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FRANCO-BRITISH SUMMIT, PARIS, 29-30 NOVEMBER 1984

NOTE OF MEETINGS BETWEEN THE CHANCELLOR OF THE EXCHEQUER AND THE FRENCH MINISTER OF FINANCE

Present:

British

The Chancellor of the Exchequer, Rt Hon Nigel Lawson MP

Mr J B Unwin, Deputy Secretary, HM Treasury

Mr D L C Peretz, PPS to the Chancellor

Mr R R Garside, Financial Counsellor, Embassy

French

M. Pierre Beregovoy, Minister of Economy, Finance & Budget

M. Daniel Lebegue, Directeur du Tresor

M. Jean-Claude Prevel, Secretary General, SGCI

M. Francois Laumonier, Chef du Cabinet

M. Daniel Dumont, Conseiller Technique, Minister's Cabinet

M. Gilles Guitton, Conseiller Technique, Minister's Cabinet

M. Jean-Francois Stoll, Conseiller Technique, Minister's Cabinet

M. Bertrand Schneiter, Conseiller Financier, French Embassy, London

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Budget Discipline

After M. Beregovoy had welcomed the Chancellor and his officials, it was agreed to start by discussing Community matters. M. Beregovoy recalled that he had attended the last two meetings of ECOFIN which had discussed budget discipline. Before the meeting with the delegation from the European Parliament after the latest

ECOFIN, he had proposed to the Irish Minister of Finance that he should be firm on substance and flexible on form, and he had accepted this advice. The meeting had been inconclusive.

The Chancellor observed that although the Italians had been difficult they were not very firm. ECOFIN had reached agreement on a text and its form, but it was then decided that the text should be adopted by the Foreign Affairs Council, with the outcome that we all knew. The moral was: Finance Ministers should handle such matters themselves. The failure to agree meant that the issue must now go to the European Council. This was sad: the European Council should not have to do this. It was of the first importance that the European Council should adopt the text in precisely the form in which ECOFIN had adopted it. The UK had made the increase in own resources dependent upon adoption of a satisfactory text on budget discipline. However we could agree to one procedural innovation to please Parliament: a letter from the Council to Parliament undertaking to consult them before the reference framework for the budget was set annually.

M. Beregovoy said that he had been able to agree the ECOFIN text but it was the position of the French Government that the last word should come from the General Affairs Council. The Chancellor would hear this view expressed at the political level the next day. The French Ministry of Finance was in favour of budget discipline but the Ministry of Agriculture had expressed reservation. In France when such a political conflict arose it was settled by the Council of Ministers or the Prime Minister; in the Community it was for the General Affairs Council to resolved. This was not necessarily satisfactory to M. Beregovoy but that was the situation.

The Chancellor said that the text could be adopted at the European Council by the Foreign Ministers deciding it quickly amongst themselves. M. Beregovoy said this was the French view also but could France and Britain persuade other countries to adopt the text? The Chancellor repeated that the Council could undertake that a letter should be sent by the Presidency to the Parliament undertaking to consult them before the reference framework was fixed, but should give no substantive role to the Parliament; it was for the Council to decide how it was going to conduct itself in the future. Unless the present text were adopted the UK could not agree to release the additional finance under the inter-governmental agreement for the 1984 supplementary budget. This was also the German position. Beregovoy added that it was the French position too. In his view, the Council's best argument was that the text governed the execution but not the elaboration of the budget by the Council. The Chancellor recalled that the Council's legal services had confirmed that the text accorded with the Treaty.

1985 Budget

The Chancellor observed that French and British views on the 1985 budget were close. It was essential that we shouyld resist the amendment proposed by the European Parliament, and stick to the 1 per cent VAT ceiling for own resources. At some stage it would be necessary to get the Germans off the political hook on which they had fastened themselves, so that they could agree to an increase in own resources before 1 January 1986. This was difficult to handle politically, but if anyone could persuade the Germans it was the French. Their role in this was crucial.

M. Beregovoy said that so far the Germans had always linked the increase in own resources to enlargement. Their position might evolve towards agreeing that own resources could be increased as soon as there was agreement in principle on enlargement. At the last Franco-German Summit they had allowed this to be understood. On the 1985 budget, execution would be difficult. Parliament would create trouble.

The Chancellor underlined the importance of sticking to the 1 per cent ceiling. We could not countenance the devices now being put forward to exceed it. M. Beregovoy foresaw a possible crisis with the European Parliament. The Chancellor said that, if the Parliament adopted a budget that exceeded the 1 per cent ceiling, the UK and France could consider taking legal action in the European Court of Justice jointly. The Council's legal grounds for court action against Parliament on the 1985 budget was clear; on the 1984 budget it was much less clear. In the latter case the issue was whether the Parliament had powers on the revenue side. M. Beregovoy commented that it was not healthy for the Parliament to vote expenditure but to have no responsibility for revenue. This was absurd.

IMPs

The Chancellor said that a head of steam had built up behind expenditure on IMPs. He was concerned about this. This Greeks were setting the pace and the Italians had a strong interest. The French had some interest in the matter but not much, as far as the Chancellor could see. If we were not careful there would be a massive commitment to spending on IMPs. The risk of such a development was evident from the evolution of expenditure on wine and Mediterranean agriculture over the last 5 years: expenditure on wine had increased 17-fold and on Mediterranean agriculture by 250 per cent. The Chancellor added that he had some ideas on how to curb this growth.

M. Beregovoy said that he agreed with the UK on 3 points concerning IMPs. (a) The Commission's proposal did not respect the position of the European Council because it did not take account of the consequences of enlargement, (b) it did not integrate IMPs into the existing structural funds and (c) the amount proposed was too high.

The French thought that 400 to 600 mecu spend over 4 years on IMPs would be appropirate. There was one point on which French and British positions differed somewhat, although they were not far apart: in the French view, once an appropriation had been made for IMPs expenditure in a country, that country should be able to decide on the application of the funds. Individual countries should enjoy some flexibility in the matter. This was a pragmatic approach and the pragmatic British should be able to agree to it. It was socialists who were supposed to be dirigiste but M. Beregovoy was putting forward a pragmatic proposal. He was a non-dirigiste socialist.

The Chancellor said that a ceiling on FEOGA guidance expenditure shouod be established for the next 5 years.

M. Prevel said that a new budget line for FEOGA guidance spending must be established. The Chancellor said that a new FEOGA guidance ceiling must be set to succeed the one which expired this year. We should bear in mind the amount to be spent on IMPs, within this ceiling. The new FEOGA guidance ceiling should be set at some 5 billion ecus over 5 years. Mr Unwin added that if no maximum figure was set there would be strong pressures to push up FEOGA guidance expenditure. Hence the importance of the ceiling. M. Beregovoy commented that the French Government had not taken a decision on the level of this ceiling. The Ministry of Finance favoured 5 billion ecus and the Ministry of Agriculture 5.5 billion. The Chancellor said that if the FEOGA guidance ceiling were too generous it would be very difficult to contain the IMPs figure within it. We were opposed to a separate envelope for the IMFs. Substantial money for IMPs would feature already in each of the 3 structural funds. M. Beregovoy asked when the ceiling for FEOGA guidance should be set, and M. Prevel replied that it would be set by the end of this year. Perhaps the word "ceiling" should not be used: to the Parliament it was like a red rag to a bull.

EIB Capital Increase

M. Beregovoy said that the President of the EIB had called on him the previous day, and M. Beregovoy had told him that he would find a doubling of EIB's capital acceptable.

The Chancellor recalled a meeting of the EIB Governors in June of 1984, just before he became Chairman of the EIB Governors. He had said then that the EIB had been growing too fast and needed a period of consolidation. A 15 per cent per annum growth rate would be too fast, which was what doubling the capital of the bank over five years would imply. The Chancellor thought that a 7 per cent per annum nominal increase would be more appropriate. Some increase would be justified by enlargement. Perhaps there should be discussion between British and French officials on this?

M. Beregovoy noted that there was disagreement between the two governments on this question. France wanted a large capital increase because it wanted the EIB to finance industrial development in the Community. It was with that in mind that he had spoken to the President of the Bank yesterday. This was a matter of consolidating the Community.

The Chancellor remarked that the matter would be discussed at the EIB Board on 11 December. Although he could not agree with the French on doubling the capital of the bank he did agree with the French emphasis on loans within the Community. In some quarters there was a wish to turn the EIB into a second version of the World Bank. M. Beregovoy confirmed his wish to see the EIB continue to lend principally within the Community, even in the UK! Mr Unwin added that the Board would discuss this question on 11 December and would make recommendations to the Governors next June. M. Beregovoy thought it would be good if French and British officials could reach agreement on these issues.

EMS

M. Beregovoy asked the Chancellor to clarify UK policy on the participation of sterling in the exchange rate mechanism. The Chancellor said that the policy with which M. Beregovoy would be familiar, remained unchanged. The question was kept under review, but there was no immediate prospect of sterling joining. The reports about this which had recently been featured in the press had not come from official sources.

M. Beregovoy remarked that Herr Schmidt, the former German Chancellor, and M. Giscard d'Estaing had both said recently they believed the US government was moving in favour of sterling's participation. The Chancellor said he did not know on what this belief was based. The UK was, however, in favour of some measures to strengthen the EMS, such as the proposal on mobilisation in the package put foward by the Committee.

M. Beregovoy observed that the Germans, who participated in the EMS, were very committed to the deutschmark, which the British showed a great interest in the ECU but did not want to join the ERM. He took due note of the UK's position.

M. Beregovoy added that he had raised the subject in particular because it could come up again with Spanish entry into the EEC. If Spain wanted the peseta to be in the ECU the French would agree only if the peseta were to enter the exchange rate mechanism at the same time. There might be a delay of several years between Spanish accession to the Community and this monetary development, but the French wouyld not agree to the peseta joining the sterling in being in the ECU and not in the ERM.

(Discussion was suspended here and resumed the next day).

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Special Fund for Africa

M. Beregovoy raised this subject and sought the Chancellor's views. The Chancellor said that there was general concern about the problems of Sub-Saharan Africa. No-one could see the pictures of starvation in Ethiopia without being moved. Britain like France had historical links with some countries on the continent. The French had made a proposal for a Special Fund for Africa, and the British Government would be happy to give it consideration but there were problems. In multilateral aid it was important to achieve gearing in order to push up total contributions. In this case many countries, for example United States, had shown no interest in the proposed Fund, so there was not likely to be much gearing. The UK had supported the IDA supplementary fund where there would have been such gearing, but unfortunately it had not been possible to gain support for a substantial sum. Mr Qureshi, Vice President of the World Bank, would be visiting the United Kingdom soon for discussions and Ministers would talk to him about the proposal. M. Beregovoy took note of the UK's position but asked the Chancellor to bear in mind that if the United Kingdom agreed to contribute to the Special Fund for African then the Netherlands and Italy would almost certainly do so and the Germans would probably reconsider their position. President Mitterrand had announced a commitment by France to contribute $150 million over three years to the Fund and the 1985 budget contained provision for the first tranche. The Chancellor asked if this $150 million was additional to previus plans for aid expenditure, and M. Lebegue confirmed that it was.

M. Beregovoy added that he had written the Chancellor a letter, which had not yet been despatched, to propose that M. Camdessus, Governor of the Bank of France and former Directeur du Tresor, accompanied by M. Lagayette, former Directeur du Cabinet of M. Delors, should visit him to discuss further the proposed Fund. If there was agreement in principle, a meeting could be held to discuss it multilaterally. M. Beregovoy did not expect the US to take part in such a meeting. The Chancellor said that nevertheless every effort should be made to get the United States to participate in such proposals, because of the extra gearing a US contribution would give. The subject could be discussed at the 17 January meeting in Washington.

World Economy

M. Beregovoy said that Herr Stoltenberg, the German Minister of Finance, foresaw GDP growth for Germany in 1985 of 2½-3%. France expected to achieve 2%. Both growth rates would depend heavily on exports. If there were a recession in the United States, then the consequences for Germany and France would be serious. When in Washington the European Minister should try to discover the intentions of the Americans concerning their Federal deficit in FY 85/86. Conversations which M. Beregovoy had had in Washington with bankers and others such as Dr Kissinger had convinced him of the renewed economic dynamism of the US, and he was surprised at the recent decline in US growth. He did not believe the US was going into recession.

The Chancellor said that UK GDP growth in 1984 would be about 2½% and in the following year 3½%. If there had been no coal strike in 1984 the rate of growth this year would have been 3½%. Next year's figure contained some 1% pushed forward from this year. The recovery in the UK was now broadly based with industrial investment especially strong and consumer spending still quite strong. The Chancellor shared M. Beregovoy's admiration for the dynamism of the US economy. He regarded the slowdown there as inevitable and was not too worried about it. Growth could not have continued at the previous high rate. He was more worried by the risk of serious dislocation arising from the failure to correct an unsustainable position of a budget deficit, which was causing US official debt to assume enormous and rapidly growing proportions, combined with its counterpart of a huge balance of payments deficit. If steps were not taken in time to correct this, and he was not too optimistic that they would be, then a correction of a dramatic and damaging kind would be forced upon the US economy. So he agreed with M. Beregovoy that they should try to find out American intentions when they visited Washington in January, and they should also try to persuade the American to cut their deficit. 1985 provided the only political window for doing this: the President had just received a great popular mandate and the next round of elections was still some way ahead. If the President did not act soon he would not act until forced to do so by a crisis.

M.Beregovoy commented that if the US did not take steps to correct the situation now, it would become more protectionist. The Chancellor agreed. Considering the enormous pressures upon it, the Administration had been very robust, but if the deficit were not corrected, the pressures would indeed grow. A reduced budget deficit would reduce the import of capital into the US and lead to lower interest rates. That would be good for world recovery.

M. Beregovoy said he was struck by the fact that at present US interest rates were coming down when the Dollar was going up. The Chancellor agreed that this was puzzling, but there was a market explanation. The momentum powering the Dollar was still there but would not last forever. So many people had expected the Dollar to fall for so long, had been wrong and had lost money thereby, that they were reluctant to take the risk of being wrong again and losing more money. But this was a time to remember the old adage "trees don't grow to the sky".

Mixed Credits

Turning to the question of what could the Europeanes do to prevent protectionism taking hold in the US, the Chancellor drew attention to one particular area where Europe could be exposed to US action: mixed credits. If the EC Governments could not reach agreement on mixed credits first amongst themselves and then with the United States in the OECD Consensus group; then there was a real risk that the US would leave the Consensus and adopt the technique of mixed credits to an extent that would far outrun anything possible for the UK or France. There were strong reasons for them to do so, as the Chancellor and M. Beregovoy had already agreed.

M. Beregovoy explained that the French had refused to endorse the Commission's text for a mandate for discussions in the OECD Consensus group. In the French view this was a subject which was appropriate for discussion in OECD rather than the Community. There were two points of principle for them in considering the subject of mixed credits:

(a) all forms of credit should be transparent; and

(b) they would refuse any new constraints in this area.

President Mitterrand would tell the Prime Minister that the French would not accept the Presidency text as it stood. There must either be a new text or discussion in OECD only. The Chancellor said this was not quite the right approach. The only way now, as in the past and in the future, was for the EC to reach a common position for negotiation with the US and

Japan. If the Community could not achieve a common position then the OECD meeting on 11/12 December was most unlikely to reach agreement. The UK fully agreed with France on the need for transparency. If the French had proposals for improving transparency, then he would welcome a discussion on them, but he did not understand what the French meant by accepting no constraints. If there were no Consensus, there would be a free-for-all in which the Americans would be the most powerful player.

M. Beregovoy said that what the French could not accept in the Commission and Presidency demarche was that French mixed credits should be the only ones under fire. France's handicap was total transparency. It was difficult to know what other countries were doing. When he said he was against a tightening of constraints, M. Beregovoy meant a tightening of constraints applied only to France. The French Government were people of goodwill but they found that their East European trade had been brought to a standstill, and their trade with the Developing Countries likewise. The Community text gave them a feeling of being got at and no agreement was possible as things now stood.

The Chancellor said there was no question of constraints being applied only to France. They would be applicable to the UK as well as France. The UK's transparency was as complete as that of France. Both countries should insist on knowing what everyone else was doing. The Commission was simply proposing an attempt to reach a common Community position and M. Beregovoy had suggested a few moments ago that this was undesirable. The Chancellor hoped that the French would make a serious attempt to reach agreement in Brussels on 10 December. If private discussions between French and British officials to agree modifications to the Community text could make that text acceptable to the French then he would favour such discussions being held. M. Beregovoy agreed that discussions could be held. Sovereignty loomed large in this matter, specifically sovereignty over aid policy. The Chancellor said there was no question of sovereignty being compromised. It was important to exercise restraint in subsidising exports, otherwise those companies whose exports were not supported by subsidies would get into difficulties.

Guangdong Nuclear Project

M. Stoll said that the commercial negotiations over the Guangdong project had ended and financial negotiations were about to begin. They would have to be concluded very quickly. The two Ministries of Finance should work in closest co-ordination. The Chancellor said he remembered this project from his days as Secretary of State for Energy. He was happy to see the negotiations had made such progress. He knew the Chinese were keen. The future sales of electricity at Hong Kong were an important element and the Chinese did not wish to upset the agreement reached over Hong Kong. They wished to demonstrate reliability. But they would try to play the French and British off against each other. M. Beregovoy agreed. M. Stoll said that ECGD and COFACE were in frequent contact on the project. Mr Unwin said it was indeed important that the French and British should keep very closely in touch on these negotiations. The terms were already very generous. If there were any thought of changing them, the two Ministries of Finance should consult first. The Chancellor said that he was sure there should be no change, and the Chinese should not be allowed to drive any wedges between the French and the British. M. Beregovoy asked if there were any difficult apparent at this stage and was told by M. Stoll that none had appeared. M. Beregovoy added that the French had thought that the matter was largely settled but the President's wife had returned from a semi-private visit to China with the impression that nothing was settled. Mr Unwin commented that the terms already offered to the Chinese were an exception to the OECD Consensus and we should, if necessary, remind the Chinese of this.

Washington Meetings

M. Beregovoy said there were meetings in prospect in Washington on 17 January and then in the spring when the IMF Interim Committee and the World Bank Development Committee would meet. It had been agreed to discuss international debt questions. The largest debtors were in Latin America but the needs of Africa were acute. The productive capacity of Latin American countries was relatively developed but that of the African countries was little developed. They must not be forgotten. Perhaps he and the Chancellor should meet before the Interim and Development Committees, to discuss.

The Chancellor said that M. Beregovoy's preoccupations were similar to his. The US had originally contemplated a meeting to deal with the problems of Latin American debt only. He had not suggested that. The UK had to think of the Commonwealth, and France had to think of Francophone countries. Both had acute needs even though they did not pose an acute threat to the international banking system. There was another aspect of the subject which should be remembered: it was important to open up these countries to private development capital. Greater flows of such capital were needed. The implications of such a policy were that the West must allow the outflow, and the developing countries must allow the inflow.

The Chancellor went on to say that he was aware of the French proposal for World Bank country loans. He had not studied it closely but he thought that it was an idea worth pursuing.

M. Beregovoy agreed with the Chancellor's remarks about flows in general but said that private aid alone was not enough. Should they try to reach a common Community position before the Washington meetings, bringing together official development assistance, private flows and country-to-country agreements? The Chancellor thought that it would be an appropriate topic for discussion at an ECOFIN lunch. Thereafter they could talke it over with the US Treasury Secretary. It was important not to arouse great expectations before the spring meetings in Washington. Although the Managing Director of the Fund had exaggerated the risks of this somewhat, the need to avoid a sense of anti-climax was important.

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10 December 1984

Charles Powell Esq
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Dear Charles

ANGLO-FRENCH SUMMIT

For the record, I enclose a copy of the extended record of the discussions between the Chancellor and M. Beregovoy in Paris on 29-30 November, prepared by Roger Garside from the Paris Embassy, who attended the discussions.

I am sending copies to Len Appleyard (FCO), Callum McCarthy (DTI), Richard Hatfield (Cabinet Office) and Roger Garside in the Paris Embassy.

Yours ever

David

D L C PERETZ
Principal Private Secretary