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PRIME MINISTER

ERM REALIGNMENT

News has come through this evening that a minor ERM realignment is likely to be agreed tomorrow (Saturday).

The Italians are moving from their 6 per cent bands to 2 1/4 per cent bands. The plan now is that they will do this by aligning the bottom of the new narrower bands with the bottom of the existing wider bands, i.e. a modest devaluation for the range. But their present market rate is within the new proposed range, so there should be no immediate impact on market rates.

I have enquired whether there is a possibility of a German revaluation. But I am told this is not being considered and of course there is nothing we can do to affect this.

The one consequence for the UK is that the notional central rate of sterling within the system is always adjusted into line with sterling's current market rate at the time of any realignment. In practice the effect this time is very small; it will involve our notional central rate being reduced by just 1/4 per cent. In other words the net movement in sterling since the time of the last realignment is very small.

The fact that both the Italians and sterling changes are so small means that there will be very little agri-monetary consequence for the CAP.

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PAUL GRAY

5 January 1990

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