



Lee PC
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RECORD OF A DISCUSSION BETWEEN THE CHANCELLOR AND THE
FEDERAL GERMAN FINANCE MINISTER AT CHEQUERS
AT 10.30 A.M. ON 2nd MAY 1984

Present	Chancellor of the Exchequer	Dr Stoltenberg
	Mr Unwin	Dr Heck
	Mr Peretz	

Economic Developments

Dr Stoltenberg said that in both Germany and the UK the recovery was now well under way: both economies were doing better than elsewhere in Western Europe. The latest independent forecasts for Germany were for a growth rate of 3-3½ per cent. The prospects, however, depended also on whether other European countries could now achieve higher growth; on the continuing debt problems of some developing countries; and on a satisfactory resolution of the expected clash with the unions over their demand for a 35 hour week. Dr Stoltenberg was confident that the German employers would stand firm. According to opinion polls the demand for a 35 hour week was not popular. But there could be a nation wide strike sometime during the next 2 months.

2. Inflation in the Federal Republic was well under control, and should fall to below 3 per cent soon. Profits were rising, as were private investment and exports. Dr Stoltenberg thought that a satisfactory resolution of the current problems in the Community could also have a helpful impact on confidence in the medium term. Unemployment was showing the first signs of a modest fall. There was of course the risk of a rise in interest rates. Although the strike threat had weakened the Deutschemark it had not so far affected domestic German interest rates. But were US rates to rise further then Dr Stoltenberg would expect a modest rise in German rates.

3. The Chancellor said that the picture in the UK was in many ways similar. Inflation was of course a little higher than in Germany, but expected to edge down later in the year. Growth was around 3 per cent. The UK, too, had labour problems (the coal strike). The



main worries for the future were of a rise in interest rates, caused by a rise in US rates. Such a rise would of course cause problems for debtor countries as well as the developed countries.

4. Dr Stoltenberg expressed a particular concern over the steel industry. He thought there was a risk of pressure from other EC countries - particularly the French - for a renewal of steel subsidies after they had been phased out (as agreed) next year. We should stick to the agreement that had been made to terminate subsidies, which were, he was advised, in any case illegal under the European treaties. The Chancellor agreed. Although this was a matter primarily for Industry Ministers, Finance Ministers had a legitimate and common interest, and he was very happy for the matters to be raised, as Dr Stoltenberg suggested, at the informal ECOFIN on 12 and 13 May.

London Economic Summit

5. The Chancellor suggested a number of areas where it might be possible to make some modest progress at the London Summit:-

(a) On the international debt situation, he suggested it would be worth examining some of the ways that problems might be solved in the longer term, and in particular the greater role that direct private investment could and should take in developing countries financing. It would be wrong for Governments to become involved, but the World Bank might be able to play a larger role (in cooperation with the IMF). Banks would also have to accept the inevitability of stretching out repayment schedules. Dr Stoltenberg agreed, and hoped (and the Chancellor agreed) that no one at the Summit would produce any new ideas for global schemes of general debt relief.

(b) It would be useful to apply further pressure - following the US/Japanese bilateral discussions - on the Japanese to open up their capital markets, as one way to help deal with the problem of the under-valued yen.

(c) On the US deficit the Chancellor thought the Americans might now be politically prepared to see something helpful said at the Summit, and Dr Stoltenberg agreed.



(d) On trade and protectionism, the Chancellor asked Dr Stoltenberg for his views, in particular, on how the question of mixed credits might best be tackled. It was agreed that this was a subject for discussion at the forthcoming OECD Ministerial meeting first; but that, depending how that discussion went, it would be helpful to have something in the Summit communique covering both protectionism and mixed credits.

6. In further discussion about US prospects, Dr Stoltenberg contrasted the very impressive growth so far in the US economy - the result of a flexible and dynamic private sector - with the problems that seemed to be mounting up for the future on the fiscal deficit, the trade balance and balance of payments. He was not convinced that the US would be able to sustain economic growth, and saw a real danger of disruption sometime in 1985 or 1986. While it was right for European leaders to express concern about this, careful wording was needed. It was important to avoid giving a "protest" image that could reinforce market and public perceptions of a Europe that was in decline. The Chancellor agreed.

7. On Argentina, Dr Stoltenberg shared the Chancellor's concern about the end-March US operation. He could only interpret the US move as intended to buy time to convince the Argentine Government of the need to agree a satisfactory adjustment programme with the IMF. This meant, however, that it was important that the next ~~dead~~ ^{was} line should not be allowed to pass in the same way. He agreed with the Chancellor on the importance of ensuring that any country that did default ~~£~~ not seen to benefit as a result.

Distribution

PS/Chief Secretary
 PS/Economic Secretary
 Sir P Middleton
 Sir T Burns
 Mr Littler
 Mr Unwin
 Mr Lavelle
 Mr Mountfield
 Mr Bottrill
 Mrs Case
 Mr Kelley
 Mr Ridley

DLCP

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3 May 1984

Mr Coles - No.10
 Mr Appleyard - FCO
 Mr McCarthy - DTI
 PS/Governor - Bank of England
 Sir J Taylor - Bonn
 Mr Wicks - Washington