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By JR NARA Date 3/30

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CLASSIFIED BY FRANK WISNER
SUBJECT: GENERAL DECLASSIFICATION
MEMORANDUM OF CONVERSATION SCHEDULE OF EXECUTIVE ORDER 11652
AUTOMATICALLY DOWNGRADED AT TWO-
YEAR INTERVALS AND DECLASSIFIED ON
DECEMBER 31, _____

PARTICIPANTS: U.S. SIDE

The Secretary
Mr. Rogers, Under Secretary for Economic
Affairs
Mr. Sonnenfeldt, Counselor
Mr. Hartman, Assistant Secretary for
European Affairs
Mr. David Passage, Notetaker

BRITISH SIDE

Mr. Harold Lever, Chancellor of the
Duchy of Lancaster
Sir Peter Ramsbotham, British Ambassador
Mr. Ulrich, Assistant to the Chancellor
Mr. William Ryrie, Minister for Financial
Affairs, British Embassy

CONFIDENTIAL

SUBJECT: UK Economic Situation
DATE/TIME: 8:15 a.m., November 15, 1976
PLACE: Breakfast, Secretary's Dining Room
DISTRIBUTION: S, S-R.W.Aherne, NSC - P.Rodman.

Kissinger: (Entering the dining room) You know, of course, Harold, I could produce total panic among my colleagues by pretending to understand anything about economic affairs or implying that I might become involved in them.

Lever: (Continuing conversation that began outside about Harold Wilson) The relationship with Harold Wilson was a kind of strange one. He used to go sailing with me and once I nearly drowned him. In my association with him he had two very narrow escapes. The first was when I nearly drowned him while we were out sailing, and the second was when I very nearly nominated him for the directorship of the International Monetary Fund.

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Kissinger: When was that?

Lever: In 1973.

Kissinger: I must say, I met Harold Wilson in the fall of 1973 and he didn't particularly make a good impression on me.

Sir Peter: I remember that fortnight in 1974 when you were enroute to Damascus and stopped over in London and met Ted Heath. Heath had just demonstrated considerable skill and courage in putting together his parliamentary majority.

Kissinger: Yes, it's true. He was almost boasting that he thought he was going to be able to run the government with only a majority of eight. Then that afternoon Scotty Reston lacerated him and things went downhill from then on. It is very interesting about Heath. If there was one foreign leader for whom President Nixon had very high regard, it was Ted Heath. I remember once I was in Mexico City. I think I was watching a world cup match on television. Nixon called me at least four times -- each time over the open phone. Every intelligence system in the world must have been tapping into that line. But he had apparently just had a call from Heath, and he was as elated as could be. Heath could have called him with the weather report and Nixon still would have been elated.

Lever: Heath was a rather strange and even a curious leader.

Kissinger: I think he is one of the ablest men in British politics.

Lever: I think he is probably better now than he was when he was in office.

Kissinger: (ending the chit-chat and beginning a serious conversation) I want you to know I am very flattered at being consulted at all on economic affairs. There are many people in Washington who tremble at the thought of my becoming involved in such issues as monetary policy.

Lever: There is absolutely no reason for you to be, Mr. Secretary. Let me recount to you an anecdote which may tell you more about my feeling regarding your mastery of economic affairs than anything else I could tell you. It

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was one morning at home and I was having breakfast with my wife. I was reading an article written by you on foreign affairs and I said to my wife, "Do you know Henry's views on foreign affairs precisely coincide with my concept of international monetary affairs." So I want you to know when Jim (Callaghan) asked me to come over to speak to you on these things, I had a certain confidence which might not otherwise have been present.

Kissinger: Before we start into this in seriousness, I want you to know that I have no authority to agree or to disagree with any of the proposals which you may be making. I know you will be seeing Simon and the President and Arthur Burns. My interest in this, however, is to understand enough so that I can argue sensibly for the foreign policy concerns that the United States must have, as we try to find a way to help Britain in the present crisis.

Lever: Oh, my dear Secretary of State, you're totally exculpated. I too have no authority to negotiate or reach any agreements. In fact, talk about having no authority, virtually all of the departments of our government trembled at the thought of me going off to Washington and the possibility that I might burst into song in my terrible ignorance.

Kissinger: If I might ask one question before you begin, may we take it that what you are saying while you are over here represents the Prime Minister's views?

Lever: Yes. The views that I represent here can be fairly described as those not only of the Prime Minister but also of the Cabinet. These are thoughts which have been thoroughly discussed and on which there is a Cabinet consensus. I have been very clearly instructed to engage in no frivolous remarks of my own. (laughter)

Kissinger: (turning to Sir Peter) Should I ask him whether he has Cabinet approval?

Sir Peter: (laughter)

Kissinger: Pay no attention; that was simply an in-joke. It has absolutely nothing to do with your mission but rather relates to an exchange between Tony (Crosland) and me over the degree of Cabinet sanction for the scheme we had worked out to fund the arrangements for settlement in Rhodesia.

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Lever: Let me begin by making a simple point. There appears to be a fundamental misunderstanding in America about the United Kingdom's economic problems. The common attitude in this country seems to be that we've been here before, but it is wrong. Taken in its historical perspective, it is true that the United Kingdom has lost the position that it once enjoyed in the world. The question for us as a country is can the United Kingdom accept that without excessive demoralization. It is not unfair for us to ask that people recognize that there is an understandable nostalgia for times past. Don't forget, when I was a schoolboy, we had a map in our schoolroom and on that map more than one-quarter of the globe was crimson. Times have changed now and I don't want anyone to think that I am harkening back with nostalgia to a time gone past. But I think it is necessary to bear in mind as a historical setting against which we must judge our current economic performance. And unfortunately the retreat of Britain from the world scene, as illustrated by the map, is sometimes confused with our economic performance. Our economic performance has just not been that bad.

Kissinger: Over what period of time are you speaking?

Lever: I am speaking about the post-war period, from 1945 until the present, or let's say 1973. Yes, we could say from 1945 to 1973. There have been a number of extraneous factors which have conspired to make the period from 1973 to 1976 a rather erratic one. But the important thing is that our performance in this time has demonstrated a remarkable strength, and yet everyone thinks that it was a failure. But in fact our performance during this period has been magnificently better than that during the pre-war period. We have been able to achieve a rising standard of life throughout the entire post-war period, especially for moderate labor people, for the middle classes. And, contrary to popular fallacy, the country has been been paying its own way. It should be noted that during most of this time our aggregate current account has been in surplus. Now one of the questions that I like to ask people who grill me on Britain's post-war economic performance, is "Do you think that we lived a little bit beyond our means, or a lot beyond our means," and most people answer that they think we have lived a lot beyond our means. The correct answer is that we have lived not at all beyond our means. I think one of the things it proves is that there is an awful lot of use of false statistics. Too many people tend to remember the performance of the Japs, Germans and the French in recovering from the depredations of war, and

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our internal political situation, of course, has not contributed to clarification. During most of the post-war period, both our political parties have shamefacedly claimed that they had it within their power and their will to reproduce precisely the same economic achievements as the French, the Germans, and the Japanese. Whichever political party was out of power claimed that the party that was in power had failed to live up to Britain's potential, and that the potential could be achieved only if you would put us in power. So what you have had during most of the post-war period is a see-saw of false promises and amnesia, as each party in turn failed to deliver, leading the electorate to choose the opposition for the next go-round.

Kissinger: What would you say are the causes of the present crisis?

Lever: What caused the crisis was a combination of the 1974 recession and the energy crisis. The only countries who could escape this combination were those who were the most successful competitively. It is important to remember that our people were called upon to accept lower rises in the standard of living and they broadly accepted this. The British people wrongly believed that they had been living beyond their means before the energy crisis; told now that they were in fact living beyond their means, they got to work. But as any economist can tell you, if you have the cost of your imports increased four or five times overnight, unless you're a pretty smart performer, you're not going to be able to increase your exports at the same pace. But it is a plain fact that Britain is today delivering more goods and services in volume for less. Britain's economic performance is the best today that it has been at any time during the post-war period. Britain is fighting for its terms of trade, but success, needless to say, is not right around the corner. And its biggest single problem is the sterling balances that have piled up. And, dear Secretary of State, if I had to assign blame in one direction, I would have to say you are personally responsible.

Kissinger: Now, Harold. We're in a transition period. All of my colleagues want jobs. Let's not be passing out the blame too freely.

Lever: It's true. The problem is that the countries who were piling them up -- that is to say basically the oil-exporting Arab countries -- simply were incapable of handling either theoretically or practically the monetary problems they

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had caused, or dealing with the monetary surpluses which they were reaping. They hadn't heard of Las Vegas yet. In fact, there were only two places they knew of that they could dispose of these enormous sums of liquidity -- Wall Street and us. And every time you wagged a finger at them, the money came pouring in on us. I went to Wilson at the time and told him, "You know it's just that they're frightened of Henry." This is only transitory, but every time the United States begins speaking of the problems that foreign liquidity would face if it tried to invest in American critical industries, hundreds of millions of pounds flowed into coffers in the city of London.

Kissinger: I had always heard that Harold was a charmer. When does the charm begin? (laughter)

By the way, do you have any idea when the BBC story (by Lever's daughter) will be on?

Sonnenfeldt: It's already run. It was actually very good.

Kissinger: Oh is that so? I'm sorry to have missed her.

Lever: Well, I'm sorry to have taken so much time with preliminaries.

Kissinger: No, no. It's very important for a perception of the problem that we have to deal with now.

Lever: So you see, our basic problem is that we have sterling wobbling and a very strange combination of economic circumstances conspiring against us. I must be absolutely straight with you. We might have handled this better in the first years in office. We probably should have done more and done it more quickly, but just as we began to get things under control, we were hit with massive inflation. And the problem is one which I submit to you would have defied the best and most capable band of economists -- that is, handling the enormous problem of the sterling balances when we had only minimum liquidity at the same time, and to be dealing with both of these under the spectre of the cloud of inflation. Now we have the problem of financing sterling balances. Let me tell you what we've done. I happen to think that it is a great deal, even though professional economists may believe that it is nothing but a series of half measures dictated by politicians practicing their cowardly trade.

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Kissinger: Cowardly politics is precisely why Treasury is almost always so much freer with their advice.

Lever: In the first place, we are at a down-start position. We are not in healthy shape trying to improve on a good performance. It is not even clear that the decline has ended, so we have that as a strike against us right off the bat. Second, although we have performed much, much better than anybody believes, we nonetheless for a variety of historical reasons are in a position which no one envies. And third, we are mucked up financially by the problem of sterling balances, a problem which we have borne manfully as our contribution to the economic structure of the Western world. Now in terms of dealing with the problem, there are two things that the government has tried to do, and in which I would argue that it has been notably successful. First, for the first time we have a serious income policy. We have got there. We have done it. We have halved the wage push from 30 percent to 14 percent this year. Secondly, however, the parity change problem is the biggest single problem in the wage push and we still have to deal with that, but we're down to two aspects in this. The first of these is responsibility. You know it is almost touching to watch Jack Jones and Hugh Scanlon, two of the most powerful men in the trades unions in my country, who could be described as kind of fuzzy-minded socialists -- almost Communistic, not really very serious. It's rather touching to listen to somebody like Jones go on the radio and exhort to all who listen, "My advice is for foreigners to buy the pound. I want to say on behalf of British labor that we are not going to let the pound down. We will stand by it and support it and defend it." You know there's almost a touching determination on the part of labor to hold to the deal they have struck, and in fact I think they mean it. And second, we are really tackling public expenditure for the first time. Now I know that the bankers won't be bought off by this or the professional economists, or the Treasury men who regard cash limits and other instruments of the torture chamber as far superior to the means that we have used up until this point to tackle public expenditure. But in fact at last we're working on it. You know it is most interesting to watch the process of British self-denigration at work. We have an almost pathetic tendency to tell foreigners that we are really terrible people in that we have no sense of self-control and are helpless at solving

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our own problems. In fact, on at least two levels of economic measurement we have done much better than any of our European partners. Our inflation, measured as a percentage of our gross national product, is down to half of what it was the year before, and now stands at a quite respectable level -- not the lowest that it has been in the post-war period, but not the highest that currently exists in Europe. And our defense expenditure, contrary to popular belief, is higher than that of any, repeat any of our European partners. Our public expenditure is certainly no higher and in fact even in one area that is not widely acknowledged, Healey has revamped the income tax and will shortly be presenting it to reflect a lower level at the highest brackets, even than in the United States. He has had a dramatic impact on corporate tax. Most of this appears as capital stock appreciation relief. It is also why the public sector deficit has gone up. Why, we lost in fact two to three billion pounds in taxes on corporations which have been foregone in order that industry might have the money that it can reinvest.

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Kissinger: Does the Cabinet make its decisions by majority vote?

Lever: No. In effect we sit around and talk about problems until a consensus emerges. The Prime Minister, of course, helps shape the discussion and he may have a consensus in mind which he chips away at until it emerges.

Kissinger: As long as he can get away with it.

Lever: Yes, but in fact the Prime Minister has a very funny role. He is not precisely presidential in that he cannot command. He can try to lead towards a consensus or he can hold back until one emerges and then claim credit for him.

Kissinger: Has he ever been challenged? Do you ever challenge him?

Lever: Sometimes. Heath was of course much tougher. Heath sometimes would enter into a conversation or a discussion with his mind made up. From time to time he would be challenged, and he would actually fight it through insisting on his point. Both Harold and Jim have made it a point of honor to sum up the consensus which emerged from the Cabinet discussions. Only very rarely have either of them begun with their point and insisted that it be the end. Now occasionally with Jim when we know that he is very keen on something, we will stay silent until a consensus has emerged which is favorable to his point of view. Only if we really feel very strongly about something do we tend to argue with him. Normally, if he wants his way, he can achieve at least enough silence to treat it as assent, but I've never known either Harold or Jim to resent disagreement. The civil servant mentality is, of course, much worse since it tends to argue back.

Kissinger: Our civil servants have the advantage of simply not carrying out what they disagree with.

Lever: Only once have I known Jim to stick his chin out in the face of what was quite evident Cabinet disapproval. And in the end even he came around saying, "Well, I happen to think that it should be done this way, but since it is very clear that the Cabinet does not, I guess I will have to bow to the Cabinet." Well, to get back to the economic portrait, there are a couple of things which look reasonably good. First, we have undergone a real fall measured in statistical terms in sterling balances. This is in part a result of the devaluation which has occurred and in part a fact that there have been substantial conversions out of sterling over the last several years. And secondly, the wages and salaries push will fall by an estimated 7 to 10 percent during the latter half of 1977. In fact, I'm not sure I think

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this latter point is all that encouraging. I think it may be quite alarming. I think it is much too high. For one thing, it could very easily lead to an enormous fight both within the government and between the government and labor. We have to make absolutely certain that our push for exports is not frustrated by imports. The savage depreciation that we have undergone has not affected our morale yet, but it must not be allowed to do so. So thus far the government has done three things. They have at last seized control of and managed to put some brake on the major engine of inflation, which was the wage-price push. Secondly, the government has adopted a tough monetary supply policy. And thirdly, at least at this point, our morale is still in pretty good shape -- we are not frightened. In fact sometimes I wish the British people weren't quite so courageous.

Kissinger: Incidentally, Harold, could I get a copy of your notes. I'd like to show them to the President. I promise you they won't go anywhere else.

Lever: Well, if you were to ask me for them, I don't see how I could possibly refuse.

Kissinger: Yes, I think it would be very helpful.

Lever: Yes, well I'm glad you asked, since I don't think I could refuse (implication is that he would not otherwise have given them).

Now let me just mention one more thing, and that is the state of our industrial relations. Two years ago industrial relations were quite frankly appalling. Now they are quite acceptable and even Transport House has agreed on the measures that are needed to keep our economy moving. It is true that our export performance has been worrying in the last few months. But I don't think this is the only statistic worth paying attention to.

Kissinger: Why is it worrying?

Lever: Basically I would think that it is hesitancy in world trade, but curiously enough the chaps at CPI tell me that they are quite confident of our export performance.

Kissinger: The fall of the pound should help, shouldn't it?

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Lever: Yes.

Ryrie: Yes, it should but there are a couple of unexplained quarters.

Lever: Yes, but things have been bouncing around quite a bit. All of my industrial people tell me that things are actually quite chirpy. You know, let me tell you a little story about when I was last here in 1969. It was under similar circumstances, and I had meetings with all your top economic people. David Kennedy, I think, was your Treasurer. The problems we faced at the time were, I regret to say it, essentially the same ones that we face now. The attitude among your people was that you were getting reasonably tired of bailing out the British, and I must say I think we were overcome with a deep sense of pessimism. We had just gone through devaluation, and any post-devaluation session has to be a bruising experience, especially for a country with any sense of pride. How you handle devaluation and the post-devaluation period is mainly a question of nerve. Our pessimism fortunately is almost always greater than that which is warranted.

Kissinger: (a bit surprised, not to say alarmed, at Lever's enthusiasm) Wasn't that computer in "The Year 2000" (referring to "2001 -- a Space Odyssey") named Harold? (Widespread agreement around the table that it was -- but they were wrong; its name was Hal.)

Lever: Well, much as I hate to break this news to you, the Treasury arranges its computer and the statistics that it's used for, to contradict me.

In fact our computer tells us that we could have as much as \$1- $\frac{1}{2}$ billion surplus in 1978. We have very good public forecasts for a surplus in 1977 on current account.

Now let me deal with another aspect and that is worries about public sector borrowing. Public sector borrowing is not quite the same thing in England as it is in the United States. The basic difference is the structure of our economy. In England, for example, if you build a steel mill or a power plant it's called public borrowing. That's the simple fact of life reflecting national ownership. In America of course, it would be called a private enterprise and hence private investment. But the names have absolutely nothing to do with the net effect. Borrowing is borrowing and you then have to take a look at what the purpose is. Now our question is what do we do about the state of our economy? First, it should be noted that we have tons of spare capacity, which can be put to productive use. Second, we have

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the highest unemployment since 1933, which means that we have an ample supply of labor ready to go to work. The biggest thing that worries me in the present circumstance is that if we should get some spare cash, our banking friends and the professional economists will say that we should use it to deflate and no one -- and I must emphasize this point -- absolutely no one, except one person, in the Cabinet thinks that this is what we should do. Even I -- a fuzzy-minded, almost fascist-inclined private enterprise fanatic -- am against deflation.

Kissinger: Why?

Lever: A deflationary course should be followed only if its purpose was to create export capacity. Until I see that that's the problem -- you see we have even now surplus export capacity, and even if we do nothing more, export capacity will continue to grow. But basically the problem is political. If we were even seen to do anything like that (referring to deflation in order to create additional export capacity) it would cause the gravest of difficulties for the government. The theory that Britain needs an extra dose of deflationary economics in order to create additional export capacity may be very much in vogue, but it also ignores a basic reality in Britain. Simon will of course say that this medicine is going to be very tough now, but it will be better for us in the end. It will make us leaner, tougher, meaner, stronger men. Quite frankly, my own view is that it could lead to nothing but long-term injury to our competitiveness, to our investment, and so on.

Kissinger: They will argue that it will speed investment.

Lever: But I don't think so. It can only slow it down. You see industrialists will only add capacity if they see a chance of using their existing capacity more fully. They certainly are not going to add to capacity if they see no chance of increasing utilization. I, the hawk, in fact, think we've gone too far. It would be very much our long-term loss. You see, what is the point of entering a balance of payments surplus six months earlier if the net effect is to set back by five years the long-term restructuring of your economy?

Kissinger: How do you argue against cutting public sector spending and thus trying to cut inflation -- on the grounds that it would cause a more massive crisis later?

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Lever: My own view is that wages policy is critical. Can we in fact continue to hold the line on wages being paid to working people while they suffer a drop in the real standard of living? I think we can, but I'm not sure that we can at a cost of higher unemployment. That would destroy the very basis for the social compact. It would do three things. There is no question in my mind that we would suffer a long-term cost. We would have no short-term gain and it would smash the social compact. I must tell you that the Prime Minister feels very, very strongly about that. So does the Cabinet and so even does CBI. We must reshape our public expenditure, but that's a ten-year project. Simon and I differ only on the question of timing -- not on the basic question itself. The halt to public expenditure, and especially the rise in it, has taken place, but we can begin to reshape it later. We simply can't do it right now.

Kissinger: If you did have to do it right now, what would happen?

Lever: (who clearly had not anticipated this question) Well, I guess we would have to take a look at several possibilities. First, if the Labor government were actually invited to do it, I think the government itself would probably break up. I do not believe that the government, certainly not as it is presently constituted, would agree to embark upon a policy of deflation. Second, if it didn't break up, it would certainly fight it, at least among itself. The left wing would insist on defense cuts which we have successfully staved-off up until this time. Even I have fought against defense cuts. We must bear our burden. I know I don't have the full intellectual understanding of the need for them, but they are the sort of thing that intuitively Britain knows it must bear.

Kissinger: The thought that you're such a simple guy is one I have to hoist aboard first.

Lever: I enjoy passing myself off as a simple provincial.

A certain reaction to a deflationary policy would be an undoubted further push in the direction of protection. This would be almost concomitant to any effort the government might take. And as much as I hate to say this, even the IMF appears to have agreed.

Kissinger: With what reasoning?

Lever: The IMF's report said, "You will only be able to do what you are trying to do with import restraints." I am of course unalterably opposed. Import restraints go against the whole fabric of our western economic structure as it has developed

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since the post-war period. You know, if I might tell you a little anecdote out to the side, I think it may illustrate my feeling about the question of import restraints. Chrysler -- you may have heard of this company -- when it was in difficulty in England some years ago, many people argued that when it fell it would prove conclusively that Britain should impose needed import restraints. This argument, aside from being very silly, is nonsensical. If you were going to put on import restraints, you should put them on if they didn't close down. But quite frankly there was no question in my mind that we should keep Chrysler open, no matter what the cost. I would much rather pay for it, and in fact at 50 or 60 million pounds, I've saved a fortune several times over in unemployment payments. So the net effect is that if we are forced to go the deflation route, the left wing would be prepared to threaten defense expenditures and there is no reason to believe they would not do so successfully. And there is no economic case whatsoever for any reduction in demand -- in fact demand is already at too low a level. One really has to question whether this is a desirable set of circumstances. If the government were to break up, we would be faced with a very unpleasant election. There can be no question that the left wing will be firmly in command of our party as it went into such an election, and in the election the voice of the moderates would cease to be in control. There would be the left wing, Transport House, and all of the remainder ranting and railing against the bankers and the industrialists. As I see it the government has now been chastened by two by-elections and we have a pretty good chance to reassert control over the national executive. The left wing is widely seen to have caused these last two losses. But if we do lose the next one, then I think one would have to look seriously at what the consequences would be of a Conservative government. If the government were to break up, then Margaret Thatcher -- no matter what her undoubted abilities -- will have her chance to see what she can do. I realize there are probably a substantial number of people who do not necessarily regard this as an ill thing, but basically one has to accept that Margaret would have a dubious legitimacy if she came in on this sort of election. But let's assume hypothetically that she won. In the first place, she would have a first-class ruckus on her hands with the trade unions. There is no reason to believe that she would have any greater success than we with her budgetary policy. As a minimum it would be several years before she could impose enough of her economic package to have an effect on the trade statistics. In short, you would have a first-class smash on your hands to no good end. Why go through this? What for? Nothing good could possibly come from it. I agree one of the things the Labor government has not yet done that it must do is bring under some sort of control the futile gas bags in Labor's left. They are of absolutely no importance in government, but they would be very important

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out of office. As long as the government is in control they can have no effect other than to embarrass and create a general nuisance. But they will be terribly disruptive to the moderates trying to keep Labor under control if this government goes out of office. But if I were to guess, I would guess that Labor will win. I have to qualify this by saying I couldn't possibly support policies I don't approve. I wouldn't and couldn't support deflation, and I don't know who would. Its immediate effect would be to lead to an immense hue and cry for cuts in defense expenditure, calls for a rise in protection, which would lead to protests from the Japanese, and grave damage to the IMF. It would set into play a whole series of frictions which could come to no good end. It's clear that we have to take charge of our economy and the first thing that we have to do is get control of our currency. First, we have to pay back the \$1- $\frac{1}{2}$ billion standby credit; second, we have to take the unwanted sterling off of the market. We badly need the safety net, and if we get the IMF deal, I would argue that we've got to use that principally for the safety net.

Kissinger: But you opposed it.

Lever: Oh, you mean referring to your safety net (the Secretary's proposal for a \$25 billion safety net for all subscriber countries whose currencies fall onto hard times because of temporary or transitory balance of payments difficulties).

Kissinger: Well, of course if our proposal had been accepted . . .

Lever: Among other things, if your proposal had been accepted, we wouldn't be here at breakfast today. The real tragedy is that you're not going to be here long enough to push it through. I have to say that the only person with creative imagination to have thought up such a scheme and the audacious political courage to fight it through -- and you will throw the milk at me for this blatant flattery -- is you.

Kissinger: But I agree with that. (laughter)

Lever: Denis (Healey) went for a \$6 billion safety net. You went for \$25 billion. But it is only on that kind of scale that such a scheme could possibly work. In effect a safety net would have to swamp or totally cover any imaginable threat which would require its use. When you look at the disproportionate scale between what Healey proposed and your proposal, it's absolutely ludicrous. But it is also fair to say that you are the only

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person who could have pushed this through. Do you know, several weeks ago I came across an article which was produced for the syndicate of European banks. You know, it is the group that includes the Dresdener Bank, Barclays, the big bank in Amsterdam, which really showed that there has been an appreciation for the position you urged. (He asked Ulrich to dig out the article from his attache case.) I'd like to read you a bit from the article. It says, and I quote, "There has been an encouraging revival of talk in recent months about a proposal for a safety net to help countries who find themselves in 'terms of trade' problems. The economic problems intended to be dealt with by the safety net are primarily transitory ones where the countries who would use the safety net simply find themselves with a need for a longer term for adjustments than the market mechanism would immediately provide." (He stops reading.)

Kissinger: Let me see now whether I understand you. What do you think the proper course of action at this point should be?

Lever: What I'm basically saying is that I think the most helpful thing you can do at this point would be to get the IMF to stretch its pedantic reflexes and grant us the \$3.9 billion standby. It would also be very helpful if they could spare my country the humiliation of attaching the strings that customarily come with such an offering.

Kissinger: What further humiliation could they inflict?

Lever: Britain is not yet to the point of carrying around a begging bowl. The purpose of the IMF when it was conceived was to serve as a body for cooperation. We mean to be strict and tough with ourselves, as I would argue we have been for the last two years. Give us the money with no deflationary terms and no trigger terms, such as \$2 million now and \$1.9 billion in six months if our trade figures show sufficient improvement. I have to say this to you and I say it to everyone here at this table and I say it with a perfectly straight face. The British government does not make promises except in good faith. It does not sign agreements on what it will or will not do. It speaks in good faith and it expects to be accepted in good faith. But even if we were to fail within the first six months and thus were supposedly not to qualify for the \$1.9 billion which extension was to be predicated upon a good performance, I still can hardly believe that the IMF would not make it available.

Kissinger: Would it be helpful to you if the terms were extended to two years?

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Lever: No, the problem isn't the time. The problem is the way it's expressed. Psychologically it is simply very much a confidence-destroying exercise to have trigger mechanisms.

Kissinger: No, no. I mean could you use two years for repayment?

Lever: Well, I would gladly agree to have two years, but we don't intend to need it. We're going to run our economy on a course that we have already set out and which we believe shows the greatest promise of success.

Kissinger: What do you propose to do about cuts in public sector expenditure?

Lever: Well, you know there is a basic difference between "cuts" and "net cuts". If you simply cut public sector expenditures without any deflationary measures, you simply take the amount of money thereby freed and release it into the marketplace. That does not net you anything. If by cuts in public sector expenditure you mean net cuts in spending then the only possible result can be higher unemployment, and that simply is not acceptable at this time.

Kissinger: Let me tell you some of the arguments that you will be hearing. I'm sure these will come as no surprise to you. I'm sure you have prepared for all of them.

There is a general theory in this town that the United Kingdom is in trouble in large part because of us. We have given band-aids in the past rather than help you to find the sort of basic reform that appears to have been needed. In other words, if we give you what you ask now, we will simply have postponed for six months your need to work out the basic structural reforms in your economy and you will be back to my successor in that period of time for more help. Whereas if we hold out now, you will have us to blame and can blame us to your Cabinet and the party and even the parliament and the British people, but in fact you will have to tighten up and thereby undertake the reforms that are needed. I must tell you I don't necessarily share this, but I simply want to let you know what you may be in for here.

Lever: I'm glad you have your problems with your colleagues too. But you know, one of the most maddening things is that I'm sure the convictions you have just expressed are held throughout the western world, but in fact, and this is a matter of some pride, everything that we borrowed in 1969 was paid back -- every last farthing.

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Kissinger: Yes, but you made no reforms.

Lever: No. With respect, that just isn't so. The social incomes policy is the most far-reaching reform we have undertaken and it is the envy of every country in the western world. I dare say even Bill Simon is envious of it. It is the sort of thing that you may even see your Congress in due course trying to create. And another thing worth bearing in mind is that during this period in the last three quarters of a century when we have gone from the Victorian gin palace to the pits of riot and decay that we find ourselves in now with our social welfare state, we have been interrupted by two world wars in which some of my countrymen would not shy to remind you the United States held out until quite late in the game.

Kissinger: Do you believe there is a direct relationship between money supply and deficits?

Lever: Which deficits?

Kissinger: Public sector. And that therefore the only way is to cut down the money supply?

Lever: Well, speaking of some of the old 'wives' tales currently in vogue, let me just point out that one of them is the theory that you can't sell gilt-edge (securities) because your public sector account is too big. The theory holds that if the public sector is too big, there can be no gilt-edge market. But in fact this is absolute nonsense. Of course you can sell gilt-edge if there is a market for them, irrespective of your public sector (borrowings). I can sell gilt. In fact Denis has put me in charge of selling them. And one of the things I'm going to suggest to Simon if he gives me this argument is "let's test it. Let's just see what we can do in the public market." You can always sell gilts if people believe they have a chance for a return on their money.

Kissinger: What about sterling balances?

Lever: I'd like to fund them, but that's something for the safety net.

Kissinger: Which is dead in Congress.

Lever: No, I think I'd use a sterling safety net, and if our plan works out and our safety net works, it might even revive yours in Congress. In fact, if you had a Democratic Treasurer, it might even fare better in Congress. But if we tried this, it will probably have to be arranged through the central bankers.

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Kissinger: If you don't mind, Harold, I'd like to ask you some questions -- some of them which will probably be highly undiplomatic. The first, may I simply ask you boldly, do you represent the Cabinet's view or just your own?

Lever: Yes, I do represent the Cabinet's views and I might say I especially represent the Prime Minister's views.

Kissinger: Denis Healey's?

Lever: Yes, Denis Healey's included.

Kissinger: That's going to be a very important point to make to Simon and the President.

Lever: I understand. Incidentally, you should know that the Prime Minister is a very sticky chap on this. He has become quite thoroughly involved. He has cleared virtually all of the proposals I am making here, letter by letter, word by word. As you know, I have a letter for the President from Jim.

Kissinger: If I might make a suggestion, Harold, and to you too, Peter, it would be why don't you send it to Brent Scowcroft tonight so it will be there tomorrow when the President returns.

Lever: You know I don't wish to brag, but I must say I've always been given high marks for my skill at salesmanship. In this case, however, I must say that the voice will be the voice of Jim Callaghan's as well.

Kissinger: So, let me see if I understand you. You want us to use our influence with the IMF for a safety net which would be used basically to help you with sterling balances but without the sorts of strings that you have had in the past.

Lever: Yes. You know, speaking of the IMF, I must say that one of the biggest bear factors in the past in international eyes has been the maltreatment of high salary earnings. Denis Healey is trying to get the Cabinet to agree to do something about this but with what success, no one knows. Now if I were the IMF, I think I'd be tempted to interfere with that.

Kissinger: My problem in discussing this with the President is, of course, that up until now we have had no concrete British proposal. Our brilliant economists have told us what's wrong with you, but not what we should do about you. You realize that I'm not asking you to abate the letter of intent of increases in money supply.

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Ulrich: No. In fact, we expect we may have to.

Kissinger: Well, the most helpful thing you can do is to give us a concrete program. We haven't been able to put together our thoughts on what is needed. My own view is that it should be treated as a political problem. I would hate to have a British government brought down by the United States, especially by US bankers. But we have to have a plausible ground for belief that the fundamental reforms have been taken. My instinct is that you have a major problem right now and there simply has to be a serious attempt to cope with what the public views to be your problems. Now I haven't seen Simon yet, but I will discuss this with him. I will be seeing him before you do.

Rogers: Simon, of course, won't embrace out-of-hand all of your proposals, but he's reasonable about these things. He'll listen.

Hartman: Treasury will also be interested in the tax angle.

Kissinger: How long are you going to be here?

Lever: I leave on the noon Concorde flight on Wednesday.

Kissinger: (looking at Sonnenfeldt) When am I going to Williamsburg? This has to be one of the more absurd things I've been roped into.

Ramsbotham: Tomorrow.

(There was then a digression on Congress, Wayne Hays and Brademas, etc. The Secretary recounted his anecdote about having testified on the national interest for at least an hour and gotten nowhere, following which Wayne Hays motioned to Brademas to join him in a corner and said, "Look you SOB, do you want your parking place to be out in Bethesda? Do you want your picture to ever again appear in a Congressional Directory?" Brademas caved and I was, of course, crushed, but grateful.)

Kissinger: Well, I will recommend to the President that he see you on Tuesday afternoon. This will give us tomorrow morning to study your proposals. I will also suggest to him that he see you alone, perhaps with Brent, but without too much staff, which simply provides a pretext for a domestic argument.

Sonnenfeldt: The visit of course should be announced.

Kissinger: Oh, yes. Of course it will have to be. May I show your paper to Simon and the President?

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Lever: I can't refuse you of course, Mr. Secretary, but I must tell you that we are terrified of leaks.

Kissinger: What in the world is there to make you think it will leak? Has anything that we have ever undertaken to keep secret leaked? I will show it only to Simon and the President.

Lever: Would you mind terribly chewing it up afterwards?

Kissinger: (to Hartman) And would you please have the record show when you begin spreading it all over town in your telephone calls which will begin immediately after this meeting ends that I was tough as nails with Lever. (laughter)

Lever: I want you to know, Mr. Secretary, that I deeply appreciate your having taken the time this morning to hear me out. Your departure, I must say, will be accompanied by a genuine wave of affection (could he have meant "anguish"?) from your Cabinet colleagues in England.

Kissinger: Well, let me tell you that as one who has had few opportunities to develop any true friendships in this business, I want you to know I have some for Jim and Tony.

Lever: No, no. Quite seriously, there is a genuine degree of affection which your British colleagues have for you. I must tell you that you take with you a genuine degree of affection from your British colleagues which I have hardly seen paralleled in my lifetime.

Sonnenfeldt: Not, of course, as a statesman, but as a lovable person.

Kissinger: (looking at Sonnenfeldt) You know it is widely reputed in this town that Hal Sonnenfeldt has the best intelligence network in Washington. Unfortunately, it's directed against me.

Meeting broke up at 9:50. Harold Lever and the Secretary talked privately in the Secretary's office for about ten minutes.

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