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From the Private Secretary

9 June 1987

VENICE ECONOMIC SUMMIT
PRIME MINISTER'S MEETING WITH PRESIDENT REAGAN

The Prime Minister had a 45 minute meeting with President Reagan this morning, before the first formal session of the Economic Summit. Secretary Schultz, Secretary Baker, Mr Howard Baker, Mr Frank Carlucci and Mr Bob Linhard were present for part of the time.

Iran/Iraq and the Gulf

The Prime Minister said that the text on Iran/Iraq and the Gulf which had been drafted overnight seemed generally acceptable. The United Kingdom was already making a substantial contribution to freedom of navigation in the Gulf through the Armilla Patrol. This had escorted 100 British ships already this year. She also was pleased that the major countries were now co-operating more effectively at the United Nations to work for a resolution of the Iran/Iraq conflict. President Reagan said that he shared the Prime Minister's satisfaction with the text. He would prefer to see the word "enforceable" added to describe action by the United Nations, and the Japanese were keen to have "just". The Prime Minister said that we could accept both.

Arms Control

The Prime Minister recalled the discussion which had taken place between the Heads of Government at dinner the previous evening. It had been evident that Chancellor Kohl was unhappy with the way in which the second zero option for missiles in the 500-1000 km range had emerged. She was sorry about that, because he was a strong and loyal ally. But she was not prepared to agree to follow-on negotiations on missiles under 500 kms in range, at least until certain conditions had been fulfilled. She could not leave British forces in Germany without the protection of shorter range nuclear weapons. They were also vital to the strategy of flexible response. There could be no question of a third zero option or de-nuclearisation of Europe. There should be no commitment to negotiations on shorter range missiles until chemical weapons had been eliminated and imbalances in

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conventional forces redressed. This would leave open the possibility of such negotiations, but only when the conditions had been fulfilled.

President Reagan said that he shared this view. He thought that NATO should only agree to negotiations on shorter range missiles once the Prime Minister's conditions had been met. On the other hand, Chancellor Kohl clearly had a major political problem, and needed to be able to point to the fact that these shorter range missiles could one day be the subject of negotiation. The Prime Minister wondered whether it was necessary to try to agree a form of words in Venice. Secretary Shultz said that the Americans had tried to draft a text which set out priorities in the arms control field, with negotiations on shorter range missiles at the end of the list. The purpose would be to let the Germans say that shorter range missiles were a negotiable subject, but in effect suspend any likely negotiations until agreement had been reached in other areas. In practice, the negotiations on shorter range missiles would not be operative for years. But we had to find a way to help the Germans through. Language would be needed for the NATO Foreign Ministers' meeting in Reykjavik. He agreed with the Prime Minister that there was no need for any statement to issue from the Economic Summit. President Reagan said that he had tried to convince Chancellor Kohl by pointing out that, if negotiations on chemical weapons and conventional forces were left until last, there would be no incentive for the Russians to negotiate on shorter range missiles. They would be the "biggest boy on the block" in this category of weapons.

Terrorism

The Prime Minister said that the draft text on terrorism which had emerged overnight was broadly satisfactory, although we would be ready to see it strengthened further by holding out the possibility of limited sanctions in the case of countries who harboured and failed to prosecute terrorists and hijackers. President Reagan said that great progress had been made in co-operation against terrorism in the past 12 months, thanks in large part to the Prime Minister's heroic efforts in getting a firm declaration from the Tokyo Economic Summit. He was perfectly happy to see the current text further strengthened, but understood that some other delegations might have problems.

World Economy

The Prime Minister said that she knew that the President was determined to deal with the United States Federal deficit and would prefer to do so by reducing expenditure. She understood that it might be helpful for him to be able to demonstrate that the United States was under pressure from its friends at the Summit on this issue. A strong reaffirmation of the United States' intention to reduce the deficit by appropriate means would be a useful signal, and would also make it easier to put pressure on Japan and Germany to take action to stimulate economic growth. President Reagan said

that progress was indeed being made in reducing the deficit. It would be cut this year by \$40 billion more than last year.

Secretary Baker said he was more optimistic about Japanese intentions. They were very concerned about the stability of their exchange rate. The recently announced package of measures was likely to be more effective than those announced in the past. He thought the Japanese really meant it this time when they said the measures would be implemented. The Prime Minister said that she was more sceptical. She had seen similar Japanese statements in the past which had not led to anything much in practice. It would be important to try to secure a very firm commitment from the Japanese to implementing action in the Economic Declaration from the Summit.

Secretary Schultz said that the United States trade deficit was declining, and the Administration were determined to make a big push to reduce the fiscal deficit. There were signs that this was working. Monetary policy would probably have to become tighter. This meant that the drive for expansion of world trade and for economic growth would not come from the United States. It was up to Germany and Japan to take the lead. President Reagan said that he agreed. There was scope for both countries to expand domestic demand. The Prime Minister said that her impression was that Chancellor Kohl would resist very strongly any pressure to bring forward tax reductions. Secretary Baker said that the Germans had promised that they would have another look later this Summer at the need for further measures to stimulate their economy if the expected growth did not materialise. They should be held to that commitment. The Prime Minister said that, once again, it would be helpful to try to secure some reference to this in the Economic Declaration.

Syria

President Reagan said that there was evidence that Syria was finally taking action to expel Abu Nidal. President Assad was rather like a social climber. He was keen to be brought back into the club of respectable nations. The President said that he had it in mind to write to Assad expressing appreciation for what had been done, but asking him to make further efforts to secure the release of hostages held by the Hizbollah in Lebanon.

We also wanted to see evidence that those in the Syrian Intelligence hierarchy who had been responsible for the Hindawi affair had been removed from their posts. She recalled that the President's earlier message to her had spoken of the need for Syria to take positive action to show that it was no longer involved in supporting state terrorism. She thought it would be a mistake for the United States to make any significant overture to Syria until these conditions had been demonstrably met. Mr Carlucci said that one had to bear in mind Syria's role in the peace process.

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The Prime Minister said that Syria's role was unlikely to be positive. She reiterated her hope that the President would take no action until it had been clearly shown that Syria had stopped its support for terrorism.

Arab/Israel

The Prime Minister said that Mr Peres was obviously in some political difficulty over the position he had taken on an international conference. It was important that Britain and the United States should support him, while avoiding the appearance of interference in Israel's internal politics. Mr Peres and King Hussein were the two people who might really be able to achieve a breakthrough in the peace process. Her own firm view was that an international conference should be just a framework for negotiations and have no substantive role. President Reagan said that Mr Peres was optimistic that he could find a way to dissolve the Coalition Government on this issue, and win support for his approach to an international conference. The President confirmed that his own view of the role of an international conference matched that of the Prime Minister.

Possible Visit to Washington

The Prime Minister said that she would like if possible to pay a brief working visit to Washington towards the end of July. President Reagan said that he would very much welcome this. It was left that I would be in touch with Mr Baker to discuss dates.

I should be grateful if this account could be given a very limited circulation. Could I also ask you to arrange for the Chancellor of the Exchequer to be shown the paragraphs on the world economy.

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