

MR TURNBULL

ERM

I have been through your minute and the Chancellor's statement with the Prime Minister. She is pretty indignant, both with the Governor's reaction and what she regards as a 'panic' statement by the Chancellor. There is talk of being back to 'Lawson days'. But the storm has subsided and I think that I have dissuaded her from any immediate activity such as tearing a strip off the Chancellor and the Governor. But there are some points which she will very likely pursue with the Chancellor when they next meet:

- she resents the introduction of new statements such as "at the earliest sensible date" and "relative inflation" when she herself has stuck loyally to agreed formulations;
- she thinks the formulation "... not seeking delay, just awaiting the right circumstances .." is very weak;
- she has commented that the passage on oil is pure nonsense. In so far as it has any meaning, it relates to balance of payments not inflation;
- she is convinced that whatever he may now say, Poehl was referring to ERM and not to EMU.

The only point on which she is insistent that we must follow up is to write to David English about the flagrant misreporting of her press conference by the Daily Mail. She thinks they should publish an apology. Perhaps Bernard should pursue this.

CHARLES POWELL

22 September 1990

CDP



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SECRET

MR. POWELL

ERM

*This is a panic  
situation - and dissiw.  
We are back  
to Lawson days' m.*

*The note: not  
marvellous.  
CDD 248.*

As I explained on the 'phone, the markets have been extremely turbulent and a degree of stability has been achieved only through intervention of \$500 million involving action in Frankfurt and New York, as well as London. The markets have chosen to interpret the Prime Minister's remarks in Berne yesterday as meaning that the prospect of ERM entry has been put off for some considerable time.

The Governor 'phoned in a state of some anxiety, principally to let off steam about what he thought were ill-chosen words. He was pressing for a statement on the lines that the Chancellor was "optimistic" about UK entry and that the Prime Minister shared this view.

I believe the causation is the other way round. Market sentiment has changed and it will seize upon words which can be adduced in evidence. Nevertheless, the Chancellor thinks he need say something in Washington to reassure the markets. I attach a copy of the statement which he has released around 1630 hours London time.

I suggest that if the No. 10 press office are questioned about it, they should make clear:

- (i) that policy has not changed and that the Madrid conditions have not been reformulated; ~~as the P.M. said~~  
*The P.M. made that clear*
- (ii) that the Chancellor and the Prime Minister are at one;
- (iii) that Pohl's remarks related to EMU and as such were consistent with UK views, and not to ERM.

I suggest we refuse to be drawn on the reference to the different impact of oil prices which seems to be pure obfuscation.

AT

ANDREW TURNBULL

21 September 1990

c:\pps\erm (slh)



*That is a new statement.*

*Sounds like Paris*

Both the Prime Minister and I have made clear that it is our policy to enter the ERM at the earliest sensible date. We are not seeking delay just awaiting the right circumstances as the Madrid conditions made clear.

*very weak*

We have, therefore, to consider relative inflation. And what really matters is what happens from now on. The oil price rise is affecting both our inflation rate and that of our European partners. Indeed in some ways we are better placed than others to handle oil price rises.

*new words - previous words have been 'when inflation is nearer the European average'*

*- This is not correct. We have to buy in much oil at the market price and sell our lighter oil at the world price. This is wrong.*

The remarks attributed to Herr Poehl the other day concerned the dangers of a premature move towards EMU. These are dangers I have been emphasising for months. His remarks did not relate to our entering the ERM - as he subsequently made crystal clear.

*not inflation*

I am sure that entry is the right policy and we will not delay when the opportunity occurs. I am confident that our entry will be welcomed by our European partners. I expect no difficulty with this - our colleagues are keen for us to join.



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TO IMMEDIATE FCO

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IMF/IBRD WASHINGTON FOR PS/CHANCELLOR

EMU: FINANCIAL SECRETARY'S VISIT TO PARIS

## SUMMARY

1. THE FINANCIAL SECRETARY DISCUSSED EMU WITH A GROUP OF INFLUENTIAL FRENCH POLITICAL AND FINANCIAL FIGURES AND OPINION FORMERS OVER LUNCH ON 20 SEPTEMBER. THE DISCUSSION, WHICH COVERED BOTH THE POLITICAL AND TECHNICAL ISSUES INVOLVED, WAS LIVELY AND PROFOUND. IT CONFIRMS THAT THERE IS STILL A DEBATE TO BE HAD IN FRANCE IN WHICH OUR VIEWS NEED TO BE ENERGETICALLY PROMOTED, PARTICULARLY THROUGH VISITS BY UK MINISTERS, BEFORE THE IGC'S.

## DETAIL

2. MR MAUDE EXPLAINED OUR EVOLUTIONARY APPROACH AND THE MECHANISMS WHICH WE THOUGHT NECESSARY TO PROMOTE ECONOMIC CONVERGENCE. DISCUSSION FOCUSED ON THE OVERALL VALUE AND VIABILITY OF EMU ITSELF (AND IN PARTICULAR OF A SINGLE CURRENCY) AND ON WHETHER OUR PROPOSALS WERE TECHNICALLY SOUND. THERE WAS LITTLE INCLINATION TO ACCUSE THE UK OF SEEKING TO DELAY REACHING THE FINAL OBJECTIVE WITH ITS PROPOSALS.

3. AMONG THE MAIN POINTS RAISED BY THE FRENCH WERE:

A) LITTLE ENTHUSIASM FOR RAPID MOVEMENT TO EMU. MOST FELT THAT IT WAS TECHNICALLY IMPRACTICABLE TO MOVE QUICKLY, ALTHOUGH SOME ARGUED THAT IF A FIRM POLITICAL DECISION WAS TAKEN NOW, THE TECHNICAL PROBLEMS WOULD FALL AWAY:

B) ONE OR TWO SUPPORTED THE PRINCIPLE OF A COMMON (REPEAT COMMON) CURRENCY, ALTHOUGH OTHERS ARGUED THAT THIS WOULD BE A COMPLICATION ON THE ROUTE TO STAGE 3. ONE INTERLOCUTOR EVEN SUGGESTED THAT THE BRITISH 'HARD ECU' MIGHT NOT BE HARD ENOUGH. SINCE ALL EUROPEAN CURRENCIES WERE ALLEGEDLY WEAK, THERE WAS A DANGER THAT A



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PARALLEL (NO A BASKET) ECU WOULD SIMPLY BE LINKED TO SUCH WEAKNESS. A 'SUPER HARD ECU', WHICH WAS STRONGER THAN THE STRONGEST CURRENCY, MIGHT BE BETTER, ALTHOUGH THIS MIGHT REQUIRE SUPPORT IN THE FORM OF A HIGHER INTEREST RATE:

C) ~~GENERAL AGREEMENT THAT EMU WAS ONLY WORTHWHILE IF ITS PRIMARY OBJECTIVE WAS PRICE STABILITY;~~

D) SOME QUESTIONED WHETHER THE UK WAS RIGHT IN ARGUING THAT ECONOMIC CONVERGENCE HAD TO PRECEDE THE CREATION OF A SINGLE CURRENCY. HISTORICAL CASES CITED OF GROUPINGS WITH A SINGLE CURRENCY BUT WIDELY DIVERGENT ECONOMIES:

E) ~~SCEPTICISM THAT A EUROPEAN CENTRAL BANK (OR EMF) COULD OR SHOULD BE INSULATED ENTIRELY FROM POLITICAL PRESSURES.~~ MR MAUDE NOTED THE INCONSISTENCY IN THE FRENCH OFFICIAL POSITION HERE - IN CALLING FOR AN INDEPENDENT CENTRAL BANK BUT EXPECTING TO HAVE SOME CONTROL OVER IT: THERE WAS UNANIMOUS AGREEMENT WITH THIS POINT.

## COMMENT

4. THE DISCUSSION SHOWS HOW, IN SPITE OF THE FRENCH GOVERNMENT'S POLITICAL COMMITMENT TO PRESSING AHEAD AS QUICKLY AS POSSIBLE, THERE IS A BODY OF EXPERT AND INFLUENTIAL OPINION HERE THAT HARBOURS DOUBTS ABOUT BOTH THE ULTIMATE OBJECTIVE AND THE BEST WAY OF ACHIEVING IT. THERE IS A DEBATE TO BE HAD IN PARIS, PARTICULARLY AS THE FRENCH BEGIN TO RECOGNISE THAT MANY OF THEIR PARTNERS, PARTICULARLY THE GERMANS, MAY BE HAVING SECOND THOUGHTS ABOUT THE PACE OF REFORM. THERE ARE, AS THERE ALWAYS HAVE BEEN, ELEMENTS OF INFORMED FRENCH OPINION READY TO LOOK AT THE DETAILS OF OUR PRAGMATIC PROPOSALS AND TO TAKE THEM SERIOUSLY. MOREOVER THERE IS NOW LITTLE INCLINATION TO QUESTION OUR MOTIVES. I AM GRATEFUL TO THE FINANCIAL SECRETARY FOR HIS VISIT. IT WAS A WELL-TIMED LAUNCH OF A SERIES OF VISITS TO PARIS BY BRITISH MINISTERS TO DISCUSS EUROPEAN MATTERS DURING THE RUN-UP TO THE IGC'S IN DECEMBER.

FERGUSSON

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