



Prime Minister
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Treasury Chambers, Parliament Street, SW1P 3AG
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Dear Charles

ANGLO-FRENCH SUMMIT 27 FEBRUARY: ECONOMIC AND MONETARY CO-OPERATION

... I attach a brief on economic and monetary co-operation for the Prime Minister's use at the Anglo-French Summit on 27 February. I am also copying it to Stephen Wall (Foreign and Commonwealth Office) and Roger Lavelle (Cabinet Office).

Yours sincerely
J M G Taylor

J M G TAYLOR
Private Secretary

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ANGLO-FRENCH SUMMIT: 27 FEBRUARY

ECONOMIC AND MONETARY COOPERATION

Our Objectives

- To make clear to the French why the UK favours a pragmatic approach to economic and monetary cooperation and the handling of the Delors Committee report.
- To emphasise the political difficulties of Treaty amendment.
- To sound out the personal position of President Mitterrand, and to impress on him the political difficulties inherent in proposals emerging from the Delors Committee.

French Objectives

- To press the case for firm commitments to progress towards EMU, and need for early institutional change.
- To sound out the UK position, and, perhaps, to urge early UK membership of the ERM.

Our Arguments

- Important that Delors Committee's Report makes clear that full EMU would require massive shifts of economic and political sovereignty from member states.
- Such a shift would require fundamental amendment to the Treaty, going beyond the competence of members of the Committee who are monetary experts. Heads of State and Government should draw the constitutional conclusions from the Report - Central Bank Governors should not make such recommendations.

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- Report should focus on practical steps within existing Treaty to be taken in immediate future, rather than long-term objective of EMU which is premature and not necessary for the Single Market.
- UK could support practical early measures which do not require Treaty amendment including:-

i. monetary cooperation

- reserve diversification and use of Community currencies in intervention. (The French are favourably disposed.)
- private ecu: removal of national impediments to use of private ecu; government borrowing denominated and payable in ecu (our ecu Treasury Bill programme points the way); and increased use of ecu in reserve holdings and intervention. (French have announced plans to launch medium to long-term bond denominated in ecu.)
- we support continued and strengthened monitoring and coordination of monetary policy.

ii. abolition of exchange controls. An important step to which all member states are now committed. Implementation of this commitment is necessary for the Single Market and must be a priority. (France still has some controls to remove. The French, in particular, are concerned that dismantling exchange controls will lead to widespread tax evasion and against that background, the Commission has issued draft proposals for a Community withholding tax.

The French attach considerable importance to this issue, but have said that they will not go back on their commitment to remove exchange controls.);

iii. fiscal policy. A further precondition for the successful economic development of the Community is the gradual elimination of budget deficits, and meanwhile their financing in a non-monetary way.

- Procedure When Committee has reported, its work will be complete. It would be a mistake for Madrid Council to refer work back to it. Should remit further work to ECOFIN, with Central Bank Governors present as appropriate.

Our Response To Their Arguments

- [If French argue for Treaty change] No. Implies readiness to accept massive shifts of economic and political sovereignty from member states. Major and wasteful diversion of effort from important task of completing Single Market. Only recently changed Treaty to deal with the jobs that need doing now. Absurd to propose further Treaty amendment so soon. UK Parliament will not give a blank cheque - ie enabling powers to be exercised at some undetermined future date.
- [If French raise spectre of "two tier Europe"] Deplore such divisive talk. Could only weaken Europe.
- [If European Central Bank raised] No secret that we believe study of this issue is premature to say the least.

[If suggested sterling should withdraw from the ecu as a non-participant in the ERM] In no one's interest to propose a change which would have far-reaching market implications.

French Views

The French remain the keenest advocates of rapid progress towards EMU. In private, they stress their pragmatism. But they have made clear that they have no reservations about possible institutional developments or Treaty change.

Mitterrand - not closely involved in recent discussions, but determined that the French Presidency - which will follow the Madrid Council - should mark a step forward in European construction, and sees monetary co-operation as a key area. He wants to see the Community pull together rather than apart, and realises the importance of working closely with the UK in achieving this. But - if only for tactical reasons - he is not above floating, or allowing others to float, suggestions of a two-tier Europe.

Prime Minister Rocard - out of an apparent concern to gain German support, has declared himself willing to contemplate an autonomous European Central Bank.

Finance Minister Berezovoy - the Trésor has been focusing on pragmatic measures (eg strengthening the EMS, including UK participation in the ERM, and greater use of Community currencies in intervention) as a way of promoting symmetry in obligations under the ERM.

De Larosiere, Governor of the Banque de France - appears to favour monetary union as locomotive for securing economic union. Advocated institutional step of creating European Reserve Fund to pool reserves, intervene on behalf of member states and play a role in monetary policy coordination - the Fund would be a first stage leading eventually towards a full European Central Bank.

Background

The Governor's tactics in the Delors Committee were discussed at your meeting of 15 February. You will clearly not wish to foreshadow exactly how the Governor will play this in the Delors Committee.

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