



RECORD OF A CONVERSATION BETWEEN THE CHANCELLOR AND M. JACQUES CHIRAC:
4.30PM, 30 NOVEMBER 1983, NO 11 DOWNING STREET

Present:

Chancellor
 Mr Kerr

M. Chirac
 M. Kosciusko-Morizet

Community Issues

M. Chirac asked about the prospects for the European Council in Athens. Had he been correct to detect in London signs of some willingness to compromise?

2. The Chancellor said that what he had detected was some convergence of views between London, Bonn and Paris. All agreed that the problem of budgetary imbalances must be solved, though views still differed on the appropriate form of the solution. All agreed too that substantial improvements in expenditure control, particularly on agriculture, were required, and the French paper tabled at the Special Council in Brussels on 28 November had shown that French views on the nature of the system were now closer than before to those of the United Kingdom. But there might be a substantial gulf at Athens between the views of France, Germany and the United Kingdom, on the one hand, and their other partners, on the other. We still hoped for an overall settlement - or failing it agreement on the principles and outline of an overall settlement - at Athens. And without a satisfactory overall settlement, we were clear that there could be no increase in own resources.

3. M. Chirac thought that too much was being asked of Heads of Government in Athens. The package of issues for decision had grown much too big. And, given the current plight of the French economy, it would be very difficult for M. Mitterrand to make many



concessions at Athens. He wondered whether the UK Government really favoured enlargement: there was a major groundswell of opposition in Southern France to Spanish and Portuguese accession.

4. The Chancellor confirmed that HMG did still favour enlargement. We however thought it very important to impose an effective discipline on the CAP before Spanish accession.

5. M. Chirac then asked about the chances of the United Kingdom joining the EMS exchange rate mechanism. The Chancellor said that this was certainly not excluded, for there was no UK objection in principle, and the matter was kept continually under review. However there were two problems. First, sterling remained a petro-currency, for the markets exaggerated the extent to which oil price changes affected the UK economy. Perhaps the market's perception might change when North Sea production peaked within the next couple of years: for the present, however, it remained the case that developments, eg. in the Middle East, which could have an effect on world oil prices, produced diametrically opposed movements in sterling and in the other EMS currencies. Secondly, sterling was still a widely-traded international currency. The extent of movements in sterling across the exchanges could put some strain on the EMS, and it was debatable whether the EMS was now well placed to cope with new strains. The Chancellor added that one great merit of the EMS was that it imposed an external financial discipline, which could be very valuable in affecting domestic economic policies in some countries. Such an external discipline was not however necessary in the United Kingdom in current circumstances: we had, since 1979, imposed our own discipline, internally.

6. M. Chirac agreed, and assumed that the Chancellor's reference was to France. The RPR were firmly opposed to the idea of France leaving the EMS.



UK and French Economies

7. M. Chirac then referred to "impressive evidence" of UK recovery. The Chancellor confirmed that we had seen growth of approximately 2½ per cent a year since the trough of the recession in early 1981. We expected 3 per cent this year and next. Inflation was down from 20 per cent to 5 per cent, and the future prospect remained good - perhaps 5½ per cent in the first half of 1984, and 4½ per cent in the second half. Employment was rising, and unemployment appeared to have stabilised. Investment was up, and a further 4 per cent increase was expected next year.

8. M. Chirac said that he had been struck by the change in the UK's overall economic climate. Kirkland of AFL/CIO had recently stressed to him how well-justified had been the UK Government's firm approach to the trade unions. Privatisation too seemed to be a considerable success: he had been particularly struck by the NFC management buy-out.

9. In France, M. Chirac said, it was clear that the Delors plan was failing. Inflation over the year would come out at 10 per cent, rather than 8 per cent. Unemployment was rising steeply, and the true figure was nearer 13 per cent than the Government estimate of 10 per cent. The balance of payments deficit had been reduced, but a surplus of FF 18 billion would be required each year merely to service outstanding debts. At the end of his own term as Prime Minister, France's overseas debt amounted to some FF 32 billion: the figure now was FF 515 billion. And the domestic economy was stagnating - which of course explained why major concessions at the European Council in Athens were simply not possible for France. The Chancellor commented that since Government and Opposition alike in France now argued for stricter public expenditure control, agreement on a proper Community spending control system would be



consistent with, and indeed helpful to, the aim the RPR shared with M. Delors.

10. M. Chirac added that he had only one criticism of the policies which the UK Government had followed since 1979. Would it not have been desirable, and indeed possible, to reduce the overall burden of taxation? And had not raising VAT in 1979 had damaging inflationary consequences?

11. The Chancellor agreed that it would be highly desirable to reduce taxes. The first priority in 1979 and since had however been to reduce the large and rising budgetary deficit which the Government had inherited. Ideally one would reduce both borrowing and taxes, and in the lifetime of this Parliament he hoped that both might be possible; but the first priority after 1979 had had to be reducing the PSBR, now down to some 3½ per cent of GDP from an inherited figure of some 5½ per cent. The VAT increase in 1979 had indeed had some inflationary effect, but only in the short term.

12. M. Chirac agreed that getting borrowing down had to be the number one priority. It would be the number one priority for the next French Government. The opinion poll experts suggested that the combined Opposition Parties now commanded the support of 58 per cent of the French electorate, and local elections were going well for the RPR. But of course the elections need not happen before March 1986, and in the interim the Government planned changes in the election laws and the press laws which would be greatly to their benefit. The political situation in France would continue to hot up.

13. The meeting ended at 5.20pm.

JOK.



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