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NOTE OF THE PRIME MINISTER'S DISCUSSION WITH THE PRIME MINISTER
OF ITALY, SIGNOR ANDREOTTI, AT 10 DOWNING STREET ON 15 JUNE, 1979,
AT 1130

Present:

Prime Minister

Signor Andreotti

Foreign and Commonwealth
Secretary

Signor Forlani (Minister of
Foreign Affairs)

Mr. B.G. Cartledge

Signor Catalano (Deputy
Diplomatic Adviser)

Mr. Antony Leydon
(Interpreter)

Signora Civelli

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Situation in Italy

Welcoming Signor Andreotti, the Prime Minister said that she was very glad that he had been able to spare the time to come to London for a discussion of the forthcoming European Council Meeting at Strasbourg, and of what they both hoped to achieve there. She would like to hear from Signor Andreotti what the next steps would be following his great success in the Italian Election against the Communists. Signor Andreotti said that he now had to form a coalition government. He hoped that the two parties in the government at present would provide the basis for constructing a stronger combination. The major difficulty at present was to secure the cooperation of the Socialist Party. Even the three parties in combination would still fall 20 votes short of an overall majority, and he was therefore obliged to seek agreements with other parties as well. He also faced problems with the trade unions, but hoped that the current negotiations with them would be complete before the end of the summer.

/The Prime Minister

CONFIDENTIAL

CONFIDENTIAL

- 2 -

The Prime Minister asked Signor Andreotti about the percentage of trade unionists in the Italian workforce. Signor Andreotti replied that he would like to make two points on the trade unions. The first was that during the past three years the trade unions had worked quite well with the government during the country's most difficult moments, for example during the negotiations with the IMF and at the time of heavy speculation against the Lira. It was also true that the number of working hours lost through strike action had fallen by two-thirds during the same period, largely because of cooperation on the part of the unions. Signor Andreotti said that this was partly due to the fact that the government had been in a minority in Parliament, and had depended on the Parliamentary support of the Socialists and the Communists. It was noticeable that since December, when the Socialists and Communists had withdrawn from the government, the level of strike action had increased (although this could be attributed in part, also, to the beginning of the period of wage negotiations). Secondly, trade union membership had fallen significantly, mainly because many workers were unwilling to pay their contributions.

Community Budget and the CAP

The Prime Minister told Signor Andreotti that she had seen reports of his press interview on the previous day, and had been encouraged by the fact that he was in agreement with so much of what the British Government would wish to say at Strasbourg. She wished Signor Andreotti to know that there was a great difference between the present Government's approach to Europe and that of the last Government. The present Government believed positively in the European ideal: the UK would not be able to go ahead except as a member of Europe. Britain's membership of the EEC was the best solution for this country, and the best for Europe as well.

/The Prime Minister

CONFIDENTIAL

CONFIDENTIAL

- 3 -

The Prime Minister said that she and her Ministers were wholly devoted to the cause of Europe, and for that reason would do everything possible to make the European ideal work and to cooperate to the greatest possible extent on all issues. This would not, however, prevent the Government from fighting their corner on matters which gave rise to problems for the UK, such as the Community Budget, Common Agricultural Policy and Fisheries. The problem lay in how to make progress on these issues without seeming to be anti-European. The Prime Minister said that she wished Signor Andreotti to know that the sooner progress could be made on these issues, the sooner the Government could convert the British people to the European ideal. The present budgetary arrangements were unjust; they had to be made just and reasonable. The Government did not, however, wish this issue to dominate the discussions at Strasbourg; what they wanted was progress so that the Community could move on to talk about other matters.

Signor Andreotti said that his total experience of five years as Prime Minister had taught him that it was possible to raise problems at European Councils but not to achieve solutions of them without slow and gradual preparation. The aim at Strasbourg, therefore, should be to have the problems set out clearly, and agreement reached on the procedure for solving them, a procedure which could perhaps involve the Commission. The Prime Minister told Signor Andreotti that when the President of the Commission had called on her three weeks ago, she had raised the problem of the Community Budget with him, and she now had from the Commission an agreed statement on the effect of the budgetary arrangements on each member, according to each of the possible ways of attributing the MCAs, and also showing what the position would be in 1980 when Article 131 would no longer apply. The facts, therefore, should not be in dispute. The Prime Minister said that she was averse to arguing with her colleagues about the facts when these were readily ascertainable.

/Mr. Jenkins

CONFIDENTIAL

CONFIDENTIAL

- 4 -

Mr. Jenkins had suggested to her that when she met President Giscard, as President of the Council, she could obtain his agreement to putting the problem of the Budget on the Agenda for Strasbourg, on the basis of securing the Council's agreement on the facts and giving firm instructions to the Commission to come forward with possible solutions to the problem at the Council's next meeting. During her talk with President Giscard in Paris, therefore, she had adopted this approach, and had recognised, in the light of the discussion, that the UK's task would not be an easy one. The UK had subsequently experienced some difficulty in arranging for the Budget question to be given a reasonably high place on the Strasbourg Agenda. The Prime Minister said that she was nevertheless determined to achieve the result that the Commission would be instructed to produce solutions. She did not underestimate the difficulties, because she was aware that not all members of the Community accepted that the present arrangements were unjust. The fact was, however, that only an unjust system could produce such unjust results, and the system must therefore be changed. Both Italy and the UK were paying more than their fair share in their net contribution to the Budget. Fairness between the partners was essential in any enterprise which was to have a thriving future. Signor Andreotti said that he believed that the first essential was to avoid any worsening of the present position. In particular, a rise in agricultural prices would increase expenditure since agriculture would take up an even greater share of the Community's Budget. The European Council had sometimes spent days at a time debating whether the Regional Fund should be increased, whereas expenditure on agricultural surpluses amounting to five or six times more in cost were passed through without any difficulty. There were two further difficulties concerning surpluses. The first was that the Community usually ended up by selling them at artificially low prices to, for example, the Soviet Union after first incurring all the expense of supporting them;

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CONFIDENTIAL

CONFIDENTIAL

- 5 -

the surpluses should be consumed in the Community itself, instead of which the members of the Community were paying twice over. The second difficulty was that under the present system instructions were given from time to time to destroy fruit and vegetables as a result of EEC regulations. This caused a serious psychological problem as far as poor people in Italy were concerned, particularly since these products were of so much greater concern to Italians. Italy wished to change the rules which produced this result.

Signor Andreotti went on to say that in his view the first essential was to find a way of avoiding agricultural surpluses, thereby reducing the cost of the CAP and the burden on the Community Budget. He had some confidence in the quasi-liberal economic thinking of Chancellor Schmidt in the FRG; but he knew that Denmark, Ireland, and probably the Netherlands, all of whom benefited from the present arrangements, would cause difficulties for Italy and the UK.

Signor Andreotti said that the problem of Mediterranean products was naturally of particular concern to Italy. In order to help countries like Cyprus, the Community frequently gave Mediterranean products less protection than others. He understood the reasons for this, but it was always at Italy's expense; in the Tokyo round, for example, there had been a great deal of discussion of reductions in tariffs on fruit and tomatoes, but no mention of similar reductions for meat and dairy produce. Italy had been able to achieve some minor changes, but in general she had a raw deal on this issue. Signor Andreotti said that Mediterranean agriculture was far more important to Italy than the discrepancy between what they contributed to the Budget and what they got back in return; for the UK, however, the opposite was true. But the situation for the two countries was in reality two sides of the same coin and of the problem of securing

CONFIDENTIAL

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CONFIDENTIAL

- 6 -

greater justice as between those who were doing well out of the system and those who were not. Signor Andreotti said that if the UK and Italy were to have a common platform, Italy was obliged to seek the UK's support on the problem of Mediterranean products.

The Prime Minister said that on the question of surpluses, President Giscard had suggested - and she was not sure to what extent this had already been discussed in the Community - that surpluses should be financed by the countries creating them and not under the CAP. Lord Carrington pointed out that President Giscard was in fact referring to future surpluses. He went on to say that, so far as Mediterranean produce was concerned, the balance of power in the Community could well shift when Spain and Portugal join Greece in the enlarged EEC.

Signor Andreotti acknowledged that if each member country had to accept responsibility for its own surplus, there would be no problem. Given the mechanism under which the CAP operated at present, however, this simply did not happen, because Community intervention to bridge the gap between prices realised and the fixed price was automatic. To achieve the result President Giscard had in mind, therefore, the rules for the CAP would have to be changed. The present system stimulated the increased production of, for example, dairy products in the FRG by the payments which it provided to German farmers. Production plans were needed, although there would have to be a degree of elasticity in them to take account of years of bad weather and other factors: but the objective should be to avoid stimulating the production of surpluses which created an increasing burden on the Community Budget.

Reverting to the question of Mediterranean products, Signor Andreotti said that the EEC had agreements with the

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CONFIDENTIAL

CONFIDENTIAL

- 7 -

countries of North Africa and with Israel which had adverse consequences for Italy. The Community absorbed only 7 per cent of Italy's production of citrus fruits; the remainder was consumed in Italy itself or exported elsewhere, which was difficult. By contrast, 80 per cent of Italy's consumption of meat and dairy produce was imported from within the EEC. This imbalance had to be corrected. Signor Andreotti recognised that, with the accession of Spain in prospect, years of preparation would be needed to secure the necessary adjustments. There was no need for Italy to suffer damage as a result of the enlargement of the Community which, indeed, Italy supported on political grounds.

The Prime Minister asked Signor Andreotti how long he had been seeking readjustments for Mediterranean products; it was clearly unlikely that results could be achieved on this between the Strasbourg and Dublin Meetings of the European Council. Signor Andreotti replied that Italy had begun the battle several years ago. Some results had been achieved, for example in winning from the Community a contribution towards the conversion of citrus fruits into fruit juice, which could be exported over a longer period and at a higher profit. The EEC had also contributed to agricultural production in Southern Italy - the so-called Mediterranean package. These were, however, modest achievements and they had taken two years to secure. Signor Andreotti said that he thought that Italy and the UK could work together and thereby achieve results. The problem, however, lay in convincing the other members that something had to be done. The other members had to realise that sacrifices would be necessary. At the same time, it was necessary to avoid creating a crisis in the Community. A crisis could come about since on questions of this kind, involving economic interests, ^{members} were inclined to adopt rigid attitudes; in the Netherlands, for example, attitudes towards the CAP remained constant as between Socialist and Conservative governments. A long and difficult negotiation

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CONFIDENTIAL

CONFIDENTIAL

- 8 -

would be needed, but, Signor Andreotti repeated, results could be secured.

The Prime Minister said that the UK would need results very quickly, since domestic political problems could otherwise arise. In 1980, the UK's net contribution to the Budget would increase enormously: the British Government could not afford to wait until the 1 per cent maximum of VAT was reached. The Government's opponents had concentrated so much on the Budget as the test of whether EEC membership was beneficial to the UK that it would be impossible to tolerate the status quo for a further two years or so. The Government had to solve two problems: the Budget itself and the CAP, which was to a large extent responsible for the Budget's size. Unless movement could be secured very soon, the Government would be in grievous political and financial difficulty. Lord Carrington said that the present situation could upset the Government's whole economic strategy. The UK could not hope to become a constructive member of the EEC for so long as her economy remained weak. It was difficult to achieve economic recovery while the enormous burden of the UK's net budgetary contribution remained.

Signor Andreotti said that the simple solution might be to establish the principle that only those countries with GNPs lower than the EEC average would qualify for a net repayment from the Budget. Psychologically, however, it might be easier to arrange a system whereby net repayments, or a proportion of them, were not given back directly to the national budgets of below-average GNP countries but to the Regional Fund or to the financing of large-scale projects in the country concerned, thus achieving a saving for the national budget. A solution on these lines might be more readily accepted by the EEC members. Signor Andreotti said that he did not by any means exclude the more direct arrangement but thought that something on these lines would be more

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CONFIDENTIAL

CONFIDENTIAL

- 9 -

acceptable. The Prime Minister commented that although the result might be the same in terms of budgetary figures, the destination of the repayments would be different: the total repayments would not necessarily come back to any particular poorer country. Signor Andreotti agreed that it would be simpler to establish a system of progressive budgetary contributions, analagous to national income tax; but because of the EEC mentality, it would be more difficult to win acceptance for such a novelty over a short period.

The Prime Minister said that a system such as Signor Andreotti had proposed would create some difficulties for the UK, since the degree of the UK's over-payment to the Budget was about to become so great that a solution on these lines could not cope with it. It was also essential that a government should have some direct control over the net refund. The British Government, for example, would wish to use any repayment in order to stimulate the UK economy, rather than acquiescing in the use of the money to prop up dying industries in Europe. Lord Carrington said that the current scale of the budgetary imbalance was such that, although he entirely accepted Signor Andreotti's view that the problem of the CAP had to be resolved by an adjustment in expenditure, the budgetary problem demanded a more radical solution. The difficulty was that, if the UK were to pay less, others - for example, the FRG - would have to pay significantly more.

The Prime Minister told Signor Andreotti that the problem was to secure some movement. She was less patient than he was and did not wish to discuss the problem three times a year without achieving any action. Action was needed at the next European Council: the problem was, how to secure it? Signor Andreotti remarked that the novelty of the Prime Minister's presence in the European Council might give a jolt to the Council's methodology, or what he would call "European Conservatism". It was important that there should be adequate

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CONFIDENTIAL

CONFIDENTIAL

- 10 -

preparation and that the European Commission should be instructed in such a way as to pave the way for decisions at the following meeting of the Council. It was also necessary to work round the flanks, in other words to engage in systematic bilateral discussion. European Council meetings were not always the best occasions for actual decisions.

EMS

Signor Andreotti recalled that the Italian Government had decided in December to join the EMS and had nearly been brought down as a result. His Government had, nevertheless, thought it right to join in order to demonstrate its European will and also because membership of the system had obliged the Government to adopt more rigid internal and monetary policies. The results so far had been favourable. Signor Andreotti asked what the British Government's attitude now was towards the EMS. The Prime Minister said that the Government was reviewing the question of the UK's relationship with the EMS and would be prepared to announce the results of their preliminary review before September. The Government would probably wish to allocate some of the UK's reserves to the EMS. At present, however, sterling was at a level well above the EMS ceiling, partly because North Sea oil was keeping the exchange rate above what would be justified by the UK's economic performance, and also because of the recent increase in the MLR to 14 per cent. The deposit of some UK reserves in the EMS would, however, serve as a declaration of faith in the UK's intention to join the system. The Prime Minister asked Signor Andreotti whether membership of the EMS had obliged the Italian Government to adopt tougher policies on money supply and inflation than they would otherwise have done. Signor Andreotti said that his Government had already planned an austerity programme before joining: but membership of the EMS made it easier to put this programme into effect since everybody knew that such measures had to be taken as a result of Italy's participation in the scheme.

/ The Prime Minister

CONFIDENTIAL

CONFIDENTIAL

- 11 -

The Prime Minister said that the British Government, too, was prepared to be very tough on inflation. Some exchange controls were being relaxed, in order to release UK investment to Europe. This was one way of gradually bringing the exchange rate down: money would be able to enter and leave the UK on more equal terms than before.

Signor Andreotti said that, when his Government had taken over, Italy's rate of inflation had stood at 23 per cent. The Government had got it down to 13.4 per cent and was determined to keep it there.

Energy

Signor Andreotti said that energy would be high on the Agenda at Strasbourg. Each member country of the Community had a different situation so far as energy was concerned: the UK had oil, the FRG coal, while Italy had nothing. It was essential to try to produce some concrete decisions at Strasbourg. It was no use simply declaring that energy consumption should be reduced by 5 per cent, and then leave it to member countries, with all their differences in resources, to carry out this prescription. It would be much better if the European Council could agree, for example, that all petrol stations in the EEC should be closed on Saturdays and Sundays. If all members were to subscribe to such a decision, it would be easier for each country to accept it. The problems of nuclear energy, as well, could be more easily tackled on a Community basis.

The Prime Minister said that she was not in favour of the weekend closing of petrol stations since this would discriminate against those who were obliged to work on Saturdays and Sundays. Each country would develop a different means of achieving the common objective. The Prime Minister said that she was more concerned by the nuclear energy issue: Europe would have to replace its coal and oil by nuclear power but there had been insufficient preparation of the public case

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CONFIDENTIAL

CONFIDENTIAL

- 12 -

for this. People had to be reminded that uranium was just as much God-given as the sun and the waves. If Europe could not be brought round to favour nuclear power, the whole economic future of the Community would be in jeopardy. Italy, like France, had taken some very far-sighted decisions. The Prime Minister and Signor Andreotti agreed that Chancellor Schmidt's proposals on nuclear safety were helpful and should be pursued.

The discussion ended at 1315.

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15 June 1979

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