

PRIME MINISTER

BILATERAL WITH THE CHANCELLOR: 27 APRIL

The Chancellor suggests two items for discussion:

- the market/trade figures etc;
- EC merger control regulation.

The market/trade figures etc

The exchange rate has shown little change today, and in New York is currently at \$1.875 and DM 3.142.

You might discuss with the Chancellor possible market reaction to Friday's trade figures and how this would be handled. In particular what action would be appropriate if the rate substantially strengthens? The approach might be:

- (i) some smoothing intervention would be appropriate, but no more than say \$50 million a day;
- (ii) if upward pressure persists the rate should be allowed to rise;
- (iii) no further reduction in interest rates should be contemplated until the rate reaches say DM 3.20. (Even then I would be worried about a further cut given the overall position of the economy);
- (iv) meantime there would be no harm in the Chancellor repeating his efforts to talk the rate down.

If, on the other hand, the exchange rate was significantly to fall, we should be on the lookout for an opportunity to nudge interest rates up by $\frac{1}{2}$ per cent - if the rate came down to, say, DM 3.10.

EC merger control regulation

This issue is coming to OD(E) later in the week. But I gather the Chancellor may wish to bend your ear about it. We have not shown you the OD(E) papers, as it seems right to let that committee attempt to reach an agreed conclusion before the issue is referred to you. So if the Chancellor raises it, I suggest you simply listen to what he has to say. Lord Young would want to put a contrary view.

In essence the argument is:

- (i) At present EC merger control rests on Articles 85 and 86 of the Treaty. This effectively limits Commission intervention until after a merger has taken place. The Commission now wish to introduce a regulation which, inter alia, would allow them to intervene before a merger was completed.
- (ii) Lord Young thinks we should continue constructive discussion on the possible shape of a regulation, without commitment, against a set of objectives designed to protect UK interests.
- (iii) The Chancellor thinks UK firms stand to gain little from a regulation, and that we should decide now on the objective of killing the idea. ✓

Nationalised industry board salaries

E(NI), chaired by the Chancellor, is discussing nationalised industry board salaries tomorrow afternoon. This issue too may, I fear, eventually have to come to you for resolution (Mr. Ridley has already sent a lobbying note to you that I have not troubled you with). You might like to tell the Chancellor that you hope it will be possible for him to sort it out at E(NI).

PRG.

PAUL GRAY

26 April 1988

EL3CSB

SECRET