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 Euro Pol: Monetary Rep, Mr. Stone
 Rpt. Bremen Euro Council - Policy, May '78,

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Prime Minister

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TO PRIORITY FCC TEL NO 518 OF 22 JUNE
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GISCARD/SCHMIDT MEETING, 23 JUNE - MONETARY ASPECTS

1. FRENCH PRESS REPORTS SUGGEST THAT A KEY TOPIC AT THE BILATERAL HAMBURG SUMMIT WILL BE EUROPEAN MONETARY MATTERS. PRESIDENT GISCARD AND HERR SCHMIDT WILL LOOK FOR COMMON GROUND ON THIS BEFORE THE BREMEN AND BONN MEETINGS, AS THEY DID BEFORE COPENHAGEN. THE AIM WOULD BE TO PROMOTE AGREEMENT AT BREMEN ON THE OUTLINES OF A NEW EUROPEAN MONETARY SYSTEM, WITH DETAILS AND TIMETABLE TO BE WORKED OUT LATER.
2. WITHIN THE FRENCH GOVERNMENT, THE FOLLOWING VIEWS ARE EXPRESSED ON THE ECONOMIC IMPACT OF NEW MONETARY ARRANGEMENTS:-
 - (A) INSTABILITY BETWEEN EEC CURRENCIES WAS THE CAUSE OF LOWER GROWTH LAST YEAR IN EUROPE THAN IN THE UNITED STATES OR JAPAN, HENCE THE NEED, IN PRESIDENT GISCARD'S WORDS, TO CREATE "A ZONE OF MONETARY STABILITY IN EUROPE".
 - (B) MONETARY ARRANGEMENTS WILL ONLY BE EFFECTIVE IF BACKED BY CLOSER CONVERGENCE BETWEEN THE PERFORMANCE OF THE EUROPEAN ECONOMIES, ESPECIALLY ON INFLATION RATES. THIS IS M. BARRE'S STATED VIEW.
 - (C) INFLATION IN FRANCE WILL BE ABOVE THE EEC AVERAGE FOR THE REST OF THIS YEAR, AND THERE IS A RISK OF DOWNWARD PRESSURE ON THE FRANC IN THE LATTER MONTHS. HENCE FRANCE SHOULD UNDERTAKE NO NEW NATIONAL COMMITMENT ON EXCHANGE RATES AT LEAST UNTIL AFTER THE END OF 1978. THIS VIEW IS HELD BY M. MONORY, THE ECONOMICS MINISTER, AND HIS OFFICIALS, AS WELL AS IN THE BANK OF FRANCE.

Pace misshy

3. ON TECHNICAL ASPECTS, FRENCH OFFICIALS ARGUE:-

- (A) A RETURN TO THE EXISTING SNAG OR SOMETHING LIKE IT WOULD NOT BE TOLERABLE. THE FRENCH FRANC HAS ALREADY BEEN FORCED OUT TWICE.
- (B) NEW ARRANGEMENTS SHOULD INCLUDE ALL COMMUNITY CURRENCIES ON EQUAL TERMS, WITHOUT SEPERATE RULES FOR THE SNAG MEMBERS.
- (C) OBLIGATIONS TO INTERVENE TO DEFEND EXCHANGE RATES SHOULD BE MATCHED BY GREATLY INCREASED SUPPORT FACILITIES, INCLUDING, IF POSSIBLE, POOLING OF RESERVES.
- (D) MAXIMUM USE SHOULD BE MADE OF THE EUROPEAN UNIT OF ACCOUNT (EUA) BOTH AS NUMERAIRE AND IN THE INTERVENTION OPERATIONS.

PART OF THIS WAS REFLECTED IN WHAT M. MONORY SAID AT THE EEC FINANCE COUNCIL ON 19 JUNE.

4. PRESIDENT GISCARD HIMSELF, HOWEVER, HAS NOT YET FULLY REVEALED HIS THINKING, EVEN TO HIS CLOSEST ASSOCIATES. WE ARE TOLD THAT HE FAVOURS THE TECHNICAL APPROACH OUTLINED IN THE PREVIOUS PARAGRAPH, BUT REGARDS HIS OFFICIAL ADVISORS AS TOO CAUTIOUS. HE HAS SAID PUBLICLY (MY TELNO 26 SAYING) THAT HE HAS GOOD REASONS TO THINK THAT PROGRESS WILL BE MADE AT BREMEN.

5. DUTET ON PRESIDENT GISCARD'S STAFF HAS EXPRESSED THE VIEW THAT NEW MONETARY ARRANGEMENTS, LINKING THE DM AND WEAKER EUROPEAN CURRENCIES, WOULD TEND TO HOLD DOWN THE DM AND REDUCE THE INCENTIVE FOR THE GERMANS TO MAKE THEIR ECONOMY GROW FASTER. THE PROGRAMME OF CONCERTED ACTION COULD BE USED TO COUNTERACT THIS TENDENCY. THOUGH THE FRENCH WOULD NOT SAY SO IN PUBLIC, THEY WERE ONLY PARTLY CONVINCED BY GERMAN ARGUMENTS THAT FURTHER STIMULUS OF THEIR ECONOMY WOULD BE FRUITLESS: THEY STILL BELIEVED THAT THE GERMANS COULD DO MORE. THE FRENCH OBJECTIVE AT BREMEN COULD THEREFORE BE TO SEEK AGREEMENT ON LAUNCHING A NEW MONETARY SYSTEM, WITH DETAILS TO BE WORKED OUT IN THE COMING MONTHS, AND WITH ITS PHASED INTRODUCTION TIED TO PROGRESS ON THE MEASURES OF ECONOMIC STIMULUS. IF THESE FELL BEHIND SCHEDULE THE MONETARY MOVES WOULD ALSO BE SLOWED DOWN. BUT HE MADE IT CLEAR THAT HE COULD NOT FORCAST THE LINE WHICH PRESIDENT GISCARD WOULD TAKE OR HOW HE WOULD REACT TO WHAT HERR SCHMIDT PROPOSED.

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6. MY INCLINATION IS TO BELIEVE THAT GISCARD WILL WISH TO GO ALONG WITH SCHMIDT. THE FACT THAT THE BRITISH DO NOT AGREE WILL NOT AFFECT HIM. I WOULD THEREFORE EXPECT A SCHMIDT/GISCARD LINE-UP ON THIS, WHATEVER CAUTIOUS NOISES THE OFFICIALS IN THE TWO COUNTRIES MAY BE MAKING.

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