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NOTE OF A MEETING WITH ITALIAN FINANCE MINISTER
AT NO.11 DOWNING STREET AT 11.00 A.M.
ON 19 OCTOBER 1984

Present Chancellor of the Exchequer
 Mr Unwin

 Signor Gorla
 Signor Sarcinelli

After an initial exchange of courtesies the Chancellor invited Signor Gorla to say something about his recent Budget.

2. Signor Gorla said that his starting point had been the very heavy burden of public debt in Italy that had accumulated since the early 1970s. The interest on this debt now accounted for 10 per cent of GNP. Although, luckily, so far Italian savers had largely been content to reinvest this interest - so that it had been available to finance further public borrowing - this was an unstable situation. He had therefore decided on a five year plan strategy designed, by about 1988, to achieve a situation where there was no further increase in the ratio of public debt to GNP, and the annual public sector deficit was no larger than interest paid on outstanding debt.

3. To bring this about he was looking for:-

- (i) an increase in tax revenue, over the period, at the same rate as the increase in nominal GNP.
- (ii) Current public expenditure remaining constant in real terms (ie., with a 3 per cent growth rate, rising at 3 per cent less than tax revenues).
- (iii) Public investment expenditure rising at the same rate as GNP.



4. This involved detailed, and difficult, work to control public expenditure - ranging from public pay and pensions to central Government transfers to the regions. Health expenditure was proving particularly difficult to control and monitor. Indeed it was possible that a particular difficulty in 1985 could relate to disbursement of health expenditure contracted by local bodies in 1984 but not yet disbursed.
5. The Chancellor asked about central Government control over provincial authorities. Signor Gorla said that although the expenditure of such authorities accounted for nearly 10 per cent of GNP, and although many were in communist hands, central Government was able to maintain control because of the very low proportion of their expenditure (10 per cent) that was financed by local taxes. By law the provinces had to have balanced budgets.
6. Returning to central Government borrowing, Signor Gorla said a further objective was to increase the average maturity of outstanding Government debt which had been only 6 to 8 months when he took office.
7. The Chancellor explained that he shared many of Signor Gorla's problems, including the particular problem of expenditure on health deriving from lack of control over doctors' prescribing habits.
8. Turning to Community issues, the Chancellor said he was grateful to Signor Gorla for the assistance he had given at the Luxembourg ECOFIN in making progress on budgetary discipline. The Community was now close to agreement, and he would like to see this reached as quickly as possible.
9. Signor Gorla agreed. He was personally convinced that improved financial discipline was needed in the Community. There should be no going back on the principles of Fontainebleu. He also felt Finance Ministers had to play an important role. Even if there were appeals from Finance Ministers' decisions, Finance Ministers would have to be present at those Council meetings where such appeals were heard.
10. On the question of the French reserve on base drift he thought it important to have a system that would work in practice. There were situations where "original" budgets might be higher than "actual" budgets (for example if food prices had fallen). He would like to see forecasts of what might happen on the two different bases.



11. As to the nature of the budgetary discipline agreement he felt that it would be easier to get the system to work if the agreement took a form less likely to cause difficulties in the European Parliament, or strong domestic reactions in member states. More generally, the compromise reached in Luxembourg represented a difficult balance for many countries, between opposing internal forces: it was most important, therefore, not to allow the substance of the text to be reopened. The Chancellor said that he strongly agreed.

12. The meeting ended at 12 noon.

13. In subsequent discussion, over lunch, Signor Gorla explained to the Chancellor the difficulties holding up the appointment of the second Italian Commissioner. These related to the growing strength of the communists in the opinion polls, and increasing expectation that they would do well in next year's local elections. This development had made the minority parties in the Government coalition uneasy about turning down, directly, the Communist request to nominate the second Commissioner.

14. The latest idea was that a new working "rule" should be proposed and adopted - that no one should be appointed Commissioner unless they had served a term in office as a Government Minister. (This of course would automatically rule out any Communist). If that rule were adopted, Signor Gorla was confident that the Italian nomination for their second Commissioner would be a socialist, Signor Forte.

DLCP

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D L C PERETZ
22 October 1984