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Office of the United Kingdom Permanent Representative
to the European Communities

Rond-Point Robert Schuman 6
1040 Brussels
Telephone 736 99 20

011/4

J R de Fonblanque Esq

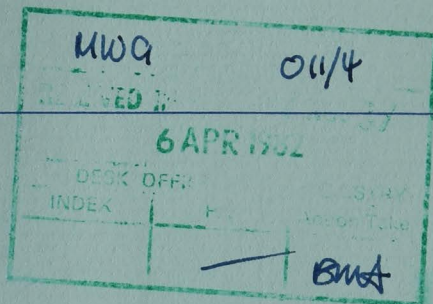
Your reference

ECD(I)

Our reference

FCO

Date 31 March 1982



R+PA. 9/4

Dear John

EUROPEAN COUNCIL 29/30 MARCH

1. I enclose, as required, the first draft of a composite record of discussions at the European Council. It draws on notes made by the Secretary of State and Sir M Palliser; on the debriefings given after dinner on 29 March by the Secretary of State and the Prime Minister; and on information received mainly from the Presidency in the Antici Group of the course of discussions in the Council itself.

2. I would be grateful if you could arrange for others who were present to comment as appropriate on the draft before you circulate it to EC Posts.

Tomlinson

John

J A Shepherd

cc PS
PS/PUS
Lord Bridge
Mr Hannay
Mr Hancock, Caboff.
Mr Clarke

cc (with enc): PS/PUS

Could any comments be sent to Mr Clarke (tel 3594) by direct player Tuesday 6 April please?

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J R de Fonblanque
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St. SpangleyItem (copy from E
read to M.)EUROPEAN COUNCIL: INFORMAL RECORD

1. No comments have been received from copy addressees on UKREP's attached draft.

2. I attach a short draft covering letter for circulation of the record. The distribution follows that for previous E. Council records.

Patricia

7/4

MWC		B11/4
19 APR 1962		
INDEX	FILE	Non Take



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to the European Communities

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1040 Brussels

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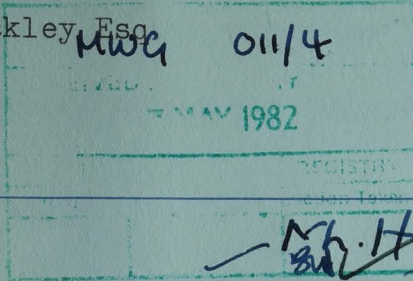
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FCO

Your reference

Our reference

Date 29 April 1982



Jean Nick,

Mr. Hall *DA* *24/5*
I need a diff reply re. saying
we do not but can never be sure
how thoroughly the record has been checked
MT 5/5

EUROPEAN COUNCIL RECORDS

68 — 1. As far as I could tell without detailed cross-checking the record of the March European Council enclosed with your letter of 8 April to John Fretwell was unchanged from that which I sent to you immediately after the European Council.

62A — 2. It was my understanding, when the new reporting system was set up this time last year, that what UKRep would produce would be very much a draft to which others in the delegation would add their contributions. In the nature of things I cannot guarantee to be present at all debriefings or to have picked up all the notes that people make. In this case much of the record was based on Sir Michael Palliser's somewhat illegible handwriting (which is why I copied my letter of 31 March to John de Fonblanque to the PUS's Private Secretary). I accept that with the Falklands crisis circumstances on this occasion were exceptional, to put it mildly. But I have the impression that there was little input from members of the delegation in June last year either. I hope therefore that in the interests of reliability and accuracy it will be possible to obtain views and comments from senior members of the delegation before circulating these records. An extra day or two would not make much difference.

Yours ever

John

J A Shepherd



Foreign and Commonwealth Office

London SW1A 2AH

MAY
7 April, 1982J A Shepherd Esq
UKREP
Brussels

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7/5

Dear John,

EUROPEAN COUNCIL RECORDS

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Thank you for your letter of 29 April about the draft record you produced of the March European Council.

2. I can understand your exasperation on this. In addition to the PUS's Private Secretary, we circulated the draft for comments to the Private Office, Lord Bridges, Mr Hannay and Mr Hancock (Cabinet Office). The problem is, as you yourself acknowledge in your letter, the perennial one of over-riding demands on senior officers' time.

3. We do, and will continue to do, what we can to encourage other members of the delegation to contribute to the record of these meetings. But I fear that we are unlikely ever to get much additional input. This is why I make it clear when circulating the record that it is 'informal', 'not exhaustive' and for background only.

Yours truly,
NideJ N T Spreckley
European Community Dept (Internal)



Foreign and Commonwealth Office

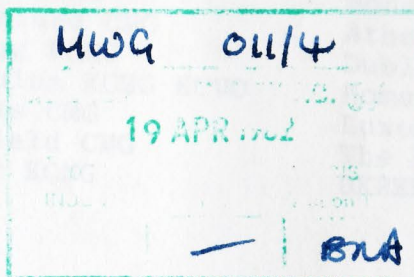
London SW1A 2AH

8 April 1982

HE Sir John Fretwell KCMG
British Embassy
PARIS

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14/5

011/4



Dear John,

EUROPEAN COUNCIL

I enclose an informal record of the proceedings of the recent European Council.

The record, which does not purport to be exhaustive, is strictly for your own background information, and that of your senior staff. It should not be quoted directly.

Yours truly,

Nick

J N T Spreckley
European Community Dept (Internal)



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EUROPEAN COUNCIL, BRUSSELS, 29/30 MARCH 1982

Copied to:

HE Sir Peter Wakefield KBE CMG	Brussels
HE Dame Anne Warburton DCVO CMG	Denmark
HE Sir Jock Taylor KCMG	Bonn
HE Sir Iain Sutherland CMG	Athens
HE Sir Leonard Figg KCMG	Dublin
HE Sir Ronald Arculus KCMG KCVO	Rome
HE Mr Jeremy Thomas CMG	Luxembourg
HE Mr Peter Mansfield CMG	The Hague
Sir Michael Butler KCMG	UKREP, Brussels

PS

PS/Mr Hurd

PS/Lord Belstead

PS/PUS

Lord Bridges

Mr Bullard

Mr Goodison

Mr Gladstone WED

Mr Wilson SED

Mr Evers RID

Mr Bayne ERD

Mr Crowe ECD(E)

Mr Laver Research

Mr Hancock	Cabinet Office
Sir Kenneth Couzens	HM Treasury
Sir Brian Hayes	MAFF
Sir Donald Maitland	DOEnergy
Sir Peter Carey	DOI
Mr Franklin	DOTrade
Mr Derx	DOEmployment

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EUROPEAN COUNCIL, BRUSSELS, 29/30 MARCH 1982

Monday 29 March

INTRODUCTION

1. The Italian Prime Minister and Foreign Minister having lost their police escort on the way from the Italian Embassy, the meeting did not begin until 1530.

2. After opening courtesies (in Dutch), Martens (Chairman), switching to French, suggested the following programme:

(a) economic and social policy, internal and external aspects;

(b) report from Presidency on 30 May Mandate;

(c) the Greek memorandum

finishing at 6.30 pm. At dinner topics of interest could be discussed, including some aspects of transatlantic relations. On Tuesday discussion would start with a Presidency text on the economic and social situation, followed by drafts on Political Cooperation subjects. The session should finish before lunch.

ECONOMIC AND SOCIAL SITUATION

3. Introducing the Commission's paper Thorn said that the Community was in a particularly difficult phase. Different member states were experiencing different economic developments, had different balance of payments problems; the level of unemployment made the unions tense; investment was too low. Common action was needed on all those problems. The Community discussion was not sufficiently exploited. Anti-inflationary policies were essential. National and Community measures were needed to cope with young unemployed, particularly those aged 16 and 17.

4. Ortoli thought unemployment might stabilise by the end of 1982. Inflation was improving, but not quickly enough.

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American trends were uncertain. The drop in oil prices was good, but it might not carry through to the final price if the dollar strengthened. A stable dollar, reduced interest rates and a decline in oil prices would be helpful. More investment should be devoted to developing countries.

5. The Community should add to national efforts. Policy towards Japan was improving with action in the GATT. The dialogue with the USA should be more organised: the exchange rate of the dollar had varied by 45% over the last year. On the internal scene public demand should have a ceiling. Private consumption could not increase if European competitiveness was to be preserved. More thought should be given to investment policy, especially in energy. We should take advantage of the scale of the market of 250 million and coordinate development efforts, eg in the telecommunications sector. The EMS could contribute, but there were divergences on reinforcement and the ECU. A real initiative was necessary: not stage 2, but with all pulling together. The EMS had not been unsuccessful in imposing discipline on Belgium and avoiding a whole series of competitive devaluations. The ECU acceptance limit should be raised from 50% to 75%. He agreed on the need for an active employment policy, especially for the young.

6. Jørgensen (Denmark) said that unemployment must be the central issue in the European Council conclusions. What Europe did economically was inevitably linked to what the other big economies like the USA and Japan did. The Community must have an economic policy to present at Versailles to the Americans and Japanese. European monetary cooperation must continue. The EMS had been a force for stability which was essential for dealing with monetary crises. Above all the Community needed an expansionary employment policy which should not of course induce inflation. Unemployment must be reduced. Inflation was no longer the problem it used to be: its place had been taken by unemployment. The following were needed to create jobs:

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- (a) public sector investment;
- (b) specific employment measures including jobs for the young: all under-25s should have the guarantee of training or a job;
- (c) energy investment as the Commission proposed; eg on increasing exploration in Danish territory, and on the search for alternative sources, but not nuclear energy;
- (d) help for small advanced industries to compete with the USA and Japan.

All the specialised Councils should be asked to take up these problems and to consult the unions at the European level.

7. Schmidt (FRG) claimed not to have much to say. He was sceptical about the value of common action. He had seen phrases about it in the Commission's paper and heard them in Ortolli's remarks. The economic situation was bad on all fronts. There was no point in pushing too hard for "common experiences" since that would merely lead into the appalling vicious circle in which the Americans found themselves. The problem could not be corrected by increasing budget deficits.

8. He had been struck that none of the five speeches at the 25th Anniversary commemoration had mentioned the vast changes in the world between 1957 and 1982. The super-powers were now much stronger and Europe was even more dependent economically on the huge economy of the USA. With interest rates at their present level no change was possible. Budget deficits were too high; inflation rates and wages and incomes likewise. They were all higher than was justified by GNP growth. No-one seemed to have the courage to say that if more investment was wanted there had to be less consumption. Different measures were needed for different countries. Some would increase taxes, others might persuade the unions to accept lower wage increases, as the Federal Government had done. Income/wage levels had to come down to promote fresh investment and to reduce /balance

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balance of payments deficits. Only the UK and Luxembourg of the member states had avoided persistent balance of payments deficits over the last few years caused by income levels being too high sucking in too many imports. The Council could not decree how each member state should deal with its problem. Nor could extra people be taken on merely to create artificial employment. He wondered how long the proposed Danish measures were supposed to last.

9. In Schmidt's view no economic event other than the crisis of the twenties and thirties and Hitler's war had been of such devastating effect as the present crisis. So he agreed with the Commission on the need to cut incomes in order to increase investment, but he repeated that it was not possible to legislate for everyone. For example indexation was very damaging and he was glad that the Federal Republic had avoided it.

10. Papandreou (speaking in English 'so as not to be misunderstood') said that the recession was of great depth and length. Keynesian macro-economic solutions would not provide the solution, nor would monetarism. The crisis was caused by the following factors: the European post-war reconstruction had been the main force for investment but Europe had now reached US levels of industrial strength. There were no new markets unless the USSR and China opened up. The third world did not offer adequate markets. Modern technology required only modest investment (in computers, telematics etc) not massive investment like the innovations of the past (steel, railways). Employment prospects were therefore poor and he shared Schmidt's pessimism. Private and public sectors were competing for the same investment resources, so choices had to be made. Greece had made them. Strict measures had been taken to reduce the huge public deficit and to allocate investment capital strictly. Luckily Greece did not face a serious unemployment problem. Some kinds of supra-national investment were necessary for Community action such as energy, especially as Europe had little oil; transport and regionally disadvantaged areas in

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the Community. He agreed with Schmidt that incomes could not rise without GNP growth. He also agreed with Jørgensen on the need to redistribute income in favour of the lowest paid workers and to redistribute unemployment. (Comment: A point he did not explain.)

11. Beginning a long and repetitive speech, Mitterrand commented that Schmidt and Jørgensen were proposing radically different ways of coping with the present problems. The present crisis was not just bad luck as Schmidt seemed to have suggested, nor did he agree with Schmidt's apparent view that a third world war was necessary to create a situation in which expansion would be possible again: surely Europe could do better than that. Europe could not compete with regimes which worked by sweated labour and authoritarianism. In his personal view too much capital was transferred by multinational companies from Europe to such countries. So the Community would have to think about protecting its markets. This did not just mean anti-dumping measures but control of capital movements, credit etc.

12. One cause of the crisis was technological change. Machines were putting hundreds out of work. The period of adaptation would be long and governments had to work out how to manage it without crushing millions of people in the process. There was social inequality on a massive scale, hence the need for redistribution of income. This was very visible in France because previous regimes had failed to remedy it, as the technocrats who thought mainly in terms of efficiency. He thought that redistribution of income would also help to reduce inflation. Everyone urged the government to introduce every kind of measure to help the young, ie to keep millions of people unproductive at public expense. This could be done up to a point, but there must be a better way. He certainly did not agree with Schmidt's "war" solution.

13. Investment under the previous regime had not been satisfactory. The public sector would now need to be enlarged and investment in research in particular would be increased. (He spoke at length about research). Reverting

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to unemployment he described the measures being taken for 16-18 year olds for whom training would be guaranteed. He then turned to the need for protection for the agricultural industry against imports from outside the Community. The Community should negotiate on this with its friends and should re-negotiate the GATT. Negotiations were also needed with the trade unions. The social security system needed reforming. In France the more employees a firm had the greater the burden of contributions on it while for instance the energy sector which employed few people paid much less. The social budget was bigger than the national budget.

14. The third world also contributed to the current crisis. There seemed to be more and more people but less and less demand for what the industrialised countries produced. The Americans were not doing anything for the third world. Europe could not replace them but must make a greater effort and do something on its own scale. The Versailles Summit should be used to press the Americans to do more: what they did in the Caribbean was not enough. Reagan had grumbled to him about high interest rates and complained that private investors had no confidence in his economic policy because of the size of the deficit.

15. Summarising, Mitterrand said that the Community could have a role in the following areas: Japan, USA, lending and borrowing, research and technology, agriculture and the fight against substitute imports, social matters.

16. Haughey (Ireland) concentrated on unemployment and the need for new measures. He described the measures the new Irish government were proposing for the reduction of the wage bill, the balance of payments deficit and inflation. The Community could help by improving competitiveness through more loans and transfers to the less prosperous regions, the Social Fund and research policy. Agriculture was vital for Ireland's future and had to share in any increased investment.

/17. Spadolini

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17. Spadolini (Italy) claimed that Europe could not have survived the present crisis without the Community. But better coordination of policies was needed. There should be a Community investment policy, coordinated reduction of public deficits and an industrial strategy to improve competitiveness. The NIC should be increased to 3 bn ecu, made permanent and given interest rate subsidy facilities. The EMS should be reinforced and progress made to the second stage. Europe was too dependent on the US economy. In the fight against unemployment it was necessary however to remember the different situations faced by the member states: some could be more active than others. These problems should be examined at the Versailles Summit.

18. Werner (Luxembourg) warned against protectionism, about which the European Council should make a declaration. He thought that Chapter I of the Mandate conclusions should be put into effect as soon as possible, including the reinforcement of Community loan mechanisms and the EMS. There should also be common rules to reduce budget deficits. He echoed others on youth unemployment, help for small industries, but thought that reduction of working hours, while desirable, would be very difficult unless everyone did it together.

19. Van Agt (Netherlands) agreed with Schmidt on interest rates and income levels. He thought the Commission report was good and agreed with its priorities. The possibility of holding a further "jumbo" Council should be considered. The last one had been quite successful. It could be the ideal forum to discuss how to share out the available employment. The North-South dialogue should also be pursued.

20. The Prime Minister said that the falling price of oil, with what flowed from it, must on the whole be a good thing, providing an opportunity for expansion. It brought problems too, but the advantages outweighed them. One had to decide how to make best use of the fall in price. Referring to Haughey's call for an action programme on unemployment she pointed out that the Commission had proposed such a programme.

/She

She agreed with the views of Schmidt and Spadolini about it: the problem must be solved without jeopardising the fight against inflation. She also agreed with Schmidt that resources for more investment would only be available if consumption were cut. This could only be done by fiscal policy; on wages the government could only persuade. Not all investment however was automatically desirable, eg steel, shipyards, cars. It would have been better to have spent the money on new small businesses which employed more people. Furthermore, large firms often paid wages at levels too high (including the nationalised industries) which set trends damaging for small firms.

21. It was necessary to have programmes and training schemes to alleviate unemployment amongst the young. The UK had put forward such a programme. The Social Fund was helpful. Some employment-creation was of course desirable, but not if it led to over-manning, which the British Government was trying to eradicate. Employment opportunities of the future in Europe would be in the service industries which now took more than 50% of the labour force. It was therefore important to get rid of the remaining barriers to the Common Market in services.

22. Externally the Japanese must be tackled for the way they ran their macro-economic policy with the yen too low and Europe's export markets consequently denied. US interest rates were a difficult subject. In conclusion it would be a great dis-service if this meeting of the European Council allowed the idea to circulate that there was some magic formula which could solve everything. The only way forward was by hard decisions and each government had to take them for itself.

23. Responding briefly to the tourde table, Thorn endorsed the importance of the North/South Dialogue. Martens then tried to sum up on the following lines:

a) Underlining the need for a coordinated policy on investment and unemployment: he asked whether the European Council could accept an objective expressed in terms of a rate 1% higher than forecast, with consumption correspondingly 1% lower. (The Prime Minister warned against putting in any figure, since no-one knew whether it would be possible to achieve it.)

- b) The objective for investment must be back by a Community industrial strategy, covering new technology etc.
- c) Unemployment would only be reduced by investment and mastering costs, but its seriousness required immediate action as well, such as vocational training for the young.
- d) The EMS had worked well, and a further impulse should be given through it to economic convergence. (Schmidt said tartly that the EMS had not been invented to allow everyone to devalue competitively: that was the easy way out.)
- e) Investment in energy.
- f) Action on US interest rates and the need to insist on movement from Japan.
- g) Need for an active policy on the North/South Dialogue.
- h) The possibility of a jumbo Council (van Agt stressed the need for thorough preparation, and Ortoli reminded the Council of the need to involve other Councils too.)

30 MAY MANDATE

24. Tindemans made a brief report. After a silence the Prime Minister said that it was disappointing that the Foreign Ministers had so far been unable to complete the task which had been set them last November at Lancaster House despite the series of meetings they had devoted to it. They had been unable to reach agreement on three key problems: a financial guideline on the CAP, milk and the budget problem. It was not in the Community's interest for this deadlock to continue, and it was for Heads of State and Government to ensure that the necessary instructions were given to enable substantive solutions to be found without further delay.

25. The Presidents of the Commission and the Council had now made new suggestions for a method to solve the budget problem. It was good that the negotiations were now seriously under way again and that the Foreign Ministers had set themselves a tight timetable for agreement both on the method and on the substantive solution of the problem. It was up to all Heads of Government to make sure that their Foreign Ministers were in a position to find an agreement both on the method and on the figures at their meeting on 3 April so as to enable early decisions to be taken.

on the three chapters of the Mandate in parallel as agreed last year.

26. As Foreign Ministers were to meet soon, the Prime Minister did not want to press then for a discussion about the details of a solution. She wanted, however, to make a few general points which she hoped Foreign Ministers would bear in mind.

27. First, we should try to give the Community a period of stability by taking this problem out of the arena of political discussion for a substantial period. A budget solution which involved either negotiations about figures every year, or another major negotiation like this one in two or three years time, would not give the Community the breathing space that it needed if it were to respond effectively to the challenges presented by its internal economic problems and an increasingly dangerous world environment.

28. Second, the method of correction should deal with the problem in its entirety and should be sufficiently flexible to ensure a fair outcome if circumstances changed.

29. Third, the scale of compensation should be fair. As a less prosperous Member State, the UK could reasonably expect to be a net beneficiary of the Community's financial arrangements, especially in view of the common commitment to the convergence of the economies of the Member States. We realised that such a big change in the present financial pattern would create problems for our partners and we were ready to take account of this. But we could see no justification for the United Kingdom being more than a very modest net contributor.

30. Mitterrand agreed that discussion should be resumed. France was not refusing to examine any aspect, but on the basis of the Thorn/Tindemans non-paper it would be difficult, without directives for the European Council. He could not accept the basis of the Thorn/Tindemans proposal.

31. Martens merely concluded that Foreign Ministers would need to do their best.

32. Discussion continued at the Foreign Ministers' dinner. Tindemans told Cheysson he had been distressed by Mitterrand's

/statement.

statement. Cheysson made a long, involved and unconvincing reply, the main thrust of which was that France could not agree a settlement the outcome of which would be as ill-defined as the Thorn/Tindemans formula. Precise figures were needed. (Comment: the main French worry seems to be that their calculations show the formula would yield progressive results for the UK.)

33. The Secretary of State had been puzzled by Mitterrand's remarks. Foreign Ministers had been rescued from failure by the Thorn/Tindemans formula, and the meeting on 3 April was to be held on the basis of it. The Secretary of State did not like this, but it was a basis for discussion. His other colleagues agreed: many expressed concern to Cheysson. Genscher intervened strongly, warning that if the affair dragged on German demands for action on their problem would grow.

DINNER DISCUSSIONS

34. Mitterrand was invited to report on his visits to Israel and the US. He started by claiming to have cleared his lines with the Arabs before he went to Israel. The timing had been difficult when he had first wanted to go the Israelis had bombed the Iraqis' nuclear reactor. The next time they had gone into South Lebanon. Then they had annexed Golan. He had had to go quickly before they did anything else! The Camp David process could not offer more than the withdrawal from Sinai: it could not solve the Palestinian question. He wanted to see Israel live within secure borders, which might need some adjustment, but something would also have to be done for the Palestinians. Israel's borders would have to be guaranteed by the USA, the Soviet Union and the European Community. None of this would be possible while Begin was there: like Abraham he thought he was working for God not Israel. But his days were numbered. In the meantime he would not negotiate. He had not been asked during his visit about the supply of arms but he had been asked to supply nuclear power stations and had said that this would only be possible with IAEA monitoring. On the West Bank he commented that Israel's actions were totally unjustified. Papandreou intervened to say that he doubted if the Israelis, were they to make a further incursion into South Lebanon, would go into the Syrian-held sectors, since Syrians were not free agents but were bound in every more they

made by the USSR, and involving them would automatically involve the Soviet Union.

35. Mitterrand, having mentioned in an aside that he had ordered a seventh nuclear deterrent submarine, went on to report on his talks with Reagan. During discussions of disarmament Reagan had asked about the position of Germany and Mitterrand had answered that the Germans were bound to be closer to the Soviet Union than the rest of the Allies for geographical reasons and because they were divided. He encouraged Reagan to reach agreement in Geneva quickly but got the impression that Reagan did not want to make rapid progress until the cruise missiles were in place in 1983. Mitterrand reckoned that the Russians were really scared of the Pershings. They could reach their territory in only six minutes from the Federal Republic.

36. Turning to his conversations on Central America, Mitterrand said that in his view the leader of the rebellion in El Salvador was fairly moderate. The Prime Minister argued that no-one who resorted to violence deserved support. Mugabe and Nkomo had agreed to exchange the bullet for the ballot. Papandreou and Schmidt however responded that guerilla activity could sometimes be necessary, with reference to the Colonels and Hitler respectively. Mitterrand suggested that Castro had not originally been a communist but had been pushed into it and thought that the same could happen elsewhere in Central America.

37. On relations between super-powers Schmidt gave voice to his favourite theme: since the days of Eisenhower no US President had served two terms, and the Russians simply could not understand this when compared with their own continuity. Schmidt also commented on the unwisdom of the current US policy of destroying its relations with China in favour of Taiwan.

38. Van Agt then raised the question of Community representation at the Versailles Summit and was supported by Heads of Government of the other small Member States. The Prime Minister said that she would not object to both Thorn and Tindemans being present at the Summit, but they would have to sort out between them who attended which of the restricted meetings. Schmidt pointed out that the Americans and Canadians would think that the Community was overegging things if it insisted on being represented by both Thorn and Tindemans at the restricted sessions when there were already four European Heads of

Government present. (Afterwards the Prime Minister told Martens privately that as far as she was concerned, he, Martens, as a Prime Minister should take precedence over the President of the Commission.)

39. Papandreou then raised the problem of the Turkish presence in Cyprus. In order to help remove the Turks, Greece would be prepared to pay the cost of replacing their army by UN troops.

40. Schmidt turned to the question of Hungary's debts. The Federal Government was prepared to help if at least two other Member States would do so. The Prime Minister said that the UK would and Van Agt confirmed that the Netherlands would. Spadolini, talking mainly about Poland, argued in favour of re-scheduling debts rather than enforcing default. But he thought that the whole future of credit for Eastern European countries should be looked at.

41. Apart from discussion of the 30 May Mandate (paras 24-33 above) Foreign Ministers discussed the Political Cooperation texts prepared earlier by Political Directors.

Tuesday 30 March

COMMEMORATION OF DR HALLSTEIN

42. The morning session opened with a minute's silence in memory of Dr Hallstein, whose death had just been announced.

GREECE AND THE COMMUNITY

43. Papandreou was invited to introduce the Greek memorandum. With the exception of Ireland, which was in many other ways different, Greece was the first country to join the Community with so low a GDP per head and so big a dependence on agriculture. The accession treaty was based on the Treaty of Rome, whose rules and mechanisms were appropriate to developed countries. They were not suitable for peripheral developing countries far behind the rest of the Community. Before Greek accession the Community had in any case experienced a widening gap between rich and poor regions. Average GDP per head in Italy for instance was much lower even than the average in North Italy. Full membership for Greece would make its problems worse. They had much imbalance in income between classes and regions. This was why at the November European Council he had stressed the need to find solutions and arrangements within the Community context to enable Greece to surmount its difficulties and develop faster, thus reducing the gap between Greece and the other member states. Special arrangements were indeed consistent with the economic guidelines laid down for the Greek economy. Some form of differentiation was required if only for a limited period: provisions taking account of Greece's specific economic problems. He warned that Portugal and Spain might well have the same problems.

44. In the Greek economy the tertiary sector was overdeveloped and parasitical. There was a whole parallel economy of which little was known, in which tax evasion was rampant, representing lost revenue of some 150-200 billion drachmas (compared with a budget of 900 million)*.

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* Figures as in Sir M Palliser's notes

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The distribution system was undeveloped and in the hands of a very few. The agricultural population was 30% of the whole and production 17% of GDP. Processing and manufacturing were only 19.6% of GDP. 85% of all companies employed fewer than five people. Greece imported 80% of its capital equipment. Investment in manufacturing industry was only 4% of GDP. In agriculture there was massive under-employment. It was highly seasonal. Holdings were very small. All this produced great disparities in incomes. The richest were the middle men exploiting the black economy. The average life-style in Athens was much like that in an Italian city, but in the country, especially in the mountains, it was more like that of Asia than Europe.

45. The world economic structural crisis made it even more difficult for Greece to adapt to the Community. Nonetheless the economy had still been growing at an average of 5% per annum. But there had been no structural reforms so the crisis had hit the Greek economy very hard. Inflation was about 25%. The government had introduced severe anti-inflationary measures, aiming to reduce the inflation rate to below 20% in 1982. But GDP had fallen in 1981 and the balance of payments deficit was \$2.3 billion. The public sector deficit in 1981 was 17% of GDP. Since the October elections the government had been trying to stabilise the currency and bring in some elements of social justice. They hoped for a 2-2½% increase in GDP in 1982 with the balance of payments deficit falling to \$2 billion and the public sector deficit down to 12% of GDP.

46. In spite of its economic difficulties Greece was spending more per head on defence than any member of the alliance other than the USA. They had 18 months military service, ^{and they} imported weapons systems which were costly in balance of payments terms. Greece's territorial integrity was threatened by Turkey, which had 120,000 troops on its Aegean coast. Yet the Alliance was not prepared to guarantee that territorial integrity, so Greece had to be prepared to do it itself.

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47. As a socialist government it had to redistribute income. Pensions and wages had been increased and indexation introduced for the first time, fully for the lowest paid, partially in the middle and not at all for those earning over \$1,000 per month. Many firms faced bankruptcy, crippled by interest rates of 20-21%. Mrs Thatcher had said it was not possible to prop up non-viable firms. But if the alternative was massive redundancy he did not see how that could be avoided.

48. Decentralisation of economic management was one of the government's main objectives. Local authorities had virtually now powers and no role in economic development, so powers had been transferred to them and they had been given 15 billion drachmas to enable them to manage their own budgets this year. The first five year programme would be ready by the autumn. (He gave details.)

49. Greece also suffered from a lack of scientists and technicians, who were all abroad. The government was trying to attract them back to the decentralised regions. Agricultural productivity was very low. The new co-operatives would take a long time to become really competitive with others in the Community, so special measures were needed. A substantial increase in agricultural prices in the Community was required. With an inflation rate of 20% Greece could not accept an increase of only 10%, which would be explosive in the agricultural labour force.

50. The arrangements being made by the Community must enable Greece to carry out its economic programme and not strangle it at birth. Exceptions to the rules in the Treaty of Rome and the accession treaty would be needed. In addition resources would have to be found to bridge the large gap between Greece and the other member states. If the Community was unwilling to transfer resources through the Regional Fund or FEOGA guidance for the restructuring of agriculture the gap would simply grow. That would be in no-one's interest. The reforms needed would not be as great as those in the 30 May Mandate. But at present resources were mainly used to support prices of northern products like milk, while Mediterranean products got very little. The problem was political. The Community was

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getting bigger. With the negotiations with Spain and Portugal the Community was beginning to have its own north-south problem. In his report on European union Tindemans had made clear that if the Community did not solve the problems of its Mediterranean members there would be a two-speed Europe which would shake the Community to the core.

51. The Commission was studying the Greek proposals and would present its own in May. There would then have to be a full discussion in the Council. A new political decision in the Community to solve Greece's problems was needed. Otherwise the Greek government would have to look at other approaches. This was not a threat. But Greece and the Community were on a slippery slope if solutions could not be found.

52. Thorn said that the Commission were studying the Greek memorandum within the Treaty framework. Some points were relatively easy, but others were much more difficult. He was glad that Papandreou had recognised that Greece had problems in common with other Mediterranean countries. He pointed out that already in 1982 there would be substantial transfers to Greece. The Commission would give a first reaction next month with a view to discussion in the Council in June. Martens summed up that the European Council took note that the Council would discuss the problem as soon as possible.

DISCUSSION OF TEXTS

53. The remainder of the session, which did not finish until shortly after 1400, was devoted to discussion of the draft Presidency conclusions on Community and political co-operation subjects, the final texts of which are attached.

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