



ECFO 001/20

OO FCO DESKBY 201930Z

PP BRUSSELS

PP COPENHAGEN

PP THE HAGUE

PP ROME

PP DUBLIN

PP PARIS

PP BONN

PP LUXEMBOURG

PP ATHENS

GRS 1100

SECRET

DESKBY 201930Z

FM UKREP BRUSSELS 201800Z MAR 83

TO IMMEDIATE FCO

TELEGRAM NUMBER 1206 OF 20 MARCH 1983

INFO PRIORITY BRUSSELS COPENHAGEN THE HAGUE ROME DUBLIN PARIS
BONN LUXEMBOURG ATHENS

E.M.S. REALIGNMENT CONFERENCE

SUMMARY

1. MINISTERIAL MEETING ADJOURNED THIS AFTERNOON WITHOUT AGREEMENT. WILL RESUME AT 9 AM TOMORROW IN HOPE OF REACHING AGREEMENT BEFORE EUROPEAN COUNCIL IN LIGHT OF OVERNIGHT CONSULTATIONS. CENTRAL BANK GOVERNORS HAVE AGREED THAT WHEN MARKETS OPEN TOMORROW, THE OFFICIAL INTERVENTION RATES WILL BE DECLARED TEMPORARILY SUSPENDED AS ALSO THE OFFICIAL DAILY FIXING IN THOSE COUNTRIES WHERE THAT APPLIES. KEY ISSUE IN DISPUTE IS EXTENT AND DISTRIBUTION OF SPREAD BETWEEN FRENCH FRANC (FF) AND DEUTSCHE MARK (DM).

DETAILED REPORT

2. MONETARY COMMITTEE YESTERDAY MORNING IDENTIFIED FOLLOWING MAIN ISSUES FOR DECISION BY MINISTERS:-

(I) EXTENT OF SPREAD BETWEEN FF AND DM CONSENSUS WAS FOR 7 - 9 PER CENT:

(II) POSITIONS OF INDIVIDUAL COUNTRIES. GERMANS WERE PREPARED TO MOVE UPWARDS MORE THAN HALFWAY BUT FRENCH RESISTED ANY DOWNWARD MOVEMENT OF FF AT ALL. OTHER MEMBERS IN GENERAL PREPARED TO SLOT IN (BELGIUM, LUXEMBOURG AND DENMARK FOLLOWING DM IN PART; ITALY AND IRELAND MOVING TO BOTTOM OF SPREAD; AND DUTCH PROBABLY FOLLOWING DM):

(III) BACK UP MEASURES TO MAKE REALIGNMENT CREDIBLE. NO SPECIFIC PROPOSALS EMERGED BUT FRENCH HINTED AT FURTHER MEASURES TO REDUCE DEMAND:

(IV) WIDENING OF INTERVENTION MARGINS. NOT FAVOURED BUT OFFERED FOR CONSIDERATION AS TEMPORARY MEASURE (SAY, TO 4 PER CENT) TO SECURE LAST DITCH SOLUTION.

3. AT SERIES OF MINISTERIAL MEETINGS YESTERDAY (WITH STOLTENBURG IN CHAIR) FRENCH (DELORS) REFUSED ANY CONCESSION AND THREATENED TO WITHDRAW FROM E.M.S. UNLESS GERMANS WILLING TO BEAR COMPLETE BURDEN OF AT LEAST 8 PER CENT ADJUSTMENT. CORE OF ARGUMENT WAS

IMMEDIATE

ADVANCE COPY

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PS

MR EVANS

MR HANNAY

CAB. OFFICE } PS MR R. ARMSTRONG
MR HANCOCK

MAFF } MR. HAYES.
MR ANDRESS

TREASURY } MR LITTLE
MR HEDLEY-MILLAR
MR MONCK
MR PERETZ

BANK OF ENGLAND } PS/GOVERNOR
MR GILL

NO 10.

DUTY OFFICER

D/B
202000Z

R.C.

3. AT SERIES OF MINISTERIAL MEETINGS YESTERDAY (WITH STOLTENBERG IN CHAIR) FRENCH (DELORS) REFUSED ANY CONCESSION AND THREATENED TO WITHDRAW FROM E.M.S. UNLESS GERMANS WILLING TO BEAR COMPLETE BURDEN OF AT LEAST 8 PER CENT ADJUSTMENT. CORE OF ARGUMENT WAS THAT FOLLOWING JUNE 1982 REALIGNMENT FRANCE HAD TAKEN SERIES OF MEASURES TO RESTORE CONTROL OVER ECONOMY: THESE WOULD TAKE TIME TO WORK AND THERE WOULD STILL BE SUBSTANTIAL GAP BETWEEN FRENCH AND GERMAN INFLATION AT END 1983. FRANCE COULD NOT BE EXPECTED TO MAKE FURTHER SACRIFICES WHICH WOULD JEOPARDISE ATTEMPTS TO MASTER INFLATION. GERMANY MUST THEREFORE TAKE RESPONSIBILITY FOR ADJUSTMENT BY REVALUING DM. IF FRANCE LEFT E.M.S. PROTECTIONIST POLICIES WOULD ALSO BE INTRODUCED. DELORS MADE MUCH OF CURRENT CRITICISM OF E.M.S. AND COMMUNITY GENERALLY IN FRANCE, AND PRODUCED LIST OF UNRESOLVED GRIEVANCES, WHICH HE EVEN ARGUED IN HIS OPENING STATEMENT, WOULD HAVE TO BE RESOLVED AS A PRIOR CONDITION FOR CONTINUED FRENCH MEMBERSHIP OF THE EXCHANGE RATE MECHANISM. THIS WAS SEVERELY CRITICISED BY THE ITALIANS (GORIA).

4. GERMANS OFFERED TO GO MORE THAN HALF WAY BUT ARGUED STRONGLY THAT EXCESSIVE REVALUATION OF DM WOULD THREATEN INCIPIENT GERMAN ECONOMIC RECOVERY. RECENT INTEREST RATE REDUCTION HAD MADE SIGNIFICANT CONTRIBUTION TO EASING PRESSURE ON FF; AND MONEY SUPPLY HAD BEEN INCREASING AT EXCESSIVE RATE.

5. AFTER OVERNIGHT CONSULTATIONS DELORS CONFIRMED IN PLENARY THAT FRANCE INSISTED ON 8 PER CENT SPREAD AND GAVE SIGNS OF BEING WILLING TO ACCEPT SOME DOWNWARD MOVEMENT OF FF, POSSIBLY WITHIN WIDENING OF MARGINS FROM TWO AND A QUARTER PER CENT TO 3 PER CENT. HE ALSO GAVE NOTICE OF FRENCH REQUEST FOR 4 - 5 BILLION DOLLAR CREDIT FACILITY FROM 1981 COMMUNITY LOAN MECHANISM AND INDICATED THAT FRENCH GOVERNMENT WOULD ANNOUNCE TOMORROW OR TUESDAY NEW MEASURES TO RESTRAIN DOMESTIC DEMAND, WITH A VIEW TO ELIMINATING THE TRADE DEFICIT BY END 1984.

6. DISCUSSIONS THEN CENTRED ON SERIES OF NEGOTIATIONS ON POSSIBLE ALLOCATION OF 8 PER CENT SPREAD. (THESE WERE UNREAL IN AN ECONOMIC SENSE, BECAUSE THERE WAS NO FIXED REFERENCE POINT AGAINST WHICH THE VARIOUS COMBINATIONS WERE OR COULD BE MEASURED; BUT THEY ASSUMED ENORMOUS POLITICAL IMPORTANCE). CURRENT POSITION IS THAT GERMANS ARE UNWILLING TO INCREASE DM BY MORE THAN 5 PER CENT, AND FRENCH TO REDUCE FF BY MORE THAN 2 PER CENT, ALTHOUGH AT ONE TIME FRENCH SEEMED WILLING TO CONTEMPLATE 2.5 PER CENT. ALL ATTEMPTS TO COMPROMISE HAVE SO FAR FAILED (EG CHANCELLOR SUGGESTED DM + 75 PER CENT AND FF - 2.75 PER CENT) AND DELORS HAS ACCORDINGLY RETURNED TO PARIS TO CONSULT PRESIDENT.

7. IF AGREEMENT CAN BE REACHED BETWEEN FRENCH AND GERMANS, OTHERS SHOULD FIT IN FAIRLY EASILY. POSSIBLE REALIGNMENT ON BASIS OF DM + 5 PER CENT AND FF - 2.5 OR 3 PER CENT WOULD BE:-

DUTCH GUILDER + 3 PER CENT

BELGIAN FRANC, LUXEMBOURG FRANC AND DANISH KRONE + 1 PER CENT

ITALIAN LIRA WITH FF

IRISH PUNT - 4 PER CENT

8. IN VIEW OF MARKET REPERCUSSIONS CENTRAL BANK GOVERNORS (WITH GREAT RELUCTANCE AND APPREHENSION) AGREED THAT FROM OPENING TOMORROW AUTHORITIES WOULD TEMPORARILY SUSPEND THEIR OBLIGATORY BUYING AND SELLING RATES FOR THEIR PARTNERS' CURRENCIES (THOUGH RETAINING THE RIGHT, IF THEY WISHED, TO INTERVENE AT RATES OF THEIR CHOOSING) AND, WHERE APPLICABLE, CANCEL THE OFFICIAL FIXING IN THEIR MARKET. THIS MAY BE WRONGLY DESCRIBED AS 'CLOSING MARKETS', BUT COMMERCIAL TRANSACTION WILL, OF COURSE, CONTINUE.

9. MINISTERS AGREED THAT STOLTENBERG SHOULD INFORM PRESS BRIEFLY, WITHOUT MENTIONING ANY FIGURES, OF ADJOURNMENT OF DISCUSSION. BUT SEVERAL MINISTERS (NOTABLY DELORS) HAVE SPOKEN TO PRESS AND

9. MINISTERS AGREED THAT STOLTENBERG SHOULD INFORM PRESS BRIEFLY, WITHOUT MENTIONING ANY FIGURES, OF ADJOURNMENT OF DISCUSSION. BUT SEVERAL MINISTERS (NOTABLY DELORS) HAVE SPOKEN TO PRESS AND MAIN FIGURES SEEM WELL KNOWN.

COMMENT

10. PROSPECTS FOR EARLY AGREEMENT TOMORROW DIFFICULT TO ASSESS. DELORS PERSONALLY SEEMS TO WANT TO REACH AGREEMENT AND HAS MADE CONCESSIONS FROM OPENING POSITION BUT HAS SO FAR BEEN UNABLE TO GET NECESSARY BACKING TO CLINCH DEAL. REPORTS OF IMPENDING FRENCH GOVERNMENT RESHUFFLE COULD LEAD TO STRENGTHENING OF HIS HAND, BUT TIME IS SHORT IF DEAL TO BE STRUCK WITH GERMANS BEFORE TOMORROW MORNING. IF DELORS UNABLE TO GET BACKING OVERNIGHT, AGREEMENT BY FURTHER NEGOTIATION IN PCESENT MINISTERIAL GROUP TOMORROW MORNING SEEMS UNLIKELY AND BUCK MAY WELL THEREFORE HAVE TO BE PASSED TO EUROPEAN COUNCIL. NEGOTIATIONS HAVE NOT BEEN HELPED BY POOR CHAIRMANSHIP BY STOLTENBERG WHO, DESPITE DIFFICULTIES, COULD IN OUR VIEW HAVE MADE GREATER EFFORTS TO BRIDGE SMALL FINAL GAP.

11. CHANCELLOR WILL REMAIN IN BRUSSELS FOR RESUMED MEETING TOMORROW (BUT WILL HAVE TO LEAVE BY LATE MORNING IN VIEW OF COMMONS BUDGET DEBATE). FINANCIAL SECRETARY WILL, AS PREVIOUSLY PLANNED, ATTEND ECOFIN (WHICH IS DUE TO FOPLOW RESUMED MEETING). UNWIN WILL STAY ON IN BRUSSELS TO BRIEF EUROPEAN COUNCIL DELEGATION.

FCO ADVANCE TO:

FCO - PS/SOS: EVANS: HANNAY

CAB - PS/ARMSTRONG: HANCOCK

MAFF - HAYES: ANDREWS

TSY - LITTLER: HEDLEY-MILLER: MONCK: PERETZ

BANK - PS/GOVERNOR: GILL

NO.10 - DUTY OFFICER (DESKBY 202000Z)

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