

CONFIDENTIAL

Prime Minister

MR. ALEXANDERAgree that draft of Flag A
Should issue?

Punt

Positive MCAs

The Minister of Agriculture has now responded, in his letter and enclosures of 11th April, to the Prime Minister's request for a note on the various factors involved in the decision to introduce positive MCAs for Britain.

2. Under Community Regulations, positive MCAs (which act as a subsidy on exports and a tax on imports) are applied when the market rate for a currency rises above its ECU parity. This is now the position for sterling, with a current gap of about $3\frac{1}{2}$ per cent. But MCAs do not cover the whole gap. There is a franchise (or "neutral zone") which is deducted before MCAs are calculated. Mr. Walker's letter principally deals with the relatively narrow question of the franchise, explained in more detail in Annex B to his letter.

3. In the March Agriculture Council Mr. Walker sought the elimination of the franchise on our positive MCAs, rather than merely its reduction to the 1 per cent level applicable to the German positive MCAs, intending to block the extension of the relevant regulation to get his way. This line was agreed in OD(E) (OD(E)(80) 5th Meeting, Item 1), but has since been frustrated by the Commission's insistence on acting as though the regulation was still in force. In the fourth paragraph of his letter he accordingly suggests that we might accept a compromise, either at the European Council or at the April Agriculture Council. The Prime Minister may feel that it would be unwise to inject this technical point into the European Council's discussions, and that the Minister of Agriculture should accordingly seek to remove this point of conflict before those discussions begin.

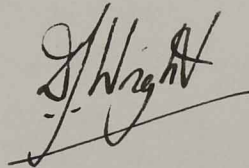
4. There is however the wider question as to the appropriate level for the Green Pound in present circumstances. When the appreciation of sterling eliminated our erstwhile negative MCA the Government theoretically had (and still has) two choices: to accept a positive MCA at the level dictated

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by sterling's relationship to other Community currencies, or to revalue the Green Pound to bring it nearer or up to the market rate for sterling.

Mr. Walker prefers the former because a revaluation of the Green Pound would reduce United Kingdom farm incomes at a time when they are already being squeezed, and because he regards the introduction of a positive MCA as consistent with the Government's Manifesto commitment to allow United Kingdom farmers to compete on equal terms. On the other hand, positive MCAs involve public expenditure and an increase in our net budget contribution of about £20 million for each percentage point. This is because we are net importers of food and have to hand over to the Community the higher levies on our imports. The Prime Minister may feel that the Green Pound rate (which was not considered as such by OD(E)) should at least be kept under review. If, for example, we are forced to agree to higher price increases than we would like in order to secure a satisfactory budget deal, it would be possible to offset a small part of its effect on food prices at home by a small revaluation (as the Germans will be doing) if it appears that the higher level of sterling is likely to be maintained (though the latest movement of sterling suggests that positive MCAs may disappear again soon).

4. I attach a draft letter in this sense.



(Robert Armstrong)

(approved by Sir R. Armstrong
and signed in his absence)

14th April 1980

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DRAFT LETTER FROM MR. ALEXANDER TO
MR. WALKER'S PRIVATE SECRETARY. MAFF

United Kingdom Positive MCAs

The Prime Minister has seen your Minister's letter of 11th April about the level of the United Kingdom's positive Monetary Compensatory Amounts and is grateful for the background information provided with it. She would prefer if possible that the dispute between ourselves and other member states on the question of the neutral zone be resolved before the 27th-28th April European Council, if necessary by means of the United Kingdom concession mentioned in the fourth paragraph of your Minister's letter.

[sideline is attached text.]

2. The Prime Minister also feels that OD(E) will need to keep the level of the Green Pound under review in the light of movements in sterling and the forthcoming negotiations on common prices.

3. I am sending copies of this letter to ^{the Private Secretaries to} members of OD(E) & to David Wright (Cabinet Office).

Would rather have
this for the time being.