

PRIME MINISTER

Four background papers about the preparation for the Bonn Economic Summit and Chancellor Schmidt's ideas on currency stability:

Flag A - A despondent minute from the Foreign and Commonwealth Secretary who seems to be (so I am advised) developing a fatalistic view about the Summit prospects and sees an increasing likelihood of a Summit failure and a rapid, indeed necessary, move to protectionism not least by the UK. He asks in effect to have a meeting to inject momentum into the preparatory group meeting in Washington on 27/29 May. You have already talked to Sir John Hunt about this - and you (and other Ministers at the Seminar) could have further discussions after the preparatory group meeting: this could even take place <sup>(with Dr. Owen)</sup> in Washington early next week.

Flag B - Complementary to Dr. Owen's minute is the paper by Ken Couzens setting out his view (with which Sir John Hunt and Sir Michael Palliser are in agreement) about the line which the UK should take on growth and currency stability at the preparatory group meeting - see paragraphs 6 and 7. It does look rather anodyne and lacking any sense of political urgency of the kind which is moving Dr. Owen, but you have already told Sir John Hunt to keep probing and pushing.

Flag C - An interesting account by Ken Couzens of his meeting with Clappier and Schulman to discuss Chancellor Schmidt's proposals for European currencies. Schulman is developing the Chancellor's ideas in some respects. They are still at an extraordinarily high level of generality and it is remarkable (paragraph 14 of Ken Couzens' note) that

/Schulman was

*None of it comes as hand futter.*

*Mr. Hicks  
wd. you pl. do the necessary acknowledgment*

*27/5*

*Agree!*

Schulman was asking what prospect there was of reaching broad agreement on these proposals by 6/7 July - 7 weeks away.

Flag D - An assessment of the implications of France rejoining the Snake.

K.R.S.

25 May 1978

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Prime Minister.

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See covering minute

PRIME MINISTER

BONN ECONOMIC SUMMIT

The papers for the Preparatory Group are being finalised this week and Douglas Haas is in Washington for the purpose. You are seeing John Hunt and Michael Palliser on Friday before they go to Washington. They are well aware of the need for beefing up the Summit proposals, and would welcome discussion with you not only on Friday but after the Group has met, in Washington. K.R.S. 19/V.

We have just received Ken Conzen's appraisal - attached Page 3

1. The prospects for the Bonn Summit are not good. The responses from the other six Governments, judged by the papers to be discussed at the Preparatory Meeting on 27-29 May, are very disappointing. For us the most important single objective is a higher growth target for the world as a whole. To achieve this I think we must adopt a positive stance on currency stabilisation, while at the same time making it clear that in our view the present world trading system will not survive in the absence of faster growth and progress towards reducing unemployment. The Germans seem determined to press for pretty unqualified adherence to the principle of free trade. We could certainly give them no new assurances in this area unless we got real progress on growth and currency arrangements satisfactory to ourselves. The German paper also proposes that there should be a new consultation procedure before protectionist measures are taken. This picks up a suggestion in the paper which you sent to President Carter that industrialised countries should explore ways of reducing pressure for protection by, among other things, improved consultation procedures. We must make sure that the Germans do not use this idea to make it impossible for the Community to look at particular problems on a case-by-case basis and to take safeguard measures when they are needed; but we must clearly respond fairly positively to the German wish to discuss this, and if our other concerns are satisfied we could go along with them.



TPM with PM

2. I have read Harold Lever's minute to you of 9 May about currency stability with great interest. His ideas are important from the point of view of European policy as well as the Summit. In this field there seems at present little prospect of progress on specific measures. The Germans hope that there will be more growth if there is greater stability, but are reluctant themselves to move on growth. The Americans hope that there will be more stability if there is greater growth outside the United States, but are reluctant themselves to move on stability. We have therefore to try to move them both along. I see attraction, as well as some risks and difficulties, in Harold Lever's suggestions. I am afraid that he almost certainly under-estimates the difficulty of moving the Americans along in his paragraph 12. Nevertheless, I am in favour of making a positive response to Schmidt's initiative. If we could ensure that we entered any currency arrangement at the right parity and that the Government retained the freedom to adjust our exchange rate as necessary to maintain our competitiveness there are obvious advantages for us in having German reserves in support.

3. On long term capital flows, including aid, one specific measure which could come out of the Summit - and we need something for the Third World - is a commitment on Retrospective Terms Adjustment (RTA), to which we gave some support in principle at the UNCTAD Meeting in March. If we are to move on this we shall need to take a decision ourselves fairly soon and then to press the other participants to do likewise.

4. On energy, we must put all the pressure we can on the Americans to take action in the Summit context, and it looks increasingly unlikely that the President's Energy Bill will pass in a form which includes the COET (crude oil equalisation tax). The alternative of an oil import tax might, if wrongly

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handled, strengthen the position of those OPEC countries which want an oil price increase. But I believe that the Saudis could be persuaded that the effect on both the dollar and on conservation would be beneficial. On balance such a tax would be helpful and I think you might consider discussing this with President Carter in Washington if by then he can still see no prospect of getting COET through Congress.

5. To sum up, I am very worried that we are short of real content on all the 5 points and think that we must try to inject some momentum into the Preparatory Meeting in Washington on 27/29 May. There will be no chance of disguising a failure at the Summit this time. A failure would damage us as a government and in my view put the whole free trading system in jeopardy, since I cannot see it surviving in the face of continued low growth and mounting unemployment.

6. I am copying this minute to the Chancellor of the Exchequer, the Chancellor of the Duchy of Lancaster, the Governor of the Bank of England and to Sir John Hunt.

(DAVID OWEN)

19 May 1978

Foreign and Commonwealth Office.

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