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cc Mr Alexander

ANGLO-GERMAN SUMMIT: MEETING WITH DR. DIETER HISS

I met Dr Hiss in Berlin. We had talks lasting in all about five hours. It is clear that on the German side this contact is known to very few people; but I suspect this is not the only occasion on which Chancellor Schmidt has used an unorthodox channel (Hiss having been Schlumann's predecessor in the Chancellor's office is now the Bundesbank representative) ^{in Berlin} in order to by-pass the coalition. He saw the contact as limited to ways of reforming the CAP. I said this was only part, though an important one, of the Budget restructuring exercise to which we attached great importance.

2. Hiss said that, by the time of the Prime Minister's visit on 16th November, Chancellor Schmidt would know the outline of the new coalition Government's programme. As regards the CAP, it would not be as ambitious or as detailed as the recent report by the working party of the SPD (chaired by Apel) but it would nevertheless show some determination to get the CAP under control. In particular, in order to stay within the financial ceiling, the possibility of national financed income aids for selected groups of farmers was not ruled out. Chancellor Schmidt was only prepared to accept a high German contribution to the Community Budget provided there was real prospect of relief within a few years. The FDP had moved somewhat closer to the position of the SPD and, within the FDP, Herr Ertl's position was no longer as strong as it had been. The threat of resignation, which Ertl had used effectively in the past was no longer such a credible weapon and he was aware of it.

3. As regards next year's price fixing, I said there were two constraints: financial possibilities within the 1 per cent ceiling (which we both agreed was a basic assumption in our discussions) and the need to be seen to take a first step in the direction of restructuring the Budget. 1981 could not be another "stand off" year. The problem was how to reconcile these requirements with the income needs of farmers (which were greater in our case than in theirs

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because of our higher inflation rate) and the French Presidential election. We felt the first need was a tough line on prices. We realised that a price freeze was not acceptable but some people thought prices should not go up by more than 4-5 per cent (although I made it clear that the Prime Minister was not committed to these figures). Secondly there needed to be a financial limit on agricultural expenditure in 1981; and thirdly additional measures especially to control milk production. He said price increases of this order would present no difficulty for Germany but would not be enough for the rest of the Community. There would be no objection from the German side if we wanted to advocate it. So far as Germany was concerned, they knew that they could moderate the effect of a ten per cent price increase by re-valuing the DM, although Herr Ertl would not like to do it alone. Would the British Government be willing to re-value the Green £? I said our position on the Green £ had not been decided but I thought it was dangerous for both of us to be talking in terms of re-valuation since this would take the pressure off other member states to limit the increase in common prices. Higher common prices put the budget up. (1.5 billion direct effect eua in a full year for a ten per cent price increase) After further discussion he thought it might be possible that at the forthcoming meeting Chancellor Schmidt could agree to:-

- i) a qualitative statement about the need for price restraint for products in surplus
- ii) a re-affirmation of the 1 per cent VAT ceiling
- iii) restricting the share of the Community Budget to be absorbed by agriculture in conformity with the German Government's statement of 4th June
- iv) an indication that the Chancellor (and the Prime Minister) intended to keep a close eye on the forthcoming agricultural price negotiations (this to show that "agricultural prices were too important to be left to the Agriculture Ministers").

4. He attached considerable importance to the institutional arrangements for handling agricultural matters in Brussels. Chancellor Schmidt had on several occasions been unsuccessful in holding the line in the German Cabinet because the Agriculture Minister was able to report back that, unless he agreed, there would be a crisis in the Community. Even when the Chancellor agreed with the Finance Minister and the Economic Minister they could not control expenditure decisions which were taken in Brussels. Hiss was sceptical about applying

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effective cash limits to the CAP; the Agriculture Ministers could always find ways of appearing to comply with them. I said experience of joint Council meetings of Ministers of Agriculture and Finance had not been encouraging. Getting the Finance or Budget Council to set financial limits might at least have some influence. Increasing the power of the Budget Commissioner over the Agriculture Commissioner would also help. We discussed the possibility of getting the European Council to endorse something like the four points mentioned in paragraph 3 but were conscious of the political difficulties which President Giscard would have before his election.

5. We discussed individual commodities as follows:-

a) Milk

I explained our support for the supplementary levy on excess output and our objections to straight increases in the co-responsibility levy. Dr. Hiss said our approach was fundamentally different from that of the French who wanted to discriminate in favour of smaller producers and against milk producers who depended on imported feed stuffs. The German position lay somewhere between the two but probably closer to French than British thinking. We discussed the practicality of operating income aids in the milk sector as part of a tough price policy. The difficulties of devising a workable scheme for supplementing farm incomes on a generalised basis might be less if it applied to only one sector of production. Each member country would have to be free to decide what kind of income transfers it wanted to go in for. I suggested it might be possible to build in a disincentive to production.

b) Cereals

I suggested adjusting the level of the intervention price according to the size of the Community surplus. In any case cereal prices were too high. Hiss recognised that Germany was vulnerable on this point and that a rigorous price policy for cereals would attract some support in France. We could, he said, "test our political will to reform the CAP in this way". He suggested that the investment decision of cereals (and perhaps other) producers could be influenced by being given medium term price targets.

c) Sugar:

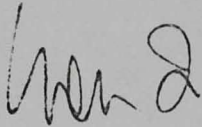
We agreed that, through the quota system, it would be reasonable to get producer to bear all financial responsibility (apart from ACP sugar) for surplus production

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d) Beef

I tried out the idea of replacing intervention with a deficiency payment system, or, as with sheepmeat, giving member states the choice. He plainly thought all this too ambitious and that the most that could be done was to reduce intervention. I said the Dutch were keen on the latter.

6. We agreed to resume discussion on these and other commodities in early December.



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