

RECORD OF THE PRIME MINISTER'S DISCUSSIONS WITH CHANCELLOR SCHMIDT
IN PLENARY SESSION AT 10 DOWNING STREET ON 11 MAY 1979 AT 1030 HOURS

Present:

Prime Minister	H.E. Herr Helmut Schmidt
Foreign and Commonwealth Secretary	Herr Hans-Dietrich Genscher (Foreign Minister)
Chancellor of the Exchequer	Herr Matthöfer (Minister of Finance)
Secretary of State for Defence	H.E. Herr Ruete
Lord Privy Seal	Herr M. Schuler (Head of Chancellor's Office)
Ian Gow, MP	Herr M. Lahnstein (Assistant Under Sec., Ministry of Finance)
Sir John Hunt	Dr. Jurgen Ruhfus, DUSS
Sir Michael Palliser	Dr. A. Grunewald (Deputy Government spokesman)
H.E. Sir Oliver Wright	Dr. H. Schulmann, DUSS
Sir Frank Cooper	Dr. K. Blech, DUSS
Sir Kenneth Berrill	Dr. H. Lautenschlager, DUSS
Mr. Ken Couzens (HMT)	Dr. W. Heck (Assistant Under Secretary of State, Ministry of Finance)
Mr. Michael Franklin (CO)	Dr. K. Zeller (Principal Private Secretary)
Mr. Julian Bullard (F.C.O.)	Dr. Alfons Bocker
Mr. Michael Butler (F.C.O.)	Herr Rothen
Mr. K.R. Stowe	Dr. J. Sudhoff (Press Spokesman)
Mr. Henry James	Dr. Peters (P.S. to Chancellor)
Mr. B.G. Cartledge	Dr. H.G. Petersmann (P.S. to Foreign Secretary)

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The Prime Minister suggested, and Chancellor Schmidt agreed, that after hearing reports from their Ministers of Finance and Foreign Ministers on their separate bilateral discussions, there should be an exchange of views on East/West relations and defence. The Prime Minister asked the Chancellor of the Exchequer to open the discussion.

Financial Matters

The Chancellor of the Exchequer said that he had explained to Herr Matthöfer the UK Government's approach to public expenditure and public borrowing and the strong need which the Government saw to release energies and give new incentives in the private sector, especially to small firms. The Government saw the strengthening of the UK economy as itself making an important contribution to the strength and success of the Community. Sir Geoffrey Howe said that, in response to a question from Herr Matthöfer, he had explained that the Government would consider afresh the UK position on the EMS but that there could not be an immediate decision. Sir Geoffrey Howe went on to say that he and Herr Matthöfer had discussed the Regulation, which was to be taken at the EEC Finance Council on 14 May, covering the interest rate subsidy to Italy and Ireland as less prosperous countries participating fully in the EMS. He had told Herr Matthöfer that, provided the UK's position could be safeguarded in the event of her own full participation, the UK need not hold up the Regulation. He and Herr Matthöfer had agreed that a formula should be negotiated which would safeguard the UK without prejudicing Italy and Ireland. Sir Geoffrey Howe said that he and Herr Matthöfer had had a useful discussion about the UK's net contribution to the EEC Budget. He had told Herr Matthöfer that, whatever the reasons which had brought about the present situation, the present and prospective scale of the net contribution was not one which any British Government could justify to the British people. It was damaging in terms of public expenditure and the balance of payments and would hamper the Government's efforts to put the economy right. This could not be in the interest of a vigorous Community.

Herr Matthöfer, Sir Geoffrey Howe continued, had stressed the importance of holding firm to the one per cent ceiling on the "VAT tranche" of contributions to the Budget. This ceiling might well be reached early in the 1980s. The Germans thought that this would enforce a restructuring of Community expenditure. Herr Matthöfer had, however, noted Sir Geoffrey Howe's view that although both the VAT ceiling and a restructuring of expenditure were necessary and would be helpful, they were very unlikely to deal with the fundamental British problem. He and Herr Matthöfer had discussed frankly some of the possible approaches to remedial action, including, on the British side, the possibility of an

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adapted or perhaps different overriding financial mechanism.

Sir Geoffrey Howe went on to say that on the question of short term help for Turkey, Herr Matthöfer and his colleagues had urged the UK to reconsider the size of their contribution. He had told them that the Government would look at this again, despite the need to contain public expenditure. The value and importance of close collaboration between the major industrialised countries on international economic and monetary affairs had also been discussed and the UK and German views on this were in line.

Herr Matthöfer agreed with Sir Geoffrey Howe's summary of their discussions.

Community Affairs

Chancellor Schmidt told the Prime Minister that she should take account of the psychological impression which would be created in the Community if it was thought that the UK wished to embark on a further renegotiation of her terms of entry to the EEC. The Prime Minister interjected that the UK had no intention of doing so. Reverting to the one per cent VAT ceiling, Chancellor Schmidt said that he thought that it would be helpful if the UK and the FRG were to emphasise their determination not to raise this. This would be the best way of enforcing a reform of the CAP. The Prime Minister said that she wished to stress that the UK could not be of much help to anybody if the Government did not turn the UK's economy round. In recent years, there had been too much emphasis on the distribution of wealth and too little on its creation. The new Government also had to reduce the dependence on government which had grown up, as well as the Government's share of the national income. The Government proposed to make major changes in economic strategy which, if successful, would enable the UK to make a significantly greater contribution to the Community. The Prime Minister said that she did not under-estimate the difficulties but the change of strategy must be accomplished if the UK was to be an effective ally and partner not only in Europe but on international issues such as the North/South dialogue. The

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Government was determined that the UK should be a faithful and good ally: the turn-round in economic strategy would be the Government's major task in achieving this.

Chancellor Schmidt said that, on the financial aspects of the CAP, it would be helpful if the UK were to prepare a first draft of her desiderata in three or four weeks time so that bilateral talks could take place before the UK's proposals were tabled in Strasbourg. Herr Schmidt expressed the view that the importance of these matters went beyond the competence of Minister of Agriculture or even of Finance Ministers; they were of general political importance. Chancellor Schmidt said that he was on the UK's side so far as agricultural surpluses were concerned; there was, for example 5 kilogrammes of milk powder in store for every European. The sales of cheap butter to the Soviet Union spoke for themselves and the Community's sugar policies were not right either. The Chancellor of the Exchequer said that he had not discussed CAP finances in detail with Herr Maffhøfer; but he had to point out that even if the changes in the CAP which the UK wished to see/ ^{took place,} and even if the one per cent ceiling on the VAT tranche were adhered to, the UK would still feel strongly that her net contribution to the total Budget of the Community was too large. If Member States were looking to the EEC to achieve greater convergence in the economies of its Members, it was quite wrong that the system of budgetary contributions should actively obstruct this process. The Prime Minister said that the cost of the CAP was at present financed in such a way that the UK, as the seventh poorest Member of the Community, had become the largest net contributor to the Community Budget.

Recalling an earlier remark of Chancellor Schmidt's, the Prime Minister asked him to what extent the UK's attitude towards the EMS would help on other Community issues. Chancellor Schmidt said that he had first to point out that, according to the FRG's figures, the UK was not the largest contributor to the Community's Budget. He suggested that the Prime Minister might check her figures with Mr. Roy Jenkins. On the EMS, he did not wish to ask

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the UK to take any particular action but it was obvious that the political and psychological impact if the UK were to enter the EMS at an early date would be considerable and would have an effect on other issues. The Prime Minister said that she certainly hoped that this would be the case. It might be difficult to reach a decision in advance of the exchange rate review in September. In the meantime, Strasbourg would be an important occasion for the Government to set out its different strategy to the Community and this would be done.

International Questions

The Prime Minister asked the Foreign and Commonwealth Secretary to report on his discussions with Herr Genscher. Lord Carrington said that he and Herr Genscher had exchanged views, over breakfast, about the UK's approach to the EEC, the Berlin question, NATO forces and defence issues. Herr Genscher had told him about his recent visit to Spain and of the Spanish interest in reaching a solution of the problem of Gibraltar; this would have to be tackled in the context of Spain's accession to the EEC. He and Herr Genscher had discussed Southern Africa; he had told Herr Genscher of the Government's commitments on Rhodesia and that they had not yet decided on the method of their approach to a resolution of the problem. Herr Genscher had expressed the view that the problems of Namibia and Rhodesia were closely related. There had also been an exchange of views on SALT II and SALT III and they had agreed that SALT III would be vital to the interests of Europe. There had been some discussion of MBFR and the latest Soviet approach to the Americans about the negotiations. Herr Genscher had raised the question of a possibly adverse Soviet reaction, in the context of Berlin, to the European Elections. The Middle East had been discussed in general terms.

Herr Genscher said that he had nothing to add to Lord Carrington's summary of their talk.

Chancellor Schmidt said that he would like to say a word about the attitude of the two governments to the ratification of SALT II. Despite some private criticisms and some misgivings,

the Federal Government would be careful not to allow these to come into the open and would give President Carter every assistance in his fight for ratification. Chancellor Schmidt said that he believed that if President Carter were to lose this battle, trust and confidence between the Soviet and American leaderships, which had already been diminished in recent years, would be further damaged. This could have an undesirable effect on the Soviet leadership and particularly, given Brezhnev's ailing health, on a new Soviet leader. If the United States Senate were to refuse ratification, after so many years of negotiation to which three US Presidents had been committed, a change of climate in East/West relations could result. There would be less eager or positive comments on SALT II from Paris but, the Chancellor thought, French reactions would not be negative. So far as SALT III was concerned, he expected that the French would stick to the line of refusing to participate in any aspect of these negotiations which could affect the national interests of France.

There followed a discussion of a number of questions concerning nuclear weapons. It was agreed that the Defence Secretary and the Federal Minister of Defence, Herr Apel, would have a private meeting in Brussels on 14 May to pursue these matters further.

East/West Relations

At the Prime Minister's invitation, Chancellor Schmidt said a few words about the Federal Government's approach to East/West relations. Chancellor Schmidt said that his Government's position was that they should endeavour energetically to reduce tension with the Soviet Union and her allies but on the basis of continuous Soviet awareness that the Alliance was strong enough to deter aggression or to defend itself if aggression were committed. This could be achieved by maintaining a credible balance of forces. The coalition government in Bonn, and the Chancellor and Herr Genscher personally, could be relied upon to adhere firmly to their policy of doing everything necessary to maintain the defences of the FRG at an effective level, but without entering the nuclear field and without

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enlarging the FRG's armed forces any further. FRG policies were necessarily conditioned by the fact that Germany was a divided country and that the situation of Berlin was precarious. His Government's policy on detente was, however, seriously motivated and not simply designed as an exercise in public relations.

Berlin

Chancellor Schmidt said that he would like to mention the enormous impact of The Queen's visit to Berlin. It might not be appreciated in the UK how much the British contribution to the guarantees given to Berlin by the three Western powers meant to the stamina of the Berliners. Trouble could be expected over the European Elections. In this context, Chancellor Schmidt said, it would be very helpful if the Prime Minister could agree to see the governing Mayor of Berlin when he visited the UK on 24 and 25 May. A photograph of the Prime Minister receiving Herr Stobbe would have a very good effect in Berlin. The Prime Minister took note and said that this could be pursued through Ambassadors.

Rhodesia

The Prime Minister invited the Foreign and Commonwealth Secretary to summarise the Government's policy on the Rhodesia question. Lord Carrington said that the Conservative Party had for long believed that the internal settlement in Rhodesia had not been given a fair run. Ian Smith had admittedly been very slow in seeking an acceptable agreement; but he had belatedly decided to do everything which had been asked of him for so long and all the Six Principles save the final one - the acceptability of any settlement to the people of Rhodesia as a whole - had been satisfied by the end of 1978. It had then been decided to hold an election and the Conservative Party had sent observers to report on whether the election had been free and fair. Their report had not yet been submitted to the Prime Minister but the general view seemed to be that the election had indeed been fair and this would mean that all six Principles had been fulfilled. In this situation, the Government would have the positive duty to bring Rhodesia back

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to legality. The fact that 64% of the population of Rhodesia had turned out to vote in the election in Rhodesia could not and should not be ignored. Even if the new constitution was not, from some points of view, very sensible, the human rights of such a substantial proportion of the population could not be ignored. The Government had not yet considered the means by which it would fulfil its commitments and would wish to have discussions with the friends of the UK, and particularly with the United States.

The Prime Minister commented that the internal settlement should have been supported by the British Government from the beginning; if this had been done, other Africans would have followed suit. There were not many countries in Africa which conducted their affairs on the basis of one man/one vote and in which the electorate could choose between four parties. The vote by the white population for black majority rule represented a major advance. Rhodesia was a country rich in natural resources and occupying a vital strategic position; it could exercise a beneficial influence on the whole region of Southern Africa. Dr. Kissinger had made a significant advance towards solving the Rhodesia problem but the resulting conference in Geneva had been badly chaired and altogether mishandled. Zambia was using the railway through Rhodesia for the import of maize and fertilisers and should have no grounds for objection if the Salisbury regime were to be recognised. There was no longer any reason to retain Rhodesia's illegal status.

Chancellor Schmidt said that he had indeed been impressed by the recent election in Rhodesia and would like to be informed of the report by the British team of observers. During the past two years, there had been close collaboration between the "Five" in the Security Council on Southern Africa: it would be important for the UK to convince this group of her case, so that further co-operation in that forum would not be impaired. Lord Carrington pointed out that public opinion in the UK was overwhelmingly in favour of recognition and the Government would have to satisfy this; they could not move too softly or too slowly. He had told Herr Genscher that a Conservative Government might have a better chance than their predecessors in persuading the South Africans not to break off negotiations with the United Nations on Namibia.

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Turkey

In a brief exchange on aid to Turkey, the Prime Minister said that the British Government would help as much as they could. Chancellor Schmidt commented that the contribution to the short-term assistance operation offered by the Labour Government had fallen far short of expectations. Herr Matthöfer said that one telephone call from Bonn to Vienna had produced from the Austrians the same amount as the UK had offered to contribute. The Prime Minister asked whether the FRG, like the UK, used export credit guarantees as a form of welfare. So far as Turkey was concerned, export credit guarantees amounted to giving the Turks goods for which they had no intention of paying. The Turks must to some extent help themselves by imposing tighter discipline and accepting the disciplines required by the IMF. Chancellor Schmidt commented that the Turks were a proud people and not very amenable to discipline.

Future Consultations

Chancellor Schmidt said that he hoped that the Prime Minister would consider having the next Anglo-German meeting in Bonn in the autumn and that this could be mentioned at their press conference. The Prime Minister agreed to this and commented that at their next meeting they should allow more time for discussions.

The plenary session ended at 1150.

Bym.

C.C. Master Set

Extracts on Turkey, May 1979

- " - Euro. Policy (CAP), May 1979

- " - SALT - Defence, May 1979

- " - Situation in Rhodesia, May 1979

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