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PROFESSOR SIR ALAN WALTERS

cc Mr Gray

EUROPE

I think your idea is ingenious and well worth pursuing. It puts the other Europeans on the spot. We ought to discuss it with the Prime Minister next week. I will look for time in the diary for this.

We have to be ready to deal with a number of counter-arguments, some of which I would expect the Prime Minister to put forward:

- the other Europeans ought to fulfil the conditions set out in paragraph 2 of your note on their merits and without our having to pay a price.
- all our objections to joining the ERM will be just as valid after the others have fulfilled your conditions as they were before. If you take the view that membership is against our interests full stop, then your note does not help.
- there is a risk that, if we set conditions, the other Europeans will set counter-conditions e.g. they might argue that they will free capital movement when we agree to a Community-wide tax on savings.
- if we tie ourselves rigidly to your conditions, then we may actually deprive ourselves of flexibility. Suppose our assessment of the advantages and penalties of membership of the ERM were to change and we decided to go in but our conditions had not been met, it would look like a defeat for us.

I am making these points because I suspect they will come up not because I disagree with you. Indeed your suggestion sits very well with the point which I was trying to make at

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Chequers that we should try to focus the discussion on achieving genuine competition in the Community.

Charles Powell

10 May 1989

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