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Mr Manfred Lahnstein, the State Secretary in the Federal German Chancellery, visited London on Friday 19 June. During the course of a long conversation which I had with him, he made three points which, he made clear, he was putting at the Chancellor's request, for transmission to the Prime Minister.

The German Political Situation

2. The first point related to the complications of the Chancellor's domestic political situation and of the management of the coalition. Mr Lahnstein said that the size of Germany's budget deficit presented the Government with a great problem about the future of the social transfer system. The present system of transfer payments and social benefits had been designed and brought into effect many years ago, when a continuing high rate of economic growth was taken for granted. Since that time, German society had matured and some of the clan which fuelled the "economic miracle" had evaporated. For other reasons, not confined to Germany, a much lower rate of growth was to be expected in the coming years. Finally, demographic changes since the system was introduced, and notably the increase in the number of old people, had greatly increased the burden of the social transfer system upon the Federal budget. It was now necessary to review the whole system with a view to reducing that burden. This was something into which the Government would be turning its attention in the coming months, with a view to the 1982 budget.

3. This was potentially a very divisive political issue. Germany was conditioned to the existing system of social transfers, which was probably one element in the social cohesion of the country. It followed that a change in the system could have implications for the maintenance of social cohesion. It would also present great difficulties for the coalition. The Free Democratic Party (FDP) might well not be able to agree upon what would need to be done, and it could not be taken for granted that the FDP would be able to remain in a coalition with the Social Democrat Party (SDP) for the rest of the present Parliament.

4. The size of the budget deficit also had implications for defence planning (though these were minor), and for aid to developing countries. Here, too, there could be problems in the coalition. I asked whether it might also present problems from the point of view of the European Community; Mr Lahnstein seemed to think that this was less likely.

5. Mr Lahnstein said that the Federal Chancellor wanted the Prime Minister to be aware of this background to the way in which he would have to deal with domestic and international political problems over the coming months.

6. I said that my impression at Chequers had been that the Federal Chancellor had recovered a good deal of the resilience which appeared to have deserted him after the last election. Mr Lahnstein confirmed this, and attributed it three reasons:

- (i) He had stopped smoking, and the process of adjustment had been very hard for him, but it was now accomplished.
- (ii) He had recently had a medical check-up, and his doctors had given him a good report: that had been very reassuring.
- (iii) He felt that he had now taken the measure of his political problem: at least he knew what he had to try to achieve, and could concentrate on trying to achieve it, though he knew well enough that there could be no guarantee of success.

The Ottawa Summit

7. Mr Lahnstein and I also had some discussion of the arrangements for the Ottawa Economic Summit. On this Mr Lahnstein said that the Federal Chancellor was conscious that four of the participants (five if one included Monsieur Thorn), would be attending their first Summit. The Chancellor thought that it would be important that Heads of State or Government should have as much time as possible for unstructured and informal discussion among themselves during this meeting, so that they had a chance to get to know each other properly and have a real exchange of views. One reason for allowing more time for such discussion was the language problem: it seemed likely that on this occasion at least three of the participants would not be able to cope in English. But the more important reason lay in the need to establish a better

relationship with President Reagan, and to draw him out more extensively on international political issues.

8. Mr Lahnstein said that the Federal Chancellor did not yet know quite what to make of President Reagan. He tended to divide American Presidents into two categories: the pure figureheads like Eisenhower and those who were very much actively in charge of their Administrations, like Kennedy and Carter. President Reagan did not seem to fit neatly into either of these categories. Moreover, he would be coming to the Ottawa Summit with some definite purpose in mind and looking for some advantage or result, but the Germans had not yet worked out what that might be. For all these reasons it would be important for the other Heads of State or Government to draw him out at the Ottawa meeting, to get him to contribute to the discussion and declare his positions.

The Middle East

9. Mr Lahnstein's third main point related to the "Near East". He said that the Federal Chancellor had noted at Chequers that the Foreign and Commonwealth Secretary had said that the Camp David initiative ought to be allowed to run its course until the completion of the Sinai agreements. The discussion had not made clear what the Foreign and Commonwealth Secretary thought should happen after that, or what future he saw for the Camp David process once that was done. I said that I did not know exactly what the Foreign and Commonwealth Secretary had in mind, but that our general view was that there was no possibility of progress in the Middle East without the Americans, that the Camp David process had to be allowed to go forward to the "natural break" which would come when the Sinai agreements were completed, but that we doubted whether it had much potential to carry progress further thereafter. The process would then have to be broadened out, and one purpose of the European initiative was to prepare for that. Mr Lahnstein asked whether we envisaged that the process of broadening out should include the Russians. I said that we were thinking more in terms of a combined United States and European effort.

10. I am sending a copy of this minute to the Private Secretary to the Foreign and Commonwealth Secretary.

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