES DATA

DATE :SEPTEMBER 2, 1987

8

D. FISCAL BALANCES AND MONETARY CONDITIONS
(IN PERCENT OF GNP/GDP, EXCEPT IF OTHERWISE NOTED)

	1987	1988	1989	1990
CENTRAL GOVERNMENT BALANCE				
CANADA	-4.8	-3.5	-3.7	-2.7
UNITED STATES	-3.6	-2.6	-2.2	-1.5
JAPAN	-3.4	...	...	...
GERMANY, FED. REP. OF	...	...	...	...
FRANCE	-2.5	-2.1	-1.7	-1.4
ITALY	-11.0	-11.1	...	...
UNITED KINGDOM	...	...	...	...
GENERAL GOVERNMENT BALANCE				
CANADA	...	...	...	...
UNITED STATES	-2.6	-1.7	-1.2	-0.2
JAPAN	...	...	...	...
GERMANY, FED. REP. OF	-2.4	-2.6	-2.7	-2.8
FRANCE	-2.8	-2.3	-1.9	-1.6
ITALY	...	...	...	...
UNITED KINGDOM	-1.0	-1.0	-1.0	-1.0
MONETARY CONDITIONS				
MONETARY GROWTH RATES: TARGET OR FORECASTED AGGREGATE (IN PERCENT)				
CANADA (M1)	11.0	7.0	6.2	6.1
UNITED STATES (M2)	5.5 TO 8.5	5 TO 8	...	...
JAPAN (M2+CD)	...	...	...	...
GERMANY, FED. REP. OF	...	...	...	...
FRANCE	...	...	...	...
ITALY (M2)	6 TO 9	...	...	...
UNITED KINGDOM (M0)	2 TO 6	1 TO 5	1 TO 5	0 TO 4
SHORT-TERM INTEREST RATE				
CANADA	7.8	7.6	7.7	7.3
UNITED STATES	5.7	5.5	5.3	5.0
JAPAN	...	...	...	...
GERMANY, FED. REP. OF	...	...	...	...
FRANCE	7.8	6.3	6.0	5.5
ITALY	...	...	...	...
UNITED KINGDOM	...	...	...	...
LONG-TERM INTEREST RATE				
CANADA	10.6	9.4	8.7	8.5
UNITED STATES	8.0	7.6	7.0	6.3
JAPAN	...	...	...	...
GERMANY, FED. REP. OF	...	...	...	...
FRANCE	9.0	8.0	7.5	7.0
ITALY	...	...	...	...
UNITED KINGDOM	...	...	...	...

NOTE: THE ESTIMATES SHOWN HERE REFLECT DIFFERING NATIONAL PRACTICES. FOR CHARACTERIZATIONS OF NATIONAL ESTIMATES, SEE THE ATTACHED GENERAL AND TABLE-SPECIFIC NOTES. THE SAME DEGREE OF PRECISION IS APPLIED FOR ALL COUNTRIES SOLELY AS A MATTER OF CONVENIENCE. IT IS NOT INTENDED TO CONVEY ANY CONNOTATION REGARDING THE DEGREE OF ACCURACY ATTACHING TO THESE ESTIMATES AND PROJECTIONS.

DATE :SEPTEMBER 2, 1987

(9)

TABLE E. MAJOR INDUSTRIAL COUNTRIES: NOMINAL AND REAL SHORT-TERM INTEREST RATES 1/
(IN PERCENT)

	1984	1985	1986	1987 JAN.	FEB.	MAR.	APR.	MAY	JUNE	JULY	AUG. 25
NOMINAL RATES											
CANADA	11.3	9.6	9.2	8.0	7.4	7.1	7.6	8.2	8.4	8.6	8.9
UNITED STATES	10.4	8.0	6.5	5.9	6.1	6.2	6.5	7.0	6.9	6.7	6.7
JAPAN	6.3	6.7	5.1	4.3	4.2	3.9	3.9	3.8	3.7	3.6	3.7
GERMANY, FED. REP. OF	6.0	5.4	4.6	4.4	3.9	4.0	3.9	3.7	3.7	3.8	3.9
FRANCE	11.7	9.9	7.7	8.5	8.4	7.9	7.9	8.1	8.2	7.8	7.9
ITALY	17.1	14.9	12.6	11.4	11.1	10.7	10.0	10.2	10.7	10.9	12.5
UNITED KINGDOM	9.9	12.2	10.9	11.0	10.8	9.9	9.7	8.8	8.8	9.2	10.3
REAL RATES 2/											
CANADA	7.3	5.4	4.4	3.1	2.6	2.2	2.6	3.2	3.3	3.5	3.8
UNITED STATES	7.1	5.4	3.8	2.2	2.3	2.4	2.8	3.4	3.4	3.1	3.2
JAPAN	4.5	6.2	5.1	3.2	3.0	2.6	2.5	2.2	2.1	2.0	2.1
GERMANY, FED. REP. OF	3.7	4.8	4.2	3.2	2.4	2.2	2.0	1.7	1.5	1.6	1.7
FRANCE	5.5	5.4	3.6	4.6	4.6	4.1	4.1	4.3	4.4	4.0	4.1
ITALY	7.5	6.7	7.5	5.8	5.5	5.1	4.5	4.6	5.1	5.4	6.9
UNITED KINGDOM	4.2	6.8	6.7	6.7	6.5	5.6	5.4	4.5	4.6	4.9	6.1

1/ INTEREST RATES ON THE FOLLOWING INSTRUMENTS: CANADA, THREE-MONTH FINANCIAL PAPER; UNITED STATE, 90-DAY BANK CERTIFICATES DEPOSIT IN SECONDARY MARKET; JAPAN, DISCOUNT RATE ON TWO-MONTH PRIVATE BILLS; FRANCE, THE FEDERAL REPUBLIC OF GERMANY, ITALY, AND THE UNITED KINGDOM, THREE-MONTH INTERBANK LOAN RATE.

2/ SHORT-TERM INTEREST RATES DEFLATED BY AN AVERAGE OF THE INCREASE IN THE PRIVATE FINAL DOMESTIC DEMAND DEFLATOR IN THE CURRENT AND THE FOLLOWING TWO QUARTERS; FOR THE MOST RECENT PERIOD, STAFF PROJECTIONS OF THE DEFLATOR ARE USED.

DATE :SEPTEMBER 2, 1987

(13)

TABLE F. MAJOR INDUSTRIAL COUNTRIES: SPOT EXCHANGE RATES, AND NOMINAL AND REAL EFFECTIVE EXCHANGE RATES

	1980	1985	1986	1985	1987					
				Q1	FEB. 20 1/	APR.	MAY	JUNE	JULY	AUG. 25
SPOT EXCHANGE RATES (CURRENCY UNITS PER U.S. DOLLAR EXCEPT AS NOTED)										
CANADA	1.17	1.37	1.39	1.35	1.33	1.32	1.34	1.34	1.33	1.32
JAPAN	227	239	169	258	154	143	141	144	150	143
GERMANY, FED. REP. OF	1.82	2.94	2.17	3.26	1.83	1.81	1.79	1.82	1.85	1.82
FRANCE	4.23	8.99	6.93	9.96	6.10	6.03	5.97	6.08	6.15	6.09
ITALY	856	1909	1491	2021	1303	1292	1291	1316	1337	1318
UNITED KINGDOM (US$/POUND)	2.33	1.30	1.47	1.12	1.53	1.63	1.67	1.63	1.61	1.62
EFFECTIVE EXCHANGE RATES (INDICES, 1974-85=100)										
IN REAL TERMS 2/										
CANADA	91.3	97.9	90.0	101.6	92.0	91.6	89.6	90.3	91.8	91.6
UNITED STATES	85.6	124.8	100.0	134.0	90.1	87.1	86.3	87.9	89.4	87.8
JAPAN	93.1	93.3	113.4	92.6	113.0	119.7	120.2	117.4	113.2	118.2
GERMANY, FED. REP. OF	105.1	93.4	102.7	91.6	109.1	108.0	108.8	109.3	109.4	109.3
FRANCE	104.7	95.9	97.8	94.0	98.1	97.2	96.9	96.5	96.6	96.3
ITALY	97.1	101.3	102.2	104.1	106.7	105.7	104.8	104.8	104.1	104.1
UNITED KINGDOM	114.4	110.5	104.5	101.8	101.2	106.4	108.1	107.6	108.0	107.3
IN NOMINAL TERMS 3/										
CANADA	92.5	95.0	85.6	98.5	86.2	85.8	84.0	84.7	86.1	85.9
UNITED STATES	85.0	127.6	104.1	135.9	94.5	91.6	90.9	92.3	93.6	92.0
JAPAN	92.9	118.1	149.7	113.5	153.8	163.8	165.7	162.4	157.2	164.2
GERMANY, FED. REP. OF	108.1	103.7	115.0	100.1	124.1	122.8	123.4	123.1	122.8	122.8
FRANCE	112.3	79.0	83.8	75.7	86.4	85.7	85.8	85.5	85.6	85.3
ITALY	100.2	67.2	69.7	68.4	72.3	71.3	70.6	70.3	70.2	70.2
UNITED KINGDOM	109.7	89.3	83.2	82.3	79.0	82.6	83.8	83.0	83.1	82.6

1/ RATES PREVAILING PRIOR TO THE PARIS MEETING.
2/ BASED ON THE FUND'S CALCULATIONS OF RELATIVE NORMALIZED UNIT LABOR COSTS IN MANUFACTURING ADJUSTED FOR EXCHANGE RATE CHANGES, USING THE WEIGHTING SCHEME DESCRIBED IN WP/87/34.
3/ BASED ON THE FUND'S MERM CALCULATIONS.

IMF STAFF ESTIMATES

DATE : SEPTEMBER 2, 1987

11

AA. OUTPUT AND EMPLOYMENT
(CHANGES, IN PERCENT, EXCEPT IF OTHERWISE NOTED)

	1987	1988	1989	1990
REAL GNP/GDP				
CANADA	2.8	2.9	3.0	3.0
UNITED STATES	2.4	2.7	2.9	2.9
JAPAN	3.2	3.4	3.5	3.5
GERMANY, FED. REP. OF	1.5	2.3	2.1	2.6
FRANCE	1.5	1.8	2.7	2.7
ITALY	2.5	2.4	2.5	2.5
UNITED KINGDOM	3.3	2.2	2.3	2.3
MAJOR INDUSTRIAL COUNTRIES	2.5	2.7	2.9	2.9
OTHER INDUSTRIAL COUNTRIES	2.0	1.8	...	...
DEVELOPING COUNTRIES	3.3	4.3	...	...
REAL TOTAL DOMESTIC DEMAND				
CANADA	2.8	2.9	2.8	2.8
UNITED STATES	1.7	1.9	2.8	2.8
JAPAN	4.0	4.4	4.4	4.4
GERMANY, FED. REP. OF	2.9	2.9	2.2	2.9
FRANCE	2.3	2.1	2.9	2.9
ITALY	3.8	2.9	2.8	3.0
UNITED KINGDOM	3.7	2.9	2.5	2.5
MAJOR INDUSTRIAL COUNTRIES	2.6	2.7	3.1	3.2
OTHER INDUSTRIAL COUNTRIES	2.2	1.8	...	...
DEVELOPING COUNTRIES	2.2	3.3	...	...
GROWTH OF EMPLOYMENT				
CANADA	2.6	2.6	...	...
UNITED STATES	2.5	1.8	...	...
JAPAN	0.7	1.0	...	...
GERMANY, FED. REP. OF	0.5	0.8	...	...
FRANCE	-0.7	0.6	...	...
ITALY	0.6	0.5	0.5	0.5
UNITED KINGDOM	0.8	0.7	...	...
MAJOR INDUSTRIAL COUNTRIES	1.4	1.3	...	...
UNEMPLOYMENT RATE (IN PERCENT)				
CANADA	9.1	8.6	8.5	8.4
UNITED STATES	6.4	6.1	6.0	6.0
JAPAN	3.0	3.0	2.9	2.8
GERMANY, FED. REP. OF	7.9	7.7	7.2	6.6
FRANCE	11.5	11.5	12.8	12.8
ITALY	11.5	11.8	12.1	12.3
UNITED KINGDOM	10.6	10.2	10.0	9.9
MAJOR INDUSTRIAL COUNTRIES	7.0	6.9	6.9	6.8

GENERAL NOTE: THE PROJECTIONS IN THIS AND THE FOLLOWING TABLES ARE THOSE OF THE FUND STAFF ELABORATED IN THE CONTEXT OF THE WORLD ECONOMIC OUTLOOK. THE PROJECTIONS WERE FINALIZED AS OF END-AUGUST, 1987 AND REFLECT THE FOLLOWING WORKING ASSUMPTIONS: OIL PRICES ARE ASSUMED TO AVERAGE $17 PER BARREL IN 1987 AND $17.60 IN 1988; EXCHANGE RATES ARE ASSUMED TO REMAIN UNCHANGED IN REAL TERMS FROM THE LEVEL PREVAILING IN MAY 1987; "PRESENT" ECONOMIC POLICIES OF THE NATIONAL AUTHORITIES ARE ASSUMED TO BE MAINTAINED.

IMF STAFF ESTIMATES

DATE :SEPTEMBER 2, 1987

12

BB. INFLATION
(CHANGES, IN PERCENT)

	1987	1988	1989	1990
GNP/GDP DEFLATOR				
CANADA	4.2	3.5	3.3	3.3
UNITED STATES	3.3	3.8	3.6	3.4
JAPAN	0.6	1.7	1.5	1.5
GERMANY, FED. REP. OF	2.4	2.2	2.5	2.5
FRANCE	3.4	3.0	2.5	2.5
ITALY	5.3	5.3	5.0	4.5
UNITED KINGDOM	4.5	4.8	4.2	4.0
MAJOR INDUSTRIAL COUNTRIES	2.9	3.3	3.1	2.9
CONSUMER PRICES				
CANADA	4.3	3.7	...	...
UNITED STATES	3.7	4.1	...	...
JAPAN	0.3	1.6	...	...
GERMANY, FED. REP. OF	0.7	2.6	...	...
FRANCE	3.3	3.0	...	...
ITALY	4.5	4.9	...	...
UNITED KINGDOM	4.2	4.5	...	...
MAJOR INDUSTRIAL COUNTRIES	2.9	3.4	...	...

IMF STA[illegible]ESTIMATES

DATE :SEPTEMBER 2, 1987

(13)

CC. TRADE AND CURRENT ACCOUNT BALANCES

	1987	1988	1989	1990
CURRENT ACCOUNT (IN BILLIONS OF U.S. DOLLARS)				
CANADA	-7	-8	-8	-8
UNITED STATES	-148	-139	-142	-146
JAPAN	85	83	86	86
GERMANY, FED. REP. OF	39	30	30	28
FRANCE	2	—	—	1
ITALY	-1	-3	-4	-6
UNITED KINGDOM	-2	-4	-3	-3
MAJOR INDUSTRIAL COUNTRIES	-31	-41	-41	-49
OTHER INDUSTRIAL COUNTRIES	-2	—	...	...
DEVELOPING COUNTRIES	-22	-16	...	...

	1987	1988	1989	1990
CURRENT ACCOUNT (IN PERCENT OF GNP/GDP)				
CANADA	-1.8	-2.0	-1.8	-1.7
UNITED STATES	-3.3	-2.9	-2.8	-2.7
JAPAN	3.6	3.2	3.0	2.8
GERMANY, FED. REP. OF	3.5	2.5	2.4	2.1
FRANCE	0.3	—	—	0.1
ITALY	-0.1	-0.3	-0.4	-0.5
UNITED KINGDOM	-0.3	-0.6	-0.4	-0.4
MAJOR INDUSTRIAL COUNTRIES	-0.3	-0.4	-0.3	-0.4
OTHER INDUSTRIAL COUNTRIES	-0.1	—	...	...
DEVELOPING COUNTRIES	-0.7	-0.5	...	...

	1987	1988	1989	1990
TRADE BALANCE (FOB/FOB)(IN BILLIONS OF U.S. DOLLARS)				
CANADA	9	9	...	...
UNITED STATES	-150	-136	...	...
JAPAN	91	87	...	...
GERMANY, FED. REP. OF	63	58	...	...
FRANCE	-5	-7	...	...
ITALY	-2	-4	-6	-8
UNITED KINGDOM	-15	-19	...	...
MAJOR INDUSTRIAL COUNTRIES	-9	-12	...	...
OTHER INDUSTRIAL COUNTRIES	-7	-9	...	...
DEVELOPING COUNTRIES	30	41	...	...

	1987	1988	1989	1990
TRADE BALANCE (IN PERCENT OF GNP/GDP)				
CANADA	2.1	2.1	...	...
UNITED STATES	-3.3	-2.8	...	...
JAPAN	3.8	3.3	...	...
GERMANY, FED. REP. OF	5.6	4.8	...	...
FRANCE	-0.6	-0.8	...	...
ITALY	-0.3	-0.5	-0.7	-0.8
UNITED KINGDOM	-2.3	-2.6	...	...
MAJOR INDUSTRIAL COUNTRIES	-0.1	-0.1	...	...
OTHER INDUSTRIAL COUNTRIES	-0.4	-0.5	...	...
DEVELOPING COUNTRIES	1.0	1.2	...	...

IMF STAFF ESTIMATES

DATE :SEPTEMBER 2, 1987

14

DD. FISCAL BALANCES AND MONETARY CONDITIONS
(IN PERCENT OF GNP/GDP, EXCEPT IF OTHERWISE NOTED)

	1987	1988	1989	1990
CENTRAL GOVERNMENT BALANCE 1/				
CANADA	-4.3	-3.9	...	...
UNITED STATES	-3.7	-3.7	...	...
JAPAN	-4.1	-4.6	...	...
GERMANY, FED. REP. OF	-1.3	-1.5	...	...
FRANCE	-2.5	-2.1	...	...
ITALY	-11.3	-10.8	...	...
UNITED KINGDOM	-2.2	-2.1	...	...
MAJOR INDUSTRIAL COUNTRIES	-3.9	-3.9	...	...
GENERAL GOVERNMENT BALANCE 2/				
CANADA	-4.6	-4.2	-3.8	-3.4
UNITED STATES	-2.3	-2.4	-2.2	-2.0
JAPAN	-1.2	-1.6	-1.6	-1.5
GERMANY, FED. REP. OF	-2.4	-2.9	-3.0	-3.6
FRANCE	-2.6	-2.1	-2.1	-2.0
ITALY	-10.3	-9.9	-9.2	-8.7
UNITED KINGDOM	-2.6	-2.5	-2.4	-2.2
MAJOR INDUSTRIAL COUNTRIES	-2.7	-2.8	-2.7	-2.6
MONETARY CONDITIONS				
MONETARY GROWTH RATES: TARGET OR FORECASTED AGGREGATE (IN PERCENT) 3/				
CANADA (M2)	...	...	...	...
UNITED STATES (M2)	6.4	6.0	...	...
JAPAN (M2+CD)	9.0	8.0	...	...
GERMANY, FED. REP. OF (CBM)	7.0	4.5	...	...
FRANCE (M3)	5.0	5.0	...	...
ITALY (M2)	9.0	7.0	...	...
UNITED KINGDOM (M0)	4.9	4.5	...	...
MAJOR INDUSTRIAL COUNTRIES	...	...	...	...

1/ DATA FOR JAPAN INCLUDE THE SURPLUS OF THE SOCIAL SECURITY ACCOUNTS AND NET LENDING BY THE FISCAL INVESTMENT AND LOAN PROGRAM (FILP) TO NONFINANCIAL PUBLIC ENTITIES. DATA FOR FRANCE ARE ON AN ADMINISTRATIVE BASIS AND DO NOT INCLUDE SOCIAL SECURITY TRANSACTIONS. DATA FOR GERMANY ARE ON A MODIFIED ADMINISTRATIVE BASIS, WITH REVENUE FROM THE SALE OF GOVERNMENT ASSETS COUNTED AS A FINANCING ITEM, AND EXCLUDE THE SOCIAL SECURITY SYSTEM. DATA FOR ITALY ARE ON A CASH BASIS. DATA FOR OTHER COUNTRIES ARE ON A NATIONAL INCOME ACCOUNTS BASIS.
2/ FOR GERMANY, DATA ARE FOR THE TERRITORIAL AUTHORITIES. DATA FOR OTHER COUNTRIES ARE ON A NATIONAL INCOME ACCOUNTS BASIS.
3/ END OF PERIOD

15

(8)

Notes to Economic Indicator Tables

The estimates shown in the tables reflect a variety of national conventions, forecasting procedures, and working assumptions. To the extent permitted by authorities' responses, the following notes clarify the main differences in the various national estimates first by providing a general characterization of the national estimates and second by listing the table-specific differences.

1. General Features of National Estimates

Canada: the estimates are on a calendar year basis and were finalized in June 1987. The exchange rate is assumed to be virtually constant through to 1990 at about C$1.34 per US dollar. Oil prices are assumed to rise by 14 percent in US dollar term in 1987, remain constant in 1988, and rise by 6 and 8 percent in 1989 and 1990, respectively.

United States: in accordance with the Managing Director's request, the data formally submitted by the U.S. authorities cover the period 1988-90. In order to permit comparisons, consistent statistics are presented for 1987 based on the Administration's recently announced mid-session review forecasts. The estimates are on a year on year calendar basis (unless otherwise specified). The estimates for 1987 and 1988 are forecasts while those for 1989 and 1990 are "objectives". The current account projections assume current nominal exchange rates.

Japan: estimates pertain to the financial year ending March 31, 1988; they were finalized on January 26, 1987. The estimates assume a yen/US dollar rate of 163, the average rate prevailing in November 1986. The FY 1986 Revolving Report of the Economic Council (annual revolving report of the Outlook and Guideline for the Economy and Society in the 1980s' by the Economic Council completed in December 1986) provide certain average figures for FY 88, 89 and 90. This revolving report is expected to be revised at the end of 1987. See table-specific notes.

France: estimates for 1987 and 1988 are based on the "Summer Economic Budget". Data for 1989 and 1990 are preliminary technical projections drawn from the medium term scenario of the Planning Directorate. These figures are not official commitments of the government and are not in every case perfectly reconcilable with the data provided for 1988. All projections assume constant nominal exchange rates with EMS currencies, and a rate of 6 Francs per US dollar.

Germany: estimates for individual calendar years were provided by the authorities for the nominal and real current account (1987 and 1988) and the fiscal balance (1987-88, 1990). The estimate for the fiscal balance for 1989 is interpolated from the 1988 and 1990 data provided by the authorities. In all other cases the calendar year estimates are interpolations of the changes between 1986 and 1991, modified to take

(16)

into account the current account information provided for 1987 and 1988. Projections assume constant real exchange rates.

Italy: estimates are very preliminary and subject to possibly extensive revisions once the new government has determined its financial strategy (to be presented to Parliament by the end of September). Estimates are on a calendar year basis.

United Kingdom: estimates for 1987 and 1988 are generally on a calendar year basis while those for 1989 and 1990 are on a fiscal year (ending March 31 of the following calendar year) basis. Estimates are "consistent" with those provided in the Financial Statement and Budget Report for 1987-88 published on March 17, 1987 and in the current version of the Medium Term Financial Strategy.

Other Industrial Countries and Developing Countries: estimates are on a calendar year basis and from the World Economic Outlook (August 20, 1987). These assume that exchange rates will remain constant in real terms at the levels prevailing in May 1987 and that oil prices will remain constant in real terms at the level prevailing in the second quarter of 1987.

2. Table-Specific Notes

Table A--Output and Employment

Real GNP/GDP: estimates pertain to GNP for the United States, Japan, and Germany and to GDP for the other countries. In the Japanese "Revolving Report", the average growth rate per annum for the period FY 1988 to FY 1990 is put at 4 percent. According to the UK authorities, GDP growth in the United Kingdom in 1987 "seems likely to exceed the Budget forecast of 3 percent" (shown in the table).

Employment: estimates for Germany pertain to the "gainfully employed" and those for Italy to the number of "full-time equivalents".

Unemployment Rate: the Japanese "Revolving Report" has a benchmark objective for unemployment of 2 percent in FY 1990. The German authorities expect the unemployment rate in Germany to decline, but the amount is not specified.

Table B--Inflation

GNP/GDP deflator: estimates pertain to GNP for the United States, Japan, and Germany and to GDP for the other countries. Estimates for the United States are on a fourth quarter over fourth quarter basis.

Consumer Prices: for Japan, an average rate of consumer price inflation of 2 percent is projected for FY 1988-FY 1990; the corresponding average for the wholesale price index under 1 percent. Estimates for the United Kingdom are for the retail price index and

(17)

pertain to year on year rates of increase in Q4 1987 for 1987 and Q2 1988 for 1988.

Table C--Trade and Current Account Balances

General Note: estimates provided by national authorities in national currency or in percent of GNP/GDP have been converted into US dollar using nationally provided exchange rates when available (Canada and Japan) and WEO exchange rate assumptions otherwise.

Current Account: estimates, in percent of GDP, for Germany in 1989 and 1990 represent an interpolation of the authorities' estimate of a surplus equivalent to 1 percent of GDP in 1991.

Trade Balance: the estimates for Germany represent an interpolation based on current account estimates and the authorities estimate of a surplus equivalent to 3 percent of GDP in 1991 are on a national account basis.

Table D--Fiscal Balances and Monetary Conditions

Central Government Balances: estimates for the United States are on a fiscal year basis (ending September 30). The Japanese authorities continue to regard it as imperative that public finance try to free itself from dependence on deficit financing bonds by FY 1990 and to lower the overall dependency on government bond financing.

General Government Balance: estimates for Germany pertain to the accounts of the territorial authorities (i.e. which are on administrative bases and exclude social security). For the United Kingdom the data refer to the public sector borrowing requirement (PSBR), and are illustrative projections, not targets. Estimate for 1989 for Germany is interpolated from 1988 and 1990 estimates provided by the authorities.

Monetary Growth: estimates for Canada are forecasts rather than official targets; the Bank of Japan projects a growth rate of around 10 percent for quarter 3, 1987; the estimate for 1988 shown for the United States is on a fourth quarter over fourth quarter basis; for Italy official target range is reported. For the United Kingdom, figures for 1988 and beyond are not targets but illustrative paths.

Interest Rates: short-term interest rates on the following instruments: Canada, 90-day commercial paper rate; United States, 90-day T-bell rate; France, money market rate.

Long-term interest rates on the following instruments; Canada, McLeod Young Weir bond rate; United States, 10-year T-bond rate, France, first-class paper rate.

G7 Indicators

		3 month interest rate	Real	Inflation rate	SDR all items commodity prices
1981		14.1	4·2	9.9	95.1
1982		11.8	4·7	7.1	87.9
1983		9.2	4·6	4.6	102.7
1984		9.6	5·1	4.5	105.7
1985		8.5	4·6	3.9	95.8
1986		7.0	5·1	1.9	86.9
1987	Jan	6.6		1.3	80.3
	Feb	6.5		1.7	81.7
	Mar	6.4		2.2	82.9
	Apr	6.4		2.7	84.2
	May	6.6		2.7	87.3
	Jun	6.6		2.7	88.9
	Jul	6.5	3·7	2.8	90.7
	Aug	6.8		n/a	92.2
Latest		7.2 (22 Sept)		(July)	91.3 (15 Sept prov)

Ch
From Terry
AA

SW27

FROM: S W MATTHEWS
DATE: 3 September 1987

SIR GEOFFREY LITTLER

cc: PS/Chancellor
Sir P Middleton
Sir T Burns
Mr Cassell
Mr Evans
Mr Odling-Smee
Mr Peretz
Mr Sedgwick
Mr Savage

A/ No need to show to Ch, I think, but you may be interested to glance at this
25 7/9

G5/G7 DEPUTIES: IMF NOTE ON INDICATORS

This brief deals with the procedural issues of how the indicators in the IMF staff's note are to be used. It then comments on the forecasts themselves and offers some thoughts on their policy implications. (Copies of the IMF's note are attached for copy recipients who have not already seen it).

USE OF INDICATORS

(i) Background

2. Multilateral surveillance has so far tended to focus on forecasts/indicators of policies and prospects in the major countries, with a view to determining their international consistency and whether current policies risk producing an unsustainable situation in the medium term. More recently, there has been some shift of emphasis toward identifying a desirable outcome and using "performance indicators". You will recall that the Venice Declaration noted in particular:

a. "the commitment by each country to develop medium term objectives and projections for its economy, and for the group to identify objectives and projections, that are mutually consistent individually and collectively; and

b. the use of performance indicators to review and assess currency economic trends and determine whether there are significant deviations from an intended course that require consideration of remedial actions".

3. In their note the IMF staff present the national projections which they have collected, together with their own WEO projections. Their note offers no guidance, though, on how these are to be developed into a mutually consistent set of objectives and projections, or on how "performance indicators" should be determined.

4. The last IMF board discussion of indicators on 22 July made little progress on these questions and gave no clear steer to the staff. Most Directors restated their previous positions. Thus Germany, Japan and the UK stressed the importance of being pragmatic and avoiding automaticity or fine-tuning. France and Italy wanted a more active use of indicators (with greater emphasis on exchange rates) to set desired policy outcomes and to trigger multilateral discussions should performance fall short of these targets. The US took an intermediate position. In his summing up the Managing Director considered that the WEO should play a major role in the indicators exercise, and that his summing up of the WEO discussion should outline in a qualitative way the desired outcome favoured by the Board. Where deviations from this occurred he would draw them to the attention of the Board in an informal manner.

(ii) Points to make

5. You will presumably want at the G5/G7 Deputies meetings to support an informal and judgmental approach to indicators, and to argue against over-ambitious use of projections to set targets and against the use of performance indicators to trigger policy responses to deviations from them. The emphasis should continue to be on identifying policy unsustainability or inconsistency.

6. You could welcome the greater implicit weight now being given to the medium term by the staff extending their forecast forward by a couple of years. In particular, it helps to identify more clearly the potential unsustainability of some countries' current policies.

THE STATISTICAL MATERIAL

7. The national projections in tables A - D are a mixture of what the various Governments expect to happen and what they would like to happen. The dividing line between the positive and the normative is, however, virtually impossible to draw. The value of the figures as projections is in any case limited by the differences in underlying assumptions about oil and commodity prices, exchange rates, economic activity in the rest of the world, etc. There is no reason therefore to revise our view that Ministers and their Deputies should focus on a single set of numbers produced by the IMF staff.

8. The staff's estimates are consistent in that they have a single set of assumptions about exogenous variables. They are taken from the "Accommodating Finance Scenario" of the WEO. This assumes a continuation of current fiscal policies and that any domestic or external financial imbalances that arise from this are smoothly financed without any changes in interest rates or real exchange rates. This is almost certainly unrealistic but it provides a useful way of identifying possible inconsistencies or policy unsustainability. Such "tensions" over the medium term will be reflected in the figures for fiscal and current account imbalances, rather than the sort of sharp changes in financial markets that one is actually likely to see. With this in mind, we comment below on the main features of the projections for the three largest countries. The forecasts for real GNP growth and current account balances are summarised in table 1.

UNITED STATES

Policies

9. In the Louvre Agreement the United States said it would reduce the Federal deficit from an estimated 3.9 per cent of GNP in fiscal 1987 to 2.3 per cent (the Gramm-Rudman-Hollings target) in fiscal 1988. In the event, the deficit is likely to be a little lower than estimated for fiscal 1987 (at around 3.7 per cent), largely because of one-off receipts from tax reform. With existing tax rates and expenditure programmes, the Administration estimates that the deficit would decline only to 3.4 per cent in

FY88, and the IMF that it would remain unchanged at 3.7 per cent. The present stalemate between the Administration and Congress on the Federal Budget for FY88 gives little ground for hope that the deficit will be much below this.

Monetary policy and the exchange rate

10. The following table shows the lows and highs in the dollar (against the DM, the yen and in effective terms) since the Louvre Agreement, and short term interest rates in the United States. Table 2 and the attached chart show exchange rate developments this year in more detail. to follow.

	DM	Yen	Effective rate (1975=100)	US short term interest rates
20 February (Louvre)	1.828	153.6	104.0	6.2
6 May (low)	1.773	139.2	99.5	6.3
11 August (high)	1.896	151.8	105.1	6.4
2 September	1.803	141.0	100.5	7.0

11. US interest rates firmed in May and have recently risen again, as the dollar has come under renewed downward pressure.

Forecasts

12. The Administration's forecasts are extremely optimistic in every respect. Real GDP is expected to grow by almost 3½ per cent a year over the rest of the 1980s, compared with an average rate of 2½ per cent since 1979. The unemployment rate is expected to decline and at the same time inflation is expected to remain low. In fact the US economy is probably now close to full employment and further reductions in unemployment may mean an acceleration of inflation.

13. The IMF's projections are more plausible and show GDP growing broadly in line with an estimated growth rate of potential of $2^3/4$ per cent a year. With no changes in real exchange rates, interest rates, or fiscal policy little further decline is shown beyond next year in the US current account deficit. Such large deficits are almost certainly unsustainable in the medium term.

Policy implications

14. On present policies there are significant risks of substantial depreciation and/or rise in US interest rates some time before 1990. This leads to the familiar conclusion that cuts in the Federal budget deficit are needed in order to reduce the excess of US investment over saving. The projections indicate that tax increases and/or expenditure reductions are required: current policies will not by themselves deliver sufficient deficit reduction.

JAPAN

Policies

15. At the Louvre, the Government of Japan undertook 'to follow monetary and fiscal policies which will help to expand domestic demand and thereby contribute to reducing the external surplus'. The Y6 trillion package, first announced in April but not presented in detail until 29 May, was greeted with some scepticism. Though some doubts remain, the IMF staff have tentatively estimated that the package will raise Japanese GNP by ½ per cent this year and by 1 - 1½ per cent in 1988.

Forecasts

X 16. Japan provided fewer national figures than anyone else, giving only forecasts for the current year. These are a little more optimistic than the IMF forecasts and our own, both on output and on the balance of payments, but the differences are not particularly large.

17. The IMF's medium term projection of growth is broadly in line with potential, but they may be a bit optimistic about the rate of real domestic demand growth, given the assumption of no changes in policies or exchange rates. Even so, the Japanese current account surplus shows little decline in dollar terms.

GERMANY

Policies

18. At the Louvre the German Government proposed 'to increase the size of the tax reductions already enacted for 1988'. Soon after, it was announced that income tax cuts of DM5.2 billion or 0.3 per cent of GNP (part of the larger tax reform originally scheduled for 1990) would be brought forward to next January. However, with public expenditure planned to continue to decline relative to GNP, the overall stance of fiscal policy in Germany is not expansionary. The Bundesbank has tolerated overshooting of its CBM targets for external reasons, but allowed German interest rates to edge up in the Summer when the dollar strengthened.

Forecasts

19. The German Government's projection of 2½ per cent a year output growth over the medium term seems reasonable, but growth looks like falling short of this in 1987 and 1988. The IMF predict 1.5 per cent and 2.3 per cent respectively and they do not see this shortfall in growth (compared with potential) being caught up in subsequent years. The Government's projection of 3 - 3½ per cent a year growth in real domestic demand seems optimistic given the policy of fiscal consolidation on which they are based. The IMF's projection of 2.9 per cent for 1988, but only 2.4 per cent over 1989-91, implies that the German current account surplus will decline rather little after 1988.

SM.

S W MATTHEWS

TABLE 1: SUMMARY OF IMF AND NATIONAL PROJECTIONS

		1987	1988	1989	1990
Real GNP/GDP					
IMF -	US	2.4	2.7	2.9	2.9
	Japan	3.2	3.4	3.5	3.5
	Germany	1.5	2.3	2.1	2.6
	France	1.5	1.8	2.7	2,7
	UK	3.3	2.2	2.3	2.3
	Italy	2.5	2.4	2.5	2.5
	Canada	2.8	2.9	3.0	3.0
	G7	2.5	2.7	2.9	2.9
National -	US	2.6	3.3	3.4	3.4
	Japan*	3.5	(3.4)	(3.5)	(3.5)
	Germany	2.5	2.5	2.5	2.5
	France	1.5	2.2	2.3	2.7
	UK	3.0	2.5	2.5	2.5
	Italy*	3.0	2.5	(2.5)	(2.5)
	Canada	2.8	3.0	3.3	2.8
	G7	2.7	3.1	3.2	3.2

Notes: * Figures in brackets are IMF estimates where no national figure supplied.

Current account IMF
(national forecasts, where available, in brackets)

		1987	1988	1989	1990
$ billion -	US	-148	-139	-142	-146
		(-154)	(-144)	(-118)	(-108)
	Japan	85	83	86	86
		(77)			
	Germany	39	30	30	28
		(40)	(30)	(25)	(20)
% of GNP -	US	-3.3	-2.9	-2.8	-2.7
		(-3.4)	(-3.0)	(-2.2)	(-2.0)
	Japan	3.6	3.2	3.0	2.8
		(3.6)			
	Germany	3.5	2.5	2.4	2.1
		(3.5)	(2.5)	(2.0)	(1.5)

TABLE 2: EXCHANGE RATES SINCE LOUVRE

	$ Effective	DM/$	Y/$	$/£
Monthly averages:				
January	105.5	1.86	154.6	1.51
February	103.9	1.82	153.4	1.53
March	103.3	1.84	157.5	1.59
April	101.0	1.81	142.9	1.63
May	100.4	1.79	140.6	1.67
June	101.7	1.82	144.4	1.63
July	103.3	1.85	150.2	1.61
August	103.3	1.86	147.6	1.60
Latest:				
(September 3)	100.2	1.80	141.0	1.65
Memoranda:				
$ Peak (26.2.85)	157.2	3.43	261.0	1.05
Plaza (20.9.85)	139.6	2.84	240.1	1.37
Louvre (20.2.87)	104.0	1.83	153.6	1.53

RA7.78

CONFIDENTIAL

For Baker
Watson in
Washington

FROM: A C S ALLAN
DATE: 11 September 1987

SIR G LITTLER

cc Mr H P Evans
Mr Walsh

EXPANSION OF G10

The Chancellor was grateful for your minute of 10 September. He will want to raise this with Mr Baker at his bilateral in Washington.

ACSA

A C S ALLAN

BF to ~~Atosc~~ ~~18/9~~

CONFIDENTIAL

From: Sir G.Littler
Date: 10 September 1987

Ch
Earlier papers tucked into front of Ecofin folder
AA

CHANCELLOR

c.c. Mr Evans
Mr Walsh

EXPANSION OF G10

This was given a run at the meeting of Deputies on 9 September. I circulated the Loehnis/Littler paper, as you had agreed, making it clear that this was background, not designed to stimulate a discussion. But Dini and others forced a long discussion over lunch, making two awkward points and eliciting national views.

2. The two awkward points are:

- Austria having formally applied, several countries - especially Germany - are nervous about rejecting them if Spain and/or Australia are admitted;
- Dini had got the IMF staff to produce a table based on IMF "calculated quotas" from the last quota review, on which an argument could be based for admitting Spain but not Australia. ("Calculated quotas" are those derived from a basket of current economic and financial indicators, ignoring history).

3. The canvass of views produced the attached untidy set of reactions. I suspect some of these are without consultation with Ministers, although some said they had consulted. Not at all helpful, I fear, but among Ministers you may do better.

(Geoffrey Littler)

CANVASS OF VIEWS

Options mentioned were:

A: No change at all
B: Admit Spain and Australia, nobody else
C: Admit Spain only
D: Admit Spain, Australia and Austria, nobody else
E: Admit any respectable applicant.

Views of officials were:

United States:	Any of the options acceptable.
Canada:	B - but insist on consensus.
Japan:	B - otherwise A : strongly objected to C and D as "packing with Europeans".
Germany:	D - or A or perhaps even C, but not B.
France:	C - or D or A or B in that order.
Italy:	C - or D.
Belgium:	A - or D. (Austria in their IMF group!).
Netherlands:	A - no alternative tolerable.
Sweden:	A - no alternative tolerable.
Switzerland:	A - or D or just possibly B if all others supported it.
U.K.:	B - I merely said that I hoped others would read our note carefully.

Covering **SECRET**

From: Sir G.Littler
Date: 10 September 1987

CHANCELLOR

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

G5 AND G7 DEPUTIES

I attach notes of the two meetings I attended in Paris last night and early this morning, both essentially in preparation for the full meetings of Ministers and Governors on 26 September.

2. You will see that the G7 Deputies were a bit ragged, but I ended up with the task of drawing the relevant essence together in a draft statement! The G5 was more effective and interesting - you will be particularly interested in the discussion we had on diversification.

3. I am sending copies to the Governor and Mr Loehnis.

(Geoffrey Littler)

G7 DEPS
9/9/87

SECRET

Note for the Record

MEETING OF G7 DEPUTIES

The Group met in Trichet's office in Paris for nearly six hours from 7 p.m. on 9 September:

Jean-Claude Trichet (France) - host
David Mulford (U.S.)
Toyoo Gyohten (Japan)
Hans Tietmeyer (FRG)
Geoffrey Littler (U.K.)
Mario Sarcinelli (Italy)
Wendy Brown (Canada)

and Alan Whittome and Jacob Frenkel (IMF) for part of the time.

IMF Structural Adjustment Facility

2. Whittome briefly presented the Camdessus proposal to triple the resources of the SAF, and to do so through a Trust Fund constructed with the maximum of protective 'under-writing' and contingent liquidity for creditors. Main points he emphasised were:

- the scheme required 6bn SDR of capital on market terms plus the equivalent of 2.5bn SDR to cover interest rate subsidy over a period;
- the IMF hoped to tap Middle East and NIC sources for between 1.2 and 1.5bn SDR;
- some Scandinavians and others might contribute outright grants which would help with the subsidy; in general the 'burden-sharing' of loans and grants could be different;
- use of gold in any form would require 85% majority of IMF votes, which was not practicable.

3. There was no discussion except that, after both the IMF representatives had left:

- Mulford commented that Camdessus had got on the wrong side of Baker with a very aggressive presentation and demand for U.S. support recently!
- Tietmeyer said that Germany found the whole proposal difficult (although not impossible) and was sure we would not get to decisions before the end of the year, if then;
- I said we must remember this was part of an approach to a special problem of the very poorest countries and it should be linked with Paris Club arrangements on the lines proposed by the Chancellor.

Surveillance

4. Frenkel presented the IMF figures and basic analysis. It was not a very apt or exciting performance - too professorial

for the audience. This was followed by an appalling hour of procedural discussion. Mulford complained about the unevenness of the figures produced by different countries, and demanded that all should meet the obligations accepted at Venice. Gyohten complained that the attempt to take detailed figures beyond one year was unnecessary and unacceptable. Dr Brown wanted the IMF to give their own answers to the questions they had raised, but Frenkel was coy. I tried to get to discussion of substance and suggested that we had adequate material even if it was not in the precise form some wanted. Challenged by Mulford I said that I was personally still unimpressed by the format of the indicators exercise and we had a brief replay of our arguments at Zurich last January. As then, Gyohten was sympathetic but Tietmeyer said that the exercise must reflect the Venice agreement since, however reluctantly, we were all committed to it, and he did not see how the material now before us could be turned into what was needed. I then pointed out that in terms the Venice agreement spoke of settling figures "early in the year", which could now only mean early next year. This resulted in an untidy remit to the IMF to explore what would be the correct basis on which to accumulate which figures by some date early next year to fulfil the Venice agreement.

5. After Frenkel's departure Mulford challenged me and others to say what we saw as the object of our work, if not to carry out the agreed indicators exercise. I said that I saw our task as being to prepare for the Ministerial Meeting. I felt reasonably sure that our Ministers would want to endorse the Louvre Accord and, with a background of nervous markets and a critical press, it would not be easy. However, I thought we could build on some growing evidence of successes (German and Japanese figures improving recently, the U.S. success with their fiscal deficit this year, better collective management) and we should look for such statements about future determination and intentions as we could together muster.

6. We then had a much calmer and more constructive talk, all taking the same basic line as I had suggested, and making some useful individual contributions. At the end I was asked by Tietmeyer and Gyohten (with only Mulford reluctant) to prepare and circulate very quickly a sketch of a possible statement embodying what we had all said, and agreed to do so. It should be as short as possible while touching on:

- satisfaction with evolution from Louvre;
- record of improvements in line with Louvre undertakings;
- reaffirmation of commitment;
- some points of future improvement.

7. Among more detailed points made were:

- U.S. fiscal '88 budget has key importance: strongest possible U.S. statement of determination, related to their target of $123 bn which is good, backed by what is now a better-looking track record of two years;
- U.S. statement on Trade Bills if possible;

- Japan and Germany reiterate commitment to foster steady growth of domestic demand and reduction of external surpluses;
- need to assert intensified cooperation, building on our good experience, if possible one or two specifics (such as swaps, Japan/Germany token interest rate reductions);
- emphasise how successful on markets - press fail to see that we are still very close to Louvre/Washington rates.

8. At various stages during a somewhat meandering discussion (there is no doubt that 7 is a less efficient number than 5!), other interesting points were made:

- Dr Brown voiced considerable doubts - shared around the table - over the possibility of ultimately resolving the external imbalance problems at present exchange rates; she asked whether it would be timely to start thinking now about how the group could handle a step change - but there was no enthusiasm to pursue the point (although to some extent the approach canvassed in Sir T. Burns' most recent submission gets towards this problem);
- Mulford gave an horrific account of the elaborate Congressional committee structure now operating on the combined Trade Bill; he said Baker was pursuing parallel strategies (veto, or amendment to remove worst elements of which there are many); he would soon have to choose and Mulford's own view was that veto would be best, if they could muster a nucleus sufficient to make the veto threat plausible;
- Mulford cautioned about future intervention: Baker was very reluctant to 'spend' more on this than the earlier limit which had nearly been reached (taken up again next day in G5);
- Tietmeyer led two pleas: one generally endorsed that all Ministers and Central Bankers should refrain from talking too much about market movements and actions; and one to Mulford endorsed by all others, that he should rethink the long-standing U.S. refusal to intervene as visibly as is sometimes desirable.

Brazil

9. Mulford gave an account of recent dealings with Brazil culminating in a meeting between Baker and both Bresser and Bracher on 8 September in Washington, at which he was present. The F.T. report is quite accurate. Baker had become very angry over Brazil's plotting with/against banks. He refused to see Brazilian emissaries and then more or less commanded the two Brazilians to appear before him in Washington. When they came in he read the Riot Act. Bracher was very resistant, but Bresser backed off and went so far as to say that he would be ready to adopt 'a conventional solution' if Baker would help ensure that Brazil could get good value from it.

10. Bresser then left and talked in different terms to the press, whereupon Baker issued his statement to the press stating that agreement had been reached, that Brazil was ready to adopt a conventional approach, that they would not seek to impose unilateral terms on banks (nothing to prevent voluntary agreements), and that he had insisted that Brazil should obtain a formal IMF standby. The effect was dramatic. Bresser at once made contact, tried to argue, was told he had no choice and caved in. Mulford added that neither he nor Baker is feeling trustful towards Brazil, but they reckon the agreement may hold. We should watch the outcome of a tripartite Brazil/Argentina/Mexico meeting in New York on (?) 21 September, and the new proposals Brazil has indicated it will make to banks in New York three or four days later. Overall, although much further rhetoric was to be expected, Mulford thought that Bresser was now genuinely persuaded to go for an IMF standby, although he would still try to con the banks first (probably not likely to succeed).

(Geoffrey Littler)

G5 DEPS
10/9/87

SECRET

Note for the Record

MEETING OF G5 DEPUTIES

The Group met in Trichet's office in Paris for two hours from 7-15 on Thursday morning, 10 September. (G7 Deputies had met for six hours the night before). We focussed on the future of the Louvre Accord.

Louvre Accord

2. Gyohten expressed concern about prospects for maintaining exchange rates at current levels. He was optimistic about the chances of adjustment in Japan: growth of domestic demand was now rising satisfactorily again and, although domestic output was also picking up, the trade balance had been showing a continuing fall since the peak in February. The August surplus of $5.1 billion was a third lower than that of last August.

3. But he was frankly worried about U.S. adjustment, partly because it was extremely difficult to see how further reductions in the fiscal deficit were to be achieved without tax ~~cuts,~~ increases partly because U.S. performance seemed relatively sluggish. Investors in Japan were increasingly nervous about the U.S. on these grounds, and of course because their exposure was already large, and they were showing increasing interest in shifts to other currencies and economies.

4. In a subsequent interjection he said that the Bank of Japan was becoming more reluctant to take interest rate action to support the dollar because of competing needs to restrain threats of internal inflation. They would not want to subscribe to any public assertion that exchange rate considerations should take priority. And if markets were allowed to develop worries about new inflation risks in the world, they would tend to sell dollars.

5. In spite of all these worries, he appeared to envisage that Japan would stick loyally to the Louvre Agreement as long as others did - and he confirmed that he favoured holding on at the forthcoming meetings.

6. In a digression, Mulford outlined the state of play on U.S. negotiations over exchange rates with Taiwan, Korea and also Hong Kong - all going very slowly and with not much result yet to show. He offered to send us privately a U.S. analytical paper. All present agreed that Taiwan was the worst case (although they happen also to enjoy a strong supportive lobby in Congress). On Korea, Gyohten's sympathy with Mulford was tempered by judgment that they needed to be encouraged to continue to reduce their still very large burden of commercial debt (over $40 billion). I spoke briefly on Hong Kong and Tietmeyer chipped in with a helpful comment on their free market and use as an entrepot for mainland China trade.

7. Mulford thought that, after initial nervousness in the markets about the Louvre Agreement, sentiment had strengthened a good deal, helped by widening of interest differentials and by second thoughts about successes in U.S. industry. The summer period had been quite calm. What had recently re-emerged, as a result of poor trade figures, and with weaker differentials, was another bout of unease, with signs of some Japanese investors liquidating bonds. He still thought the underlying market was resilient. It would be very helpful if the Washington meetings could emphasise continuity and momentum. To this end he hoped for helpful statements on, for example, the Japanese intentions for the 1988 budget, acceleration of German tax reform (strongly negatived by Tietmeyer), something on interest rates, as well as whatever the U.S. could say on fiscal and trade policy.

8. Trichet pressed strongly on interest rates, at first seeming to canvass the old idea of concerted and universal rate reductions (he spoke several times on the familiar French theme of the unjustifiably high level of real interest rates - although at one point he also acknowledged that there must be an imbalance of supply and demand). He later pressed only for some symbolic move by Japan and Germany, to pre-empt or reverse the disposition of markets to begin looking for increases. Gyohten was sceptical (see comment above); Tietmeyer was more sympathetic (apparently he had argued against the recent Bundesbank decision to raise rates very marginally); I opposed the universal approach but said that wider differentials could certainly have a role and this was Mulford's position also.

9. Finally an interesting discussion developed on resources for intervention, starting from Mulford's caution the previous evening about the U.S. reaching its limits. Trichet asked wo the U.S. contemplate borrowing foreign currencies. Mulford revealed that some thought had been given to this earlier, but pursued because of objections against another 'Carter Bond'; he added that he was not personally opposed and had been wonde about some borrowings by the U.S. Government in yen/DM, to hel meet Budget financing needs.

US to borrow foreign currencies

10. After some predictable warnings about financing domestic deficits in this way, Gyohten and Tietmeyer confirmed that they would not object to having their currencies borrowed by the U.S. Gyohten then broadened the discussion to ask what about swaps, and I threw in the argument for developing cross-holdings. There was good support for the latter idea (the name "diversification" was thought to be more appealing), although Tietmeyer warned that the Bundesbank, but not himself, were rigorously opposed.

11. The conclusion reached was that some move in this field might be of substantive value and also of some symbolic value if it could be publicised in Washington. As a minimum, and even if it was not strictly necessary, the announcement of extensions of swap arrangements might be worth considering.

SECRET

Multinational Institutions

12. There was a fairly rapid agreement that, faced with the well-known problems of the Congress, we would all set the order of priority as follows:

& SSA [illegible]?!

1. complete IDA 8;

2. launch arrangements for the GCI (World Bank);

3. set up the expanded SAF (IMF);

4. - and distinctly last - IMF quota review.

(A nuance was that the French hoped 2 and 3 could be close together).

13. We agreed that it would be sensible for Baker at the G5 Meeting to explain and secure agreement if possible on this.

Future Meetings

14. Mulford confirmed the 26 September arrangements:

9-30 until 12: G5

12-45 until 5: G7.

15. We noted that all G7 Deputies will be in Washington from 6 p.m. on the previous day, in case it should be helpful for them or G5 Deputies to meet.

(Geoffrey Littler)

I sh'd be grateful for urgent comments of the Chancellor. My own view is that it is too [illegible] to say that it would appear that the [illegible] clear that the Louvre continues with position unchanged. N.

SECRET

From: Sir G.Littler
Date: 15 September 1987

CHANCELLOR

c.c. Sir P.Middleton
Sir T.Burns

WASHINGTON: G7 STATEMENT

I showed you in the plane over the weekend the first draft I had prepared for a possible G7 Statement in Washington - having taken this on at the request of my G7 Deputy colleagues on the basis that I would reflect our discussion together as faithfully as possible.

2. Hans Tietmeyer had one or two small and I thought sensible suggestions which I have incorporated. I have now sent the draft to all my G7 colleagues as promised and asked for their reactions. I thought you might like to see this version. I hope to be able to give you a round-up of reactions by the end of this week.

(Geoffrey Littler)

Ch

I have marked on the weekend draft (below) the changes made. They improve it (particularly para 4) – but note "monetary policy" has replaced "interest rate differentials" in last paragraph.

AH

SECRET

DRAFT [14 September]

STATEMENT OF THE GROUP OF SEVEN

1. The Finance Ministers and Central Bank Governors of seven major industrial countries met today. This continues the series of meetings in which they have been carrying out surveillance of their economies and gradually developing a stronger and more effective cooperation along the lines agreed at the 1986 Tokyo and 1987 Venice Summit Meetings of their Heads of State or Government.

2. The Ministers and Governors reviewed together the evolution of foreign exchange markets, and of events and policies, since the Louvre Agreement. They took satisfaction from the improving quality and techniques of their cooperation in fostering exchange rate stability, and the degree of success achieved over a period in which their efforts have inevitably been on trial.

3. They are convinced that greater exchange rate stability has been welcomed by traders and investors and has indeed contributed to the renewed strengthening of output which has recently been taking place.

4. In the light of experience, the Ministers and Governors consider that their judgment earlier this year - that their currencies had come within ranges broadly consistent with underlying economic fundamentals - was and remains valid. They recall that an important part of that judgment was the agreement they reached that the continuing conduct of economic and financial policies must be appropriate and effective.

5. In the Louvre Agreement the Ministers and Governors set out the policies which they intended individually to pursue, believing them to be consistent, and undertaking to monitor them together and as necessary intensify or adapt them. They note that some important decisions have been taken in individual countries which were foreshadowed in the February statement, and that generally the evolution of policies has been along the lines intended.

6. Some important favourable effects are beginning to be seen: the sharp reduction in fiscal 1987 in the United States federal budget deficit is a welcome step towards necessary adjustment; the major programme of additional expenditures in Japan is being rapidly implemented; in Germany the reductions in income taxes from 1988 are to be substantially greater than previously planned; there has been a welcome revival of domestic demand in the surplus countries whose currencies had sharply appreciated; and further steps have been taken in the direction of liberalisation and structural change. External imbalances remain high, but there have been quite strong reductions in them in real terms and growing indications that they are now diminishing in dollar terms.

7. The Ministers and Governors note that the successful trade performance of some newly industrialised economies continues to be an important factor contributing to external imbalances and they repeat their view expressed on earlier occasions that these economies should reflect their growing importance and responsibilities by reducing trade barriers and pursuing policies that allow their currencies to reflect more fully underlying economic fundamentals.

SECRET

8. The Ministers and Governors are satisfied that they correctly identified the appropriate directions of policy in the Louvre Agreement. The continuing task in carrying forward their agreement and cooperation together is now to develop and intensify the appropriate policies in each of their countries as necessary.

9. The Ministers and Governors commit themselves again to the directions of policy set out in the Louvre Agreement and expect to take further measures in accordance with them over the coming months. In particular:

- the Government of the United States expresses its determination to carry further in fiscal 1988 progress already achieved in reducing the federal budget deficit and to continue to resist protectionist action which can only damage the interests of all;

- the Governments of the Federal Republic of Germany and Japan reassert their commitment to continue to foster steady growth of domestic demand and reduction of external surpluses;

- the Governments of each of their countries will continue to pursue liberalisation of markets, tax reforms and other structural changes to maximise the scope for a high rate of sustained non-inflationary growth.

During the coming year the developments of their economies will be monitored increasingly closely under the surveillance arrangements outlined in the Venice Summit.

10. The Ministers and Governors intend to carry forward their cooperation in fostering exchange rate stability and to develop further in the light of experience the range of techniques and the resources available to them. This will be a continuing process. In the immediate future they aim to strengthen their cooperation in the management of monetary policies, and their central banks will be broadening the existing network of swap arrangements in each other's currencies.

original draft

DRAFT

[14 September]

1. The Finance Ministers and Central Bank Governors of seven major industrial countries met today. This continues the series of meetings in which they have been carrying out surveillance of their economies and gradually developing a stronger and more effective cooperation along the lines agreed at the 1986 Tokyo and 1987 Venice Summit Meetings of their Heads of State or Government.

2. The Ministers and Governors reviewed together the evolution of foreign exchange markets, and of events and policies, since the Louvre Agreement. They took satisfaction from the improving quality and techniques of their cooperation in fostering exchange rate stability, and the degree of success achieved over a period in which their efforts have inevitably been on trial. [and in which there has been no shortage of disturbing events and variations in market pressures.]

3. They are convinced that greater stability has been welcomed by traders and investors and has indeed contributed to the renewed strengthening of output which has recently been taking place.

4. In the light of experience, the Ministers and Governors consider that their judgment earlier this year - that their currencies had come within ranges broadly consistent with underlying economic fundamentals - was and remains valid. [But they stress that] They recall that an important part of that judgment was [and remains subject to the important qualification] the agreement that that the continuing conduct of economic and financial policies must be appropriate and effective.

5. In the Louvre Agreement the Ministers and Governors set out the policies which they intended individually to pursue, believing them to be consistent, and undertaking to monitor them together and as necessary intensify or adapt them. They note that some important decisions have been taken in individual countries which were foreshadowed in the February statement, and that generally the evolution of policies has been along the lines intended.

6. Some important favourable effects are beginning to be seen: the sharp reduction in fiscal 1987 in the United States federal budget deficit is a welcome step towards necessary adjustment; the major programme of additional expenditures in Japan is being rapidly implemented; in Germany, --- there has been a welcome revival of domestic demand in the surplus countries whose currencies had sharply appreciated; and further steps have been taken in the direction of liberalisation and structural change. External imbalances remain high, but there have been quite strong reductions in them in real terms and growing indications that they are now diminishing in dollar terms.

para on NICs

7. The Ministers and Governors are satisfied that they correctly identified the appropriate directions of policy in the Louvre Agreement. The continuing task now is to develop and intensify them as necessary.

8. The Ministers and Governors commit themselves again to those directions of policy and expect to take further measures in accordance with them over the coming months. In particular:

- the Government of the United States expresses its determination to carry further in fiscal 1988 progress already achieved in reducing the federal budget deficit and to continue to resist protectionist action which can only damage the interests of all;
- the Governments of the Federal Republic of Germany and Japan reassert their commitment to foster steady growth of domestic demand and reduction of external surpluses;
- the Governments of each of their countries will continue to pursue liberalisation of markets, tax reforms and other structural changes to maximise the scope for a high rate of sustained non-inflationary growth.

During the coming year the developments of their economies will be monitored increasingly closely under the surveillance arrangements outlined in the Venice Summit.

9. The Ministers and Governors intend to carry forward their cooperation in fostering exchange rate stability and to develop further in the light of experience the range of techniques and the resources available to them. This will be a continuing process. In the immediate future they aim to strengthen their cooperation in the management of [~~interest rate differentials~~ monetary policy], and their central banks will be broadening the existing network of swap arrangements in each other's currencies.

RA7.87

SECRET

FROM: A C S ALLAN

DATE: 16 September 1987

MR CULPIN

WASHINGTON: G7 STATEMENT

... See the attached papers. The Chancellor ~~will~~ would be grateful for your urgent comments. His own ~~views~~ view is that it is too long and that it nowhere appears to say in clear terms that Louvre continues with parities unchanged.

ACSA

A C S ALLAN

FROM: J. COLENUTT
DATE: 17 September 1987

cc Mr. Matthews
Mr. Savage

MRS RYDING,

ROAL INTEREST RATES IN THE G7

I have attached the table as requested.

2. The inflation rates used are those published by the OECD (copy of OECD publication attached). These rates may differ from those appearing in the press.

J. Colenutt

Baker speed

Taylor → Fern 16/9

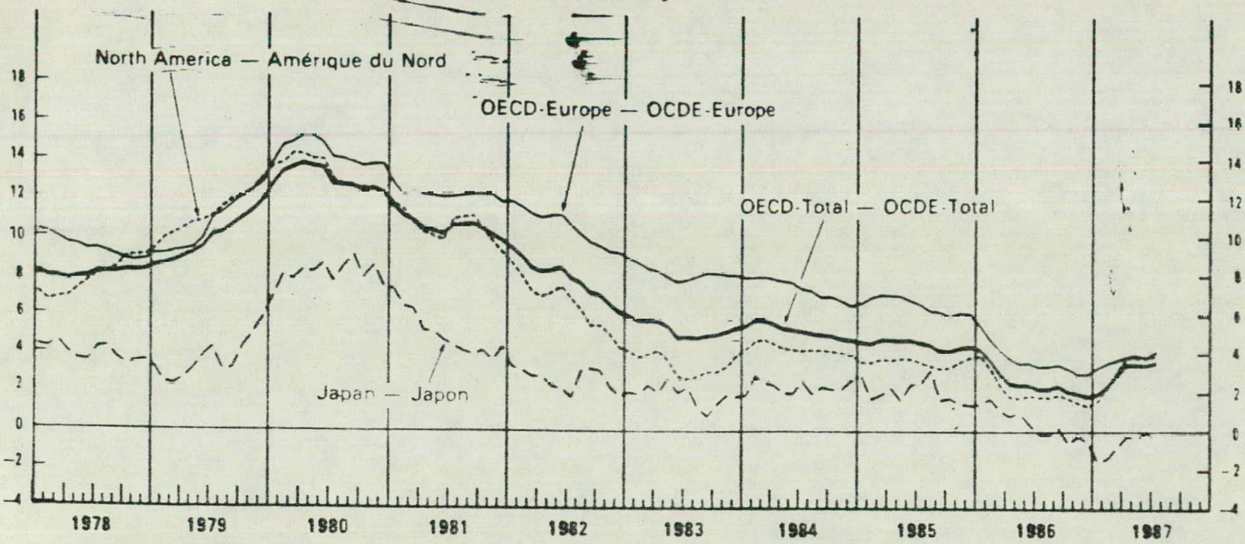
Minute for me to Geoff re Miyazawa.

Advance Release of Main Economic Indicators
(monthly).

1980 = 100

1980 = 100

Per cent change over 12 months
Variations en pourcentage sur 12 mois



	Weight in 1985 (5) / Pondération en 1985	1984	1985	1986	1986 Q3	1986 Q4	1987 Q1	1987 Q2	1987 FEB	MAR	APR	MAY	JUN	JUL	12-month rate of change / Variation sur 12 mois
ALL ITEMS — TOTAL															
Canada	3.7	137.6	143.1	149.0	149.8	151.3	152.7	154.8	152.7	153.4	154.1	155.0	155.4	156.8	4.7
United States · États-Unis	47.9	126.1	130.5	133.1	133.3	134.0	135.5	137.5	135.3	136.1	136.8	137.2	137.8	138.1	3.9
Japan · Japon	14.4	112.1	114.4	114.9	114.6	114.5	113.7	115.1	113.5	114.1	115.1	115.3	115.0	114.2	−0.4
Australia · Australie	1.7	139.4	148.8	162.4	163.9	168.6	172.0	174.6	172.0			174.6			9.3
New Zealand · Nouvelle Zélande	0.2	152.8	176.3	195.6	199.6	217.4	222.5	229.8	222.5			229.8			18.4
Austria · Autriche	0.7	122.9	126.9	129.0	129.2	129.2	129.4	130.5	129.3	129.6	129.5	130.2	131.4	132.0	2.4
Belgium · Belgique	0.9	134.0	140.5	142.3	142.5	142.6	143.5	144.5	143.5	143.7	144.4	144.4	144.6	145.8	2.4
Denmark · Danemark	0.6	140	146	152	153	154	155	157	154	156	157	155	159	158	4.1
Finland · Finlande	0.5	142	151	156	157	158	160	162	160	161	161	162	162	162	3.4
France	6.1	149.3	158.0	162.2	162.4	163.5	165.5	166.9	165.5	155.7	166.6	166.9	167.2	157.8	3.4
Germany · Allemagne	6.6	118.4	121.0	120.7	120.4	120.0	120.7	121.1	120.7	120.7	121.0	121.1	121.3	121.3	0.7
Greece · Grèce	0.4	216.4	255.8	314.7	316.5	335.1	345.9	365.5	342.7	353.6	361.5	363.3	371.0	365.5	16.9
Iceland · Islande (1)	—	552	728	889	897	927	975	1017	975	991	1001	1017	1032	1035	18.7
Ireland · Irlande	0.2	169.3	178.5	185.2	185.8	186.2	189.6	190.6	189.6			190.6			2.8
Italy · Italie (2)	4.1	174.3	190.3	201.4	201.9	204.3	207.2	209.6	207.4	208.0	208.8	209.7	210.5	[illegible]	[illegible]
Luxembourg (1,3)	—	134.3	139.8	140.2	139.7	140.0	140.3	139.8	140.4	140.3	140.0	139.8	139.8	139.4	−0.3
Netherlands · Pays-Bas	1.4	120.0	122.7	122.9	122.1	123.2	121.5	122.1	121.5	121.8	122.1	122.1	122.0	121.9	0.1
Norway · Norvège	0.5	148	154	165	168	171	176	178	176	177	178	178	179	180	8.1
Portugal (1)	0.3	238.3	284.3	317.4	318.5	326.3	338.6	344.7	338.4	341.1	344.5	345.2	344.1	345.2	9.2
Spain · Espagne	2.0	163.4	178.0	193.7	195.8	198.1	201.0	202.5	201.0	202.0	202.4	202.3	202.3	204.2	4.8
Sweden · Suède	1.0	143	154	160	160	162	163	165	164	165	165	165	165	[illegible]	[illegible]
Switzerland · Suisse	1.1	119.3	123.3	124.2	123.8	124.4	125.7	125.7	125.7	126.0	126.1	125.4	125.7	125.8	1.6
Turkey · Turquie	0.7	310	450	605	609	660	734	800	732	759	775	813	812	928	37.7
United Kingdom · Royaume Uni	5.0	133.3	141.8	146.4	146.5	148.4	150.2	152.5	150.3	150.6	152.4	152.5	152.5	152.4	4.4
OECD Total · OCDE Total	100.0	131.7	137.6	141.1	141.3	142.2	143.3	145.3	143.3	144.1	144.9	145.4	145.7	[illegible] (e)	3.3
North America · Amérique du Nord	51.6	126.9	131.5	134.2	134.3	135.3	136.8	138.6	136.8	137.4	138.1	138.5	139.1	139.4	[illegible]
OECD-Europe · OCDE-Europe	32.1	144.0	153.4	159.2	159.4	161.0	163.0	164.9	163.0	163.6	164.5	[illegible]	[illegible]	[illegible] (e)	4.2
EEC · CEE	27.6	143.8	149.8	154.7	154.8	156.0	157.8	159.1	157.8	158.0	158.9	159.1	159.4	[illegible] (e)	3.3
FOOD — ALIMENTATION															
OECD-Total · OCDE-Total	100.0	128.2	132.6	137.3	138.0	138.8	140.3	141.6	140.6	140.8	141.2	141.8	141.9	141.8 (e)	3.0
North America · Amérique du Nord	51.6	119.9	122.6	126.7	127.7	128.7	130.7	131.8	130.9	130.8	131.2	131.8	132.5	132.4	4.3
OECD-Europe · OCDE-Europe	32.1	142.8	150.8	158.6	159.0	160.0	161.9	163.2	161.5	162.5	163.0	163.1	163.5	165.8 (e)	3.0
EEC · CEE	27.6	139.4	145.8	152.6	153.1	153.7	155.2	156.1	155.3	155.6	156.1	155.9	156.3	156.1 (e)	2.0
ALL ITEMS LESS FOOD — TOTAL SAUF ALIMENTATION															
OECD-Total · OCDE-Total	100.0	132.8	138.9	142.0	142.1	143.1	144.4	146.3	144.3	145.0	145.9	146.8	146.7	147.0 (e)	3.7
North America · Amérique du Nord	51.6	128.5	133.5	135.9	136.0	135.7	138.1	140.0	138.0	138.8	139.5	140.0	140.5	140.9	3.9
OECD-Europe · OCDE-Europe	32.1	144.3	154.3	159.4	159.6	161.3	163.3	165.3	163.3	163.8	164.9	165.2	165.8	166.1 (e)	4.4
EEC · CEE	27.6	142.2	150.9	155.1	155.2	156.6	158.2	159.9	155.2	158.6	155.8	159.5	160.3	160.8 (e)	3.7
ENERGY — ÉNERGIE (4)															
OECD Total · OCDE Total	100.0	131.8	135.2	123.3	120.7	117.7	119.4	121.4	119.7	119.8	120.6	121.1	122.7	123.0 (e)	1.5
North America · Amérique du Nord	51.6	125.2	127.3	115.5	113.8	109.6	112.6	115.8	113.1	113.5	114.2	115.2	117.9	118.8	3.3
OECD-Europe · OCDE-Europe	32.1	149.5	157.7	142.1	138.5	136.7	137.5	137.1	137.4	136.7	137.1	135.9	137.2	137.0 (e)	−1.1
EEC · CEE	27.6	151.5	159.9	144.0	140.5	138.5	136.8	138.5	128.7	137.9	138.4	138.1	138.5	[illegible] (e)	−1.8

1. Excluding Rent 2. From 1986 new index 3. From 1984 new index 4. Includes *Fuel and Electricity* and, where available, *Gasoline*. Belgium, Greece, Iceland, Portugal and Spain are not included in the aggregate series. 5. The country weights used in the aggregate indices are based on the private consumption and exchange rates of the previous year.

1. Non compris les loyers 2. A partir de 1986 nouvel indice 3. A partir de 1984 nouvel indice 4. Comprend *Combustibles et Électricité* et quand la série existe *Essence*. Les indices agrégés ne comprennent pas la Belgique, la Grèce, l'Islande, le Portugal et l'Espagne. 5. Les poids des pays utilisés dans les indices agrégés sont basés sur la consommation privée et les taux de change de l'année précédente.

Source OECD

UNCLASSIFIED

psl/11A

~~PS~~ BF 21/9

FROM: A C S ALLAN

DATE: 17 September 1987

MR S MATTHEWS

cc Sir G Littler
Sir T Burns
Mr H P Evans
Mr Culpin
Mr Walsh

AGGREGATE G7 STATISTICS

The Chancellor would be grateful for figures for aggregate G7 fiscal deficits as a percentage of GDP and average real interest rates for the G7, in both cases giving annual figures over a run of years.

2. I should be grateful if you could let me have figures by close of play on Monday, 21 September.

ACSA

A C S ALLAN

744/21

FROM: ROBERT CULPIN
DATE: 17 SEPTEMBER 1987

CHANCELLOR

Thanks. I will minute Sir GL as indicated in my note @ [illegible] on [illegible]

G7 STATEMENT

Sir Geoffrey Littler's draft.

2. I don't think length matters.

3. I agree that the Louvre needs to be reaffirmed more explicitly - and quotably. The drafting problem is that you can't just say Louvre with unchanged parities because it is actually Washington unchanged.

4. What's the code for that? It might not be brilliant to repeat "stability around current levels", or whatever the phrase was, because that was used in April to <u>shift</u> the goal-posts. And "stability around the levels prevailing at our Spring Meetings" would be pretty heavy handed.

5. Sir Geoffrey Littler is much better at this than I am. But the sort of thought we need in paragraph 4, after the first sentence, is this:

> They therefore reaffirm unchanged their determination to act together to promote [or prolong] a period of stability in exchange rates.

Or:

> This reinforces their existing determination to promote/prolong a period of stability in exchange rates.

6. If anyone can work in the word "managed", as in managed floating, so much the better.

7. As I said last night, I think we ought to have some proposition, probably at the end of paragraph 4, about the performance of the G7 as a whole. We need the facts from Sir Terence Burns. But we ought to be able to say that policy remains anti-inflationary, with a low overall fiscal deficit and high real interest rates - something like that.

8. Paragraph 6 will look Panglossian, particularly because we all expect the US budget deficit to increase next year. But there may be nothing we can do about that.

9. My only other comment is that the reference in the last sentence to an "aim to strengthen co-operation in the management of monetary policies" is cryptic.

Rc

ROBERT CULPIN

Pse reply to Sir GL 15/9 as follows.

Thanks. I am content with the Tietmeyer amendments.

The main missing element in the current draft is a clear, unifying affirmation that the course continues and what [illegible] have [illegible] ~~[illegible]~~ might suggest that [illegible] the goalposts. This omission is striking, although [illegible]. Otherwise the paper seems fine. It would be helpful to have some reference to the G7 as a whole, as well as to individual countries; convergence [illegible] well known [illegible] although there are imbalances the performance of the G7 as a whole is satisfactory and the policy stance anti-inflationary. There are 2 or 3 ways [illegible] figs.

RA7.90

SECRET

B pvy

FROM: A C S ALLAN

DATE: 17 September 1987

SIR G LITTLER

cc Sir P Middleton
Sir T Burns

WASHINGTON: G7 STATEMENT

The Chancellor was grateful for your minute of 13 September and the attached draft G7 statement.

2. He is content with the Tietmyer amendments.

3. He feels that one important omission from the current draft is a clear, ringing and quotable reaffirmation that Louvre continues - and without anything that might suggest that we have moved the goal posts. He feels it is important that a passage on these lines is added.

4. Otherwise, he is content with the draft, although he feels it would be helpful to have some reference to the G7 as a whole, as well as to individual countries, conveying the thought that, although there are well known imbalances, the performance of the G7 as a whole is satisfactory and the policy stance firmly anti-inflationary. There may be some useful figures which could be quoted.

ACSA

A C S ALLAN

sw27

FROM: S W MATTHEWS
DATE: 18 September 1987

CHANCELLOR

cc: Sir P Middleton
Sir T Burns
Sir G Littler
Mr Cassell
Mr Lavelle
Mr Evans
Mr Odling-Smee
Mr Peretz
Mr Sedgwick
Mr Savage

Rup Washington

G5/G7 SURVEILLANCE DISCUSSIONS: INDICATORS

This brief deals mainly with the statistical material circulated by the Fund staff for the G5/G7 Surveillance Discussions with the IMF Managing Director in Washington. It first comments on how the staff have interpreted the Venice Declaration and other procedural issues. It then discusses the forecasts themselves and offers some thoughts on their policy implications. (A copy of the IMF's note is attached - top copy only).

2. You asked - Mr Taylor's minute to Mr Evans of 16 September - what Baker had in mind when he said "... in the long run, we must look for ways to add discipline to the exchange rate system." Mr Lankester reports that Baker has no blue-print, merely a feeling that the indicators exercise was not working well and needed to be narrowed down - perhaps attempting to set targets for current accounts of the balance of payments. It is difficult to think of a less sensible target.

3. You should be aware that the Canadians - Michael Wilson's letter to Camdessus of 26 August, just received - have come out strongly in favour of indicators. Not content with supplying (optimistic) figures to 1990, as requested by the Fund, they have offered figures, apparently accurate to two decimal places, as far ahead as 1993!

USE OF INDICATORS

4. The multilateral surveillance discussions in Washington will be the first since the G7 signed up to the Venice Declaration.

You will recall that the Declaration noted in particular:

a. "the commitment by each country to develop medium term objectives and projections for its economy, and for the group to identify objectives and projections, that are mutually consistent individually and collectively; and

b. the use of performance indicators to review and assess current economic trends and determine whether there are significant deviations from an intended course that require consideration of remedial actions".

5. In their note the IMF staff present the national projections which they have collected, together with their own WEO projections. Their note offers no guidance, though, on how these are to be developed into a mutually consistent set of objectives and projections, or on how "performance indicators" should be determined.

6. The US may well complain about incomplete and out-of-date national forecasts being supplied to the Fund. If so, you could argue that it is preferable to work with a single, coherent set of projections such as that produced by the IMF. If necessary, you could also point out that, while the US Administration has supplied figures to 1990, they are quite unrealistic (see paragraph 16 below) and do not provide a practical basis for any indicators exercise, let alone the "performance indicators", after which the Americans still appear to hanker.

7. Views within the G7 on the usefulness of "performance indicators" continue to differ. We , along with the Germans and Japanese, have stressed the importance of being pragmatic and avoiding automaticity or fine-tuning. France and Italy want a more active use of indicators (with greater emphasis on exchange rates) to set desired policy outcomes and to trigger multilateral discussions should performance fall short of these targets. How far any country (particularly the US) would in practice be prepared to change its policies remains a moot point.

8. While stressing the UK's commitment to the Venice Declaration, you will want to work toward a downgrading of the indicators exercise in favour of closer and more practical co-operation on managing exchange rates. The "indicators" can remain as a useful set of medium-term projections - to be supplied by the IMF - which would provide a common reference point for surveillance discussions.

9. You will in any case want to stress the importance of the G5/ G7 meetings producing new commitments on reducing the US budget deficit, strengthening domestic demand growth in Japan and Germany, resisting protectionism etc, rather than getting bogged down in procedural issues.

THE STATISTICAL MATERIAL

10. The national projections in tables A - D are a largely inseparable mixture of what the various Governments expect to happen and what they would like to happen. The Japanese are reluctant to quantify even what they would like to happen in the medium-term. They give no figures at all beyond the current year. The value of the figures as projections is in any case limited by differences in underlying assumptions. There is no reason therefore to revise our view that Ministers should focus on a single set of numbers produced by the IMF staff.

11. The staff's estimates are consistent in that they are based on a common set of assumptions about exogenous variables. They are taken from the "Accommodating Finance Scenario" of the WEO. This assumes a continuation of current fiscal policies, and that any domestic or external financial imbalances that arise from this are smoothly financed without any changes in interest rates or real exchange rates. This is almost certainly unrealistic, but it provides a useful way of identifying possible inconsistencies or policy unsustainability. Given the assumptions, such "tensions" over the medium term will be reflected in the figures for fiscal and current account imbalances, rather than the sort of sharp changes in financial markets that one is actually likely to see.

12. With this in mind, we comment below on the main features of the projections for the three largest countries. The forecasts for real GNP growth and current account balances are summarised in tables 1 and 2.

UNITED STATES

Policies

13. In the Louvre Agreement the United States said it would reduce the Federal deficit from an estimated 3.9 per cent of GNP in fiscal 1987 to 2.3 per cent (the Gramm-Rudman-Hollings target) in fiscal 1988. This is equivalent to a reduction from $170 billion to $108 billion In the event, the deficit is likely to be a little lower than estimated for fiscal 1987 (at around $160 billion), largely because of one-off receipts from tax reform and a number of other factors (e.g. asset sales). For fiscal year 1988, nothing is yet decided, but the likely range is from the Administration's hope of perhaps a small reduction on FY1987 to a CBO baseline (i.e. on the basis of current legislation) figure of $183 billion.

Monetary policy and the exchange rate

14. The following table shows the lows and highs in the dollar (against the DM, the yen and in effective terms) since the Louvre Agreement, and short term interest rates in the United States. Table 2 and the attached chart show exchange rate developments this year in more detail.

Not attached! will obtain on monday.

	DM	Yen	Effective rate (1975=100)	US short term interest rates
20 February (Louvre)	1.828	153.6	104.0	6.2
6 May (low)	1.773	139.2	99.5	6.3
11 August (high)	1.896	151.8	105.1	6.4
16 September	1.815	144.3	101.0	7.5

15. US interest rates firmed in May and have recently risen again, as the dollar has come under renewed downward pressure.

Forecasts

16. The Administration's forecasts are extremely optimistic in every respect. Real GDP is expected to grow by almost 3½ per cent a year over the rest of the 1980s, compared with an average rate of 2½ per cent since 1979. The unemployment rate is expected to decline and at the same time inflation remains low, although the US economy is probably now close to full employment, so that further reductions in unemployment could mean an acceleration of inflation.

17. The IMF's projections are more plausible and show GDP growing broadly in line with an estimated growth rate of potential of $2^{3}/4$ per cent a year. The United States **current account deficit** is turning out a touch higher this year and next year than expected by the Fund in April 1987. Moreover, on present policies and exchange rates, the Fund staff see no improvement in the deficit in dollar terms in the medium-term:

	1986	1987	1988	1989	1990
$ billion					
Fund forecasts					
1. Made in April 1987	-141	-139	-129		
2. Made in August 1988	-141	-148	-139	-142	-146

Policy implications

18. On present fiscal policies there are significant risks of substantial dollar depreciation and/or rise in US interest rates some time before 1990. This leads to the familiar conclusion that cuts in the Federal budget deficit are needed in order to reduce the excess of US investment over saving. The projections indicate that tax increases and/or expenditure reductions are required: current policies will not by themselves deliver sufficient deficit reduction.

19. Continuing enormous current account deficits will mean that protectionist pressures are likely to remain strong. You will want of course to secure satisfactory assurances from the Administration on their intentions with regard to the current and future Trade Bills.

JAPAN

Policies

20. At the Louvre, the Government of Japan undertook 'to follow monetary and fiscal policies which will help to expand domestic demand and thereby contribute to reducing the external surplus'. The Y6 trillion package, first announced in April but not presented in detail until 29 May, was greeted with some scepticism. Though some doubts remain, the IMF staff have tentatively estimated that the package will raise Japanese GNP by ½ per cent this year and by 1 - 1½ per cent in 1988.

Forecasts

21. Japan provided fewer national figures than anyone else, giving only forecasts for the current year, and no quantified medium-term objectives. The forecasts are a little more optimistic than those of the IMF and ourselves, both on output and on the balance of payments, but the differences are not particularly large.

22. The IMF's medium term projection of growth is broadly in line with potential, but they may be a bit optimistic about the rate of real domestic demand growth, given the assumption of no changes in policies or exchange rates. Even so, the Japanese current account surplus shows little decline in dollar terms.

Policy implications

23. There is a risk that domestic demand growth in Japan will continue to be a little disappointing, and you will want to obtain satisfactory commitments that macroeconomic and structural

policies will be used to ensure that domestic demand growth is adequate to reduce the current account surplus.

GERMANY

Policies

24. At the Louvre the German Government proposed 'to increase the size of the tax reductions already enacted for 1988'. Soon after, it was announced that income tax cuts of DM5.2 billion or 0.3 per cent of GNP (part of the larger tax reform originally scheduled for 1990) would be brought forward to next January. However, with public expenditure planned to continue to decline relative to GNP, the overall stance of fiscal policy in Germany is not expansionary. The Bundesbank has tolerated overshooting of its CBM targets for external reasons, but allowed German interest rates to edge up in the Summer when the dollar strengthened.

Forecasts

25. The German Government's projection of 2½ per cent a year output growth over the medium term seems reasonable, but growth looks like falling short of this in 1987. The IMF predict 1.5 per cent and do not see this shortfall in growth (compared with potential) being caught up in subsequent years. The Government's projection of 3 - 3½ per cent a year growth in real domestic demand seems optimistic. The IMF's projection of 2.9 per cent for 1988, but only 2.4 per cent over 1989-91, implies that the German current account surplus will decline rather little after 1988.

Policy implications

26. German domestic demand growth in the 1980's has been remarkably sluggish - its level in 1987 is likely to be only 7½ per cent above 1980 - and it is proving difficult to raise its growth rate now. This may reflect hysteresis effects, but structural adjustment efforts have also been weak (e.g. the high

subsidies paid to coal mining and farming) and policy changes are used to encourage the re-allocation of resources in line with changing patterns of demand and competitiveness.

84.

S W MATTHEWS

Table 1: Summary of IMF and National Projections

		Real GNP/GDP				Real Domestic Demand			
		1987	1988	1989	1990	1987	1988	1989	1990
IMF -	US	2.4	2.7	2.9	2.9	1.7	1.9	2.8	2.8
	Japan	3.2	3.4	3.5	3.5	4.0	4.4	4.4	4.4
	Germany	1.5	2.3	2.1	2.6	2.9	2.9	2.2	2.9
	France	1.5	1.8	2.7	2.7	2.3	2.1	2.9	2.9
	UK	3.3	2.2	2.3	2.3	3.7	2.9	2.5	2.5
	Italy	2.5	2.4	2.5	2.5	3.8	2.9	2.8	3.0
	Canada	2.8	2.9	3.0	3.0	2.8	2.9	2.8	2.8
	G7	2.5	2.7	2.9	2.9	2.6	2.7	3.1	3.2
National -	US	2.6	3.3	3.4	3.4	2.0	2.4	2.8	3.0
	Japan*	3.5	(3.4)	(3.5)	(3.5)	4.1	n.a	n.a	n.a
	Germany	2.5	2.5	2.5	2.5	3.0	3.5	3.0	3.0
	France	1.5	2.2	2.3	2.7	2.4	1.9	2.6	3.0
	UK+	3.0	2.5	2.5	2.5	3.5	2.5	n.a	n.a
	Italy*	3.0	2.5	(2.5)	(2.5)	4.1	3.1	n.a	n.a
	Canada	2.8	3.0	3.3	2.8	2.0	2.8	3.4	2.6
	G7	2.7	3.1	3.2	3.2	2.8	n.a	n.a	n.a

Notes: * Figures in brackets are IMF figures where no national figure supplied.
+ FSBR figures.

Table 2: Projections of Current Balances

		1987	1988	1989	1990
IMF -	$ billion				
	US	-148	139	-142	-146
	Japan	85	83	86	86
	Germany	39	30	30	28
	% of GNP				
	US	-3.3	-2.9	-2.8	-2.7
	Japan	3.6	3.2	3.0	2.8
	Germany	3.5	2.5	2.4	2.1
National -	$ billion				
	US	-154	-144	-118	-108
	Japan	77	n.a	n.a	n.a
	Germany	40	30	25	20
	% of GNP				
	US	-3.4	-3.0	-2.2	-2.0
	Japan	3.6	n.a	n.a	n.a
	Germany	3.5	2.5	2.0	1.5

Papers please
G7 draft
statement

SECRET

From: Sir G.Littler
Date: 18 September 1987

MR ALEX ALLAN

G5/7

I promised a round-up before the weekend, but I am afraid this is interim only - I hope to have further calls over the weekend or on Monday.

2. There was <u>not</u> a German/US bilateral contact yesterday. (Tietmeyer apologised. They are having one next Thursday in Washington (arriving the day before we do). Tietmeyer himself had got confused over the dates).

3. I have had a few trifling verbal suggestions on the draft communique from Trichet: nothing from others yet. Tietmeyer is going to try it out on Gleske (Bundesbank) this weekend and will call me on Monday.

4. I shall report again before close on Monday, since I shall be travelling myself on Tuesday.

GL

(Geoffrey Littler)

Washington

From: Sir G.Littler
Date: 21 September 1987

CHANCELLOR

c.c. Mr Walsh

Governor (B/E)
Mr Loehnis (B/E)

G10 MINISTERIAL: STEERING BRIEF

The meeting is to begin at 8 a.m. on Sunday, 27 September, in the Executive Board Room of the IMF. You will want to finish by as soon as possible after 9 a.m. because the Interim Committee opens at 9-30 a.m.

2. At Annex I is a suggested sequence for steering the meeting, and at Annex II a draft communique.

3. Also annexed is a draft paper by you to be placed on all seats for the meeting - basically the same as what Anthony Loehnis and I circulated to Deputies. We can have this retyped and copied in Washington during Saturday.

GL

(Geoffrey Littler)

STEERING NOTE

Chairman:
- Open meeting.
- Welcome Amato and Greenspan: their first G10.
- Deputies had helpful meeting recently and report by Lamberto Dini has been circulated to save time

ITEM : ADOPTION OF AGENDA:

Chairman:
- Agenda in telex not quite complete: corrected in document on table by addition of two items:
  - draft communique;
  - election of my successor as Chairman.
- Is the agenda thus revised acceptable?
- Invite Dini to add any brief comments (he has promised me to be very brief!).

ITEM : EXTENSION OF THE GAB

Chairman:
- Need a decision at this meeting to enable IMF staff to complete the process of formal extension in time.
- Proposition is simply a further five-year period of the Arrangements as they stand.
- Ask the IMF to confirm that is correct.
- Then need only ask whether any member has any objection or comment?
- If OK, invite IMF to go ahead.

ITEM : ENLARGEMENT OF MEMBERSHIP

Chairman:
- Recall discussion last year when Spain/Australia had sought membership.
- A major problem for several members then seemed to be fear of being unable to stop if once any addition to membership were made.
- Since then of course Austria has formally sought membership also.
- As Chairman I thought it would help our talk if we could construct a defensible set of criteria for membership which would avoid the threat of creeping expansion.
- I can see no way, if we were to admit Austria, of holding the line against some other possible claimants of roughly equal size.

- I have circulated a short note which simply offers a set of possible criteria, and provides what seem to me to be the relevant figures : existing IMF quota shares and existing GNP.

- I suggest there could be a defensive line which could be held, admitting Spain and Australia but no other country, on this kind of basis.

- Invite discussion.

(DEFENSIVE: If suggestion is made that "IMF calculated quotas should be used: Better to stick with the real world of quotas actually used, in combination as I have suggested with the most widely recognised criterion of size - GNP.

ITEM : PREPARATORY EXCHANGE OF VIEWS BEFORE OTHER MEETINGS

Chairman:
- There may be little time available. I think you will have to judge at the time whether to call on the following to offer a perspective:

  - Onno Ruding (Interim Cttee Chairman)

  - Michel Camdessus

- You will want to discourage discussion. If there is discussion I have been warned that Matutes, the Spanish Commissioner, wants to speak favourably on indicators!

- No conclusions at all are expected.

ITEM : DRAFT COMMUNIQUE

- a draft has been prepared by the Secretariat (attached), which will need an addition on extension/enlargement, if decisions are taken.

ITEM : ELECTION OF NEW CHAIRMAN

- It is the turn of Sweden - Mr Feldt.

ANNEX II

Communiqué of the Ministers and Governors
of the Group of Ten

Washington, D.C., September 27, 1987

1. The Ministers and Central Bank Governors of the countries participating in the General Arrangements to Borrow met in Washington on September 27, 1987. The meeting was chaired by the Rt. Hon. Nigel Lawson, Chancellor of the Exchequer of the United Kingdom. The Managing Director of the International Monetary Fund, Mr. M. Camdessus, took part in the meeting, which was also attended by Mr. J.C. Paye, Secretary-General of the Organisation for Economic Co-operation and Development, Sir Geoffrey Littler, Chairman of the Working Party No. 3 of the Organisation for Economic Co-operation and Development, Mr. A. Lamfalussy, General Manager of the Bank for International Settlements, and Mr A. Matutes, Member of the Commission of the European Communities.

2. The Ministers and Governors had a preliminary exchange of views on matters to be discussed in the forthcoming meetings of the Interim Committee and Development Committee.

3. Mr. Kjell-Olof Feldt, Minister of Finance of Sweden, was elected Chairman of the Group of Ten for the coming year.

G R O U P   O F   T E N

(Note by the Chairman)

ENLARGEMENT OF MEMBERSHIP

At a previous meeting concern was expressed whether there could be any way of drawing a line on the admission of members.

As a basis for discussion I offer the following possible guide-lines for a strictly limited enlargement of membership:

1. Group of Ten and GAB membership must be identical.

2. The Group consists of willing industrial countries with the most substantial economies.

3. Economic substance for this purpose can appropriately be measured by gross domestic product and IMF quota shares.

4. Membership should continue to be restricted: new members should not be admitted unless their economies are clearly more substantial than those of the smallest existing members; to qualify they should clearly outrank one or more existing members in both GDP and IMF quota shares.

5. GAB quotas for new members should be settled on the basis of IMF quota shares in relation to those of other members of similar size.

The Annex to this note gives relevant figures.

(Signed) Nigel Lawson

ANNEX

G.D.P., FUND QUOTAS AND G.A.B. MEMBERS' SHARES

	GDP 1986	Fund Quota		GAB Share	
	$ bn	SDR bn	%	SDR mn	%
G.A.B. Members:					
United States	4167	17.9	(20.1)	4250	(25.0)
Germany	890	5.4	(6.1)	2380	(14.0)
Japan	1959	4.2	(4.7)	2125	(12.5)
France	706	4.5	(5.0)	1700	(10.0)
United Kingdom	545	6.2	(6.9)	1700	(10.0)
Italy	504	2.9	(3.3)	1105	(6.5)
Switzerland	134	-	-	1020	(6.0)
Canada	359	2.9	(3.3)	892.5	(5.25)
Netherlands	171	2.3	(2.5)	850	(5.0)
Belgium	111	2.1	(2.3)	595	(3.5)
Sweden	132	1.1	(1.2)	382.5	(2.25)
Total				17000	(100)
Applicants:					
Australia	161	1.6	(1.8)		
Spain	227	1.3	(1.4)		
Other OECD Members:					
Austria	94	0.78	(0.87)		
Denmark	80	0.71	(0.80)		
Norway	69	0.70	(0.78)		
Finland	70	0.57	(0.64)		
New Zealand	26	0.46	(0.52)		
Turkey	59	0.43	(0.48)		
Greece	39	0.40	(0.45)		
Portugal	29	0.38	(0.42)		
Ireland	25	0.34	(0.38)		
Luxembourg	5	0.08	(0.09)		
Iceland	4	0.06	(0.07)		
Other:					
South Africa	62	0.91	(1.03)		

3606/8ic

FROM: J COLENUTT

DATE: 21 September 1987

MR ALLAN

cc Sir G Littler
Sir T Burns
Mr H Evans
Mr Culpin
Mr Walsh
Mr Matthews

AGGREGATE G7 STATISTICS

I have attached a table showing average real interest rates for the G7. Figures for G7 fiscal deficits are shown in the latest World Econmic Developments note.

Alan Colenutt

J COLENUTT
Ext 5548

REAL INTEREST RATES IN G7

~~21/9/87~~

Real Interest Rates in the G7

	Nominal short rate (1)	Inflation Rate (2)	Real rate (3)
UK	10.0	4.4	5.4
US	7.5	3.9	3.5
Japan	3.8	−0.4	4.2
Germany	4.0	0.8	3.2
France	7.9	3.4	4.4
Italy	12.8	4.7	7.7
Canada	9.3	4.7	4.4
Crude average			G7 4.7
			G5 4.1

(1) Three month money market rates, 17/9/87 source: Reuters.

(2) Latest change on 12 months earlier for July (except for Germany

(3) Latest short nominal rates deflated by inflation rate.

3319.66

Prep Washington.

SECRET

FROM: H C GOODMAN

DATE: 21 September 1987

MR PERETZ

cc: Mr Kelly
Mr Polin
Miss McRobbie

BRIEFING FOR WASHINGTON MEETINGS

Your minute of 15 September.

I attach the intervention tables and the charts on exchange rate movements since Louvre prepared by Mr Polin and Miss McRobbie. Both contain information up to close on Friday, 18 September.

H C Goodman

H C GOODMAN

PPS cc Sir G Littler
Sir T Burns
Mr Kelly

Background for the Washington meetings.

DLP 21/9

SECRET

INT 1

SECRET

TOTAL MARKET INTERVENTION ($ TRANSACTIONS) SINCE 23 FEBRUARY PARIS ACCORD

$ million equivalent

FEBRUARY/ SEPTEMBER	(1) US	(2) Japan	(3) W.Germany	(4) France	(5) UK	(6) Rest of EEC Countries		(7) Total EEC Countries
23 FEB 87 TO 18 SEPT 87	4554	17870	1584	5197	16895 *(+15926)	Italy	-1296	
						Spain	10872	
						Greece	36	
						Ireland	1011	
						Denmark	2824	
						Belgium	287	
						Holland	707	
						Portugal	-10	
TOTAL	4554	17870	1584	5197	16895 * (+15926)		14431	38107
% OF TOTAL G5 PLUS OTHER EEC COUNTRIES INTERVENTION	7.5	29.5						63.0

overall total: 60.531 billion

* figure in brackets shows market intervention reported at concertation

note: col (7)=cols(3)+(4)+(5)+(6)
overall total=cols(1)+(2)+(7)

****

Other countries dollar intervention:

Canada	-761
Sweden	1942
Norway	1489
Switz.	455
Total:	3125

INT2

SECRET

TOTAL MARKET INTERVENTION (NON-$ TRANSACTIONS) SINCE 23 FEBRUARY PARIS ACCORD

$ million equivalent

FEBRUARY/ SEPTEMBER	(1) US	(2) Japan	(3) W.Germany	(4) France	(5) UK	(6) Rest of EEC Countries		(7) Total EEC Countries
23 FEB 87				1050 DM	1220 DM	Ireland	-200 DM	
TO					(+884DM)	Belgium	1628 DM	
18 SEPT 87						"	94 Dfls	
						"	191 SwFr	
						"	465 ECU	
						Italy	-5019 DM	
						"	53 ECU	
						Spain	66 DM	
						Denmark	1400 DM	
						Holland	582 DM	
						Portugal	37 £	
						"	34 DM	
						"	11 Ffr	
						"	10 Yen	
						"	6 SwFr	
						"	3 Lira	
TOTAL	0	0	0	1050 DM	1220 DM		-1509 DM	761 DM
					(+884DM)		94 Dfls	94 Dfls
							197 SwFr	197 SwFr
							518 ECU	518 ECU
							37 £	37 £
							11 Ffr	11 Ffr
							10 Yen	10 Yen
							3 Lira	3 Lira

								1631
% OF TOTAL G5 PLUS OTHER EEC COUNTRIES INTERVENTION	0.0	0.0						100.0

Totals:

0.761 billion DM	0.037 billion £
0.094 billion Dfls	0.011 billion Ffr
0.197 billion Swfr	0.010 billion Yen
0.518 billion ECU	0.003 billion Lira

Overall
Total:
1.631 billion

notes: col (7)=cols (3)+(4)+(5)+(6)
overall total = cols (1)+(2)+(7)

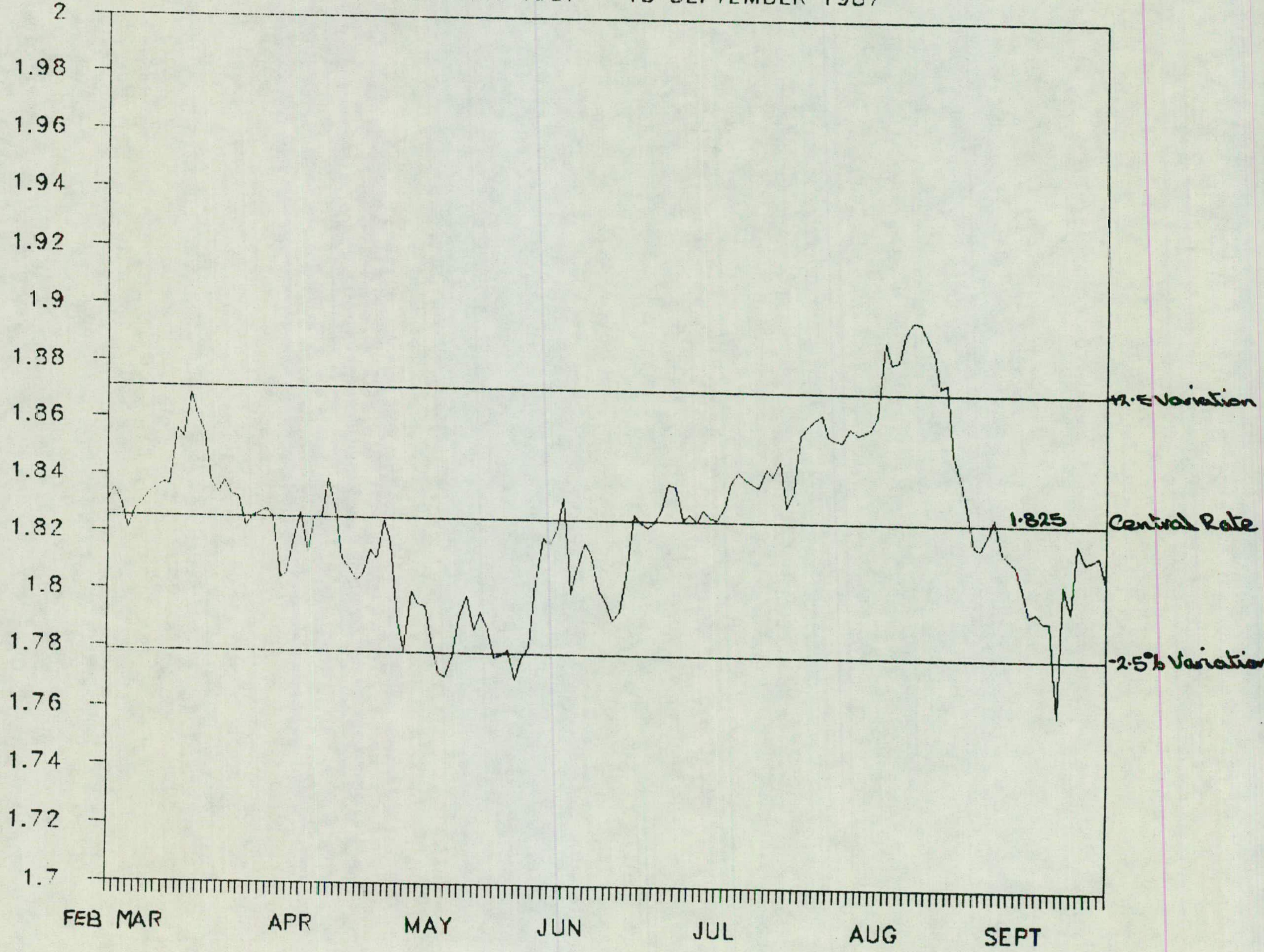
****

Other countries non-$ intervention: Sweden -42 DM

Total : -42 DM

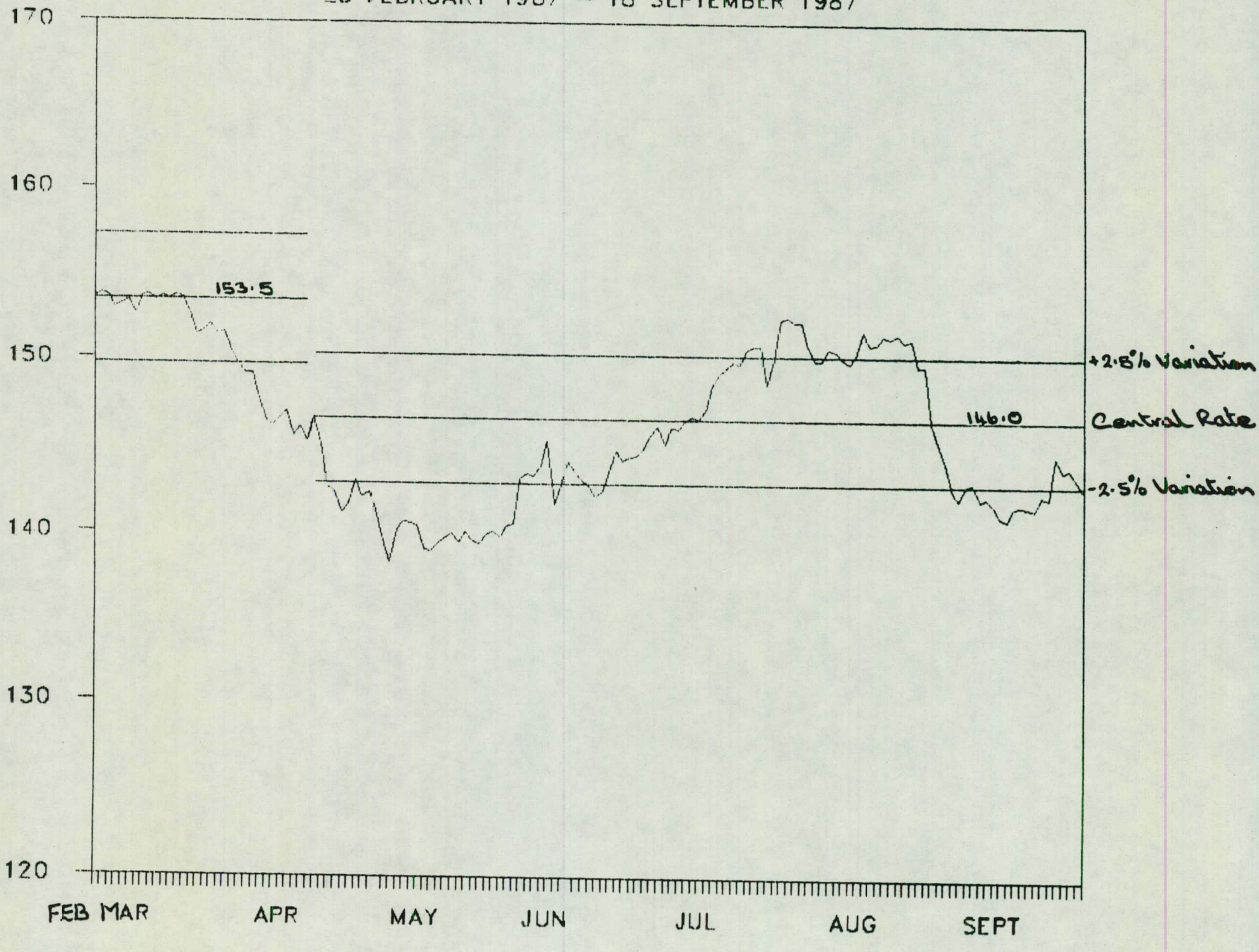
DEUTSCHEMARK DOLLAR

23 FEBRUARY 1987 – 18 SEPTEMBER 1987



YEN DOLLAR

23 FEBRUARY 1987 – 18 SEPTEMBER 1987



SECRET

From: Sir G.Littler
Date: 21 September 1987

CHANCELLOR

c.c. Sir T.Burns
Mr Culpin

DRAFT G7 STATEMENT

I have received only minor comments - not all helpful - from Tietmeyer (already incorporated in my circulated draft), Trichet, Gyohten and Sarcinelli; and a quite extensive redraft from Mulford. The latter is depressing: it removes some of the sense of evolution and progress I had tried to bring in; it carps about German performance; and it highlights indicators!

2. I attach:

- the Mulford draft complete;
- a collation of my earlier draft and all subsequent comments, including Mulford and also including a new paragraph I would like to suggest to reflect your idea of emphasising the global G7 position.

3. This will all be for discussion at a meeting of G5 Deputies at 6 p.m. on Friday. I hope we can go over it in Barbados or on the plane, so that I can get your reactions before that meeting.

(Geoffrey Littler)

S E C R E T

COLLATION OF DRAFTS AND COMMENTS [21 September]

STATEMENT OF THE GROUP OF SEVEN

[The original Littler draft is not underlined: amendments are underlined and the source of them named in bold type]

1. The Finance Ministers and Central Bank Governors of seven major industrial countries met today. This continues the series of meetings in which they have been carrying out surveillance of their economies and gradually developing a stronger and more effective cooperation along the lines agreed at the 1986 Tokyo and 1987 Venice Summit Meetings of their Heads of State or Government.

Mulford: Substitute:

1. The Finance Ministers and Central Bank Governors of seven major industrial countries met today. This continues the economic policy coordination process agreed by their Heads of State or Government at the 1986 Tokyo Summit and strengthened at the 1987 Venice Summit meetings. The Ministers and Governors are convinced that this process[~~which relies on the use of economic indicators,~~] provides an important and effective means of promoting a healthy and prosperous world economy and stable monetary system.

2. The Ministers and Governors reviewed together the evolution of foreign exchange markets, and of events and policies, since the Louvre Agreement. They took satisfaction from the improving quality and techniques of their cooperation in fostering exchange rate stability, and the degree of success achieved [~~over a period in which their efforts have inevitably been on trial.~~]

Tietmeyer (late): "in maintaining exchange rates within fairly narrow limits"

SECRET

Gyohten: ? Delete last phrase: "over a period....." OVERTAKEN

Mulford: Substitute:

2. .... since the Louvre Agreement and the April G7 meeting in Washington. They believe that the greater exchange rate stability which has been achieved has [~~facilitated the strengthening of~~] benefited their policies and performance. OK

3. They are convinced that greater exchange rate stability has been welcomed by traders and investors and has indeed contributed to the renewed strengthening of output which has recently been taking place.

Mulford: Delete whole of paragraph 3. OK

?? **Trichet:** Replace "traders and investors" by "the markets" NOT TRUE!

4. In the light of experience, the Ministers and Governors consider that their judgment earlier this year - that their currencies had come within ranges broadly consistent with underlying economic fundamentals - was and remains valid. They recall that an important part of that judgment was the agreement they reached that the continuing conduct of economic and financial policies must be appropriate and effective.

Mulford: Delete whole of paragraph 4. NO

Trichet: Substitute:

4. In the light of experience, the Ministers and Governors reaffirm their judgment that their currencies are within ranges broadly consistent with underlying economic fundamentals. But ~~their~~ judgment remains subject to ~~their~~ the continuing pursuit of appropriate economic and financial policies.

OK

S E C R E T

5. In the Louvre Agreement the Ministers and Governors set out the policies which they intended individually to pursue, believing them to be consistent, and undertaking to monitor them together and as necessary intensify or adapt them. They note that some important decisions have been taken in individual countries which were foreshadowed in the February statement, and that generally the evolution of policies has been along the lines intended.

Gyohten: ? Delete: "believing them to be consistent" OK

6. Some important favourable effects are beginning to be seen: the sharp reduction in fiscal 1987 in the United States federal budget deficit is a welcome step towards necessary adjustment; the major programme of additional expenditures in Japan is being rapidly implemented; in Germany the reductions in income taxes from 1988 are to be substantially greater than previously planned; there has been a welcome revival of domestic demand in the surplus countries whose currencies had sharply appreciated; and further steps have been taken in the direction of liberalisation and structural change. External imbalances remain high, but there have been quite strong reductions in them in real terms and growing indications that they are now diminishing in dollar terms.

Trichet: Delete last phrase: "and growing indications...."

Gyohten: Insert in Japan sentence: "and income tax cuts" ✓

Sarcinelli: The draft is too optimistic. Suggest it could be toned down by deleting "sharp" in second line and deleting "rapidly" in fifth line.

Mulford: Substitute for whole paragraph:

and income tax cuts

6. Some important favourable results are beginning to be seen although problems remain. The ~~sharp~~ Significant reduction in fiscal 1987 in the United States federal budget deficit is a welcome step as is the continued success in resisting protectionist pressures. The major programme of additional expenditures in Japan is being rapidly implemented. In Germany the reductions in income taxes from January 1988 are greater than previously planned. External imbalances remain high, although there have been reductions in real terms and growing indications that they will be diminishing in dollar terms. Growth in domestic demand in some surplus countries is picking up, although it remains below the levels that had been expected earlier.

OK as is

Littler: Insert new paragraph as follows:

6A. The Ministers and Governors studied not only the economic relations between their own countries, but also the overall impact of their policies taken together ~~on the world economy as a whole~~. They consider that the balance of their policies is satisfactory: in particular they judge that their overall monetary stance is appropriate to contain inflation while giving room for further sustained growth.

OK as is

Tietmeyer (late): large trade surpluses ✓

7. The Ministers and Governors note that the [~~successful trade performance~~] of some newly industrialised economies continues to be an important factor contributing to external imbalances and they repeat their view expressed on earlier occasions that these economies should reflect their growing importance and responsibilities by reducing trade barriers and pursuing policies

that allow their currencies to reflect more fully underlying economic fundamentals.

8. The Ministers and Governors are satisfied that they correctly identified the appropriate directions of policy in the Louvre Agreement. The continuing task in carrying forward their agreement and cooperation together is now to develop and intensify the appropriate policies in each of their countries ~~as necessary~~.

Trichet: Insert "main" before "appropriate" No!

Mulford: Delete last two words: "as necessary" ✓

9. The Ministers and Governors ~~commit~~ recommit themselves ~~again~~ to the directions of policy set out in the Louvre Agreement and expect to take further measures in accordance with them over the coming months. In particular:

- the Government of the United States expresses its determination to carry further ~~in fiscal 1988~~ the progress already achieved in reducing the federal budget deficit and to continue to resist protectionist action which can only damage the interests of all;

Trichet: Insert "the same" after "fiscal 1988"

- the Governments of the Federal Republic of Germany and Japan reassert their commitment to continue to foster steady growth of domestic demand and thus encourage reduction of external surpluses;

(Tietmeyer late) ✓

Mulford: Substitute:

OK if Nig'll wear it, wh I v. much doubt (Cutting Grow)

- the Government of Japan will continue to foster a reduction of external surpluses by implementing monetary and fiscal policies which will provide as much stimulus to the economy in fiscal 1988 as is occurring in the current year.

- the Government of the Federal Republic of Germany will take additional monetary and fiscal actions to increase domestic demand and reduce its external surplus due to growth which is slower than expected earlier.

OK

- the Governments of each of their countries will continue to pursue liberalisation of markets, tax reforms and other structural changes to maximise the scope for a high rate of sustained non-inflationary growth.

Mulford: Amend first two lines to read:

OK

- the Governments of each of their countries will intensify their efforts to liberalise markets, implement tax reforms and

Gyohten: Amend last three lines to read:

Better now, but acceptable if necessary

to pursue structural changes to maximise the scope for a high rate of sustained non-inflationary growth and to attain better external balances

During the coming year the developments of their economies will be monitored ~~increasingly~~ closely under the surveillance arrangements outlined in the Venice Summit.

Mulford: Delete these three lines, (but see below, para 10). OK

Gyohten: Delete the word "increasingly" OK

Trichet: Substitute the following:

The developments of their economies will be monitored increasingly closely under the surveillance arrangements based on a set of indicators outlined in the Venice Summit. NO

Sarcinelli: Insert new paragraph as follows:

9A. The Ministers and Governors reiterate that ~~while~~ monetary policies should ~~continue to be orientated towards fighting inflation, they should also~~ take into account the need for maintaining appropriate interest rate differentials to ensure exchange rate stability ~~and smoothe capital flows. Orderly monetary conditions in international markets will certainly be helpful in managing the situation according to the agreed strategy.~~

No harm — & perhaps some good — if cut down thus

SECRET

10. The Ministers and Governors intend to carry forward their cooperation in fostering exchange rate stability and to develop further in the light of experience the range of techniques and the resources available to them. This will be a continuing process. In the immediate future they aim to strengthen their cooperation in the management of monetary policies, [and their central banks will be broadening the existing network of swap arrangements in each other's currencies.] Pöhl. — strongly disagree. We must try & stick the fact, & if we do it gets featured in the communiqué!

Gyohten: Warns that reference to monetary policies may cause difficulties.

Mulford: Substitute for whole of the paragraph:

OK subject to X & Y

10. The Ministers and Governors intend to carry forward their economic policy coordination efforts. During the coming year the developments of their economies will be monitored increasingly closely under the strengthened surveillance arrangements outlined in the Venice Summit. In light of the progress achieved to date in laying the basis for a reduction of imbalances, and the [further progress envisaged] ~~additional actions which are planned,~~ the Ministers and Governors consider that currencies remain within ranges broadly consistent with underlying economic fundamentals. They reaffirmed their commitment to continue to cooperate closely to foster the stability of exchange rates. Add swap sentence.

X

Y

NB What?

Gyohten: No objection to draft, but will need to know what we mean by reference to techniques.

Spare

SECRET

From: Sir G.Littler
Date: 21 September 1987

CHANCELLOR

c.c. Sir T.Burns
Mr Culpin

DRAFT G7 STATEMENT

I have just had a few additional comments on my original draft from Tietmeyer, reflecting a talk with Poehl. They are:

On paragraph 2: Delete last phrase "over a period...." and substitute: "in maintaining exchange rates within fairly narrow limits".

On paragraph 7: Delete "successful trade performance" and substitute: "large trade surpluses".

On paragraph 9 (Germany): Expand last phrase to read: "domestic demand and thus encourage further reduction".

On paragraph 10: Poehl wants the reference to expanded swap arrangements deleted.

2. He had two other points from Stoltenberg:

- like you, Stoltenberg found a lack of ringing declaration that Louvre still lives (but neither Hans nor I has yet seen the best way to remedy this): perhaps opening of para 10, where he thought "intend to" was weak.
- he is worried about the naming of only 3 countries in para 9, and is fishing for an indent for each country.

(Geoffrey Littler)

Washington

SECRET

From: Sir G.Littler
Date: 21 September 1987

CHANCELLOR

c.c. Sir T.Burns
Mr Culpin

DRAFT G7 STATEMENT

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Marked on text below

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(Geoffrey Littler)