

Meeting Record

cc Master

The PM
S(a-b)

10 DOWNING STREET

LONDON SW1A 2AA

From the Private Secretary

2 November 1989

GERMANY

The Prime Minister had a talk yesterday afternoon with Sir Christopher Mallaby about Germany.

Sir Christopher judged the prospects for the CDU/FDF coalition to be quite good. They stood at some 50 per cent in the opinion polls. The economy was performing outstandingly well. Chancellor Kohl was trying to strike a cautious and balanced attitude towards developments in East Germany and elsewhere in Eastern Europe, and he had deliberately avoided talk of German reunification. He had acted responsibly in his handling of President Gorbachev's visit in the summer. There was no doubt that the alternatives to Chancellor Kohl - a coalition involving the SPD and the Greens - would be much worse from the point of view of Britain's interests.

The Prime Minister accepted without question that it was very much in our interests that Chancellor Kohl should continue in office and that the Federal Republic should remain a steady and reliable partner. But there were nonetheless aspects which caused her concern. At the risk of over-simplifying, she saw a tendency for official thinking to spend too much time speculating on Germany's geopolitical position and how it might develop. Of course this was important. But it was clear that - whatever their formal position - Britain, France and the Soviet Union were fundamentally opposed to German reunification. It was Germany's role in Western Europe rather than Central Europe which should be the more pressing concern. The massive and persistent trade surplus - the sum of bilateral surpluses with every other EC member state - based on an under-valued DM and subsidies to German industry was leading to increasing German economic dominance of Western Europe. The special arrangements for imports from East Germany strengthened this tendency.

The Prime Minister continued that this dominance was reflected in Germany's determination to get its own way on Community issues, for instance the desire to reduce the competitiveness of other European countries evident in support

for the Social Charter. Other European Governments seemed disinclined to challenge Germany on its permanent trade surplus: there was a contrast here with the robust way in which the United States was tackling Japan about its proportionately smaller trade surplus. She would like to see the focus of our diplomacy turn more single-mindedly towards tackling these problems by:

enlisting German support against a restrictive and anti-competitive Social Charter;

bringing home to the German government and German industry the dangers inherent in the Delors Stages 2 and 3 for the sound money policies of the Bundesbank;

pressing for a revaluation of the German mark (although this would need to be handled very discreetly to avoid repercussions in the exchange markets);

and urge the importance of reducing State Aids and other subsidies.

She would be ready to send a message to Chancellor Kohl (or, as she subsequently told the Foreign Secretary, to see him ahead of the Strasbourg European Council) to make some of these points. They were crucial to our own economic prospects and to securing the sort of Europe we want. None of this was to belittle the importance of developments in Central Europe and Germany's role in them. They would need the most careful handling. But the problems with Germany in Western Europe - including Germany's attitude to SNF and other defence issues - were of even greater concern and the weight of our effort should go into dealing with them.

I should be grateful if this letter could be given a very limited circulation only.

I am copying this letter to John Gieve (H.M. Treasury).

C. D. POWELL

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Foreign and Commonwealth Office.