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PRIME MINISTER

STRASBOURG EUROPEAN COUNCIL:
ECONOMIC AND MONETARY UNION

You have a meeting with the Chancellor, the Foreign Secretary and the Governor of the Bank of England tomorrow afternoon to discuss the handling of EMU at the European Council in Strasbourg.

Ostensibly the only decision being sought at Strasbourg is on whether to start an IGC in the second half of 1990. As you have pointed out this is not a purely procedural decision. Agreeing to an IGC implies acceptance that Treaty amendment is necessary: we do not agree that it is.

The situation is clouded by uncertainty over exactly what Chancellor Kohl intends to propose. he seems to be saying that there should be consensus on the aims and contents of EMU before an IGC starts. This is not in practice helpful since:

- it assumes an IGC is necessary;
- he appears to think such consensus can be reached in time for an IGC to start in the second half of 1990;
- worse still, he envisages a finishing date, to enable the results of an IGC to be implemented by 1994.

In short, he is unlikely to be much help.

You have agreed to the Chancellor's approach which accepts that we will be out-voted on the starting date for an IGC but tries to attach conditions to it. These would:

- reiterate the steps which need to be taken before an IGC (continued analysis of all the options, full and adequate preparation, liberalisation of capital movements);

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- ensure that our ideas would be taken into account during an IGC and that it would not deal only with the Delors' proposals: also that experience with implementing Stage I would be taken into account: and that the principle of subsidiarity would be given full weight;1
- confirm the need for a high degree of convergence of economic performance.

At tomorrow's meeting you might:

- ask the Chancellor what success we have had with floating these conditions privately (we cannot do it openly ourselves, since we shall vote against an IGC altogether);
- ask the Foreign Secretary for his latest assessment of the German position;
- consider whether we can get agreement now to the proposition that no subsequent stage of EMU should be implemented until Stage I has been completed and in action for a reasonable period (the Governor's proposition);
- commission any further work on the Speaking Note which has been provided for your use at Strasbourg (copy in folder).

On another matter, I have heard this evening that the Foreign Secretary has it in mind to do a paper for Cabinet on Thursday on Strasbourg. You might ask him what he intends this should cover: and suggest you see it in draft (it is after all you who represents the UK at European Councils).

You will find in the folder:

- the draft Speaking Note for Strasbourg

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- the conclusions of the Madrid Council on EMU (plus your conditions on ERM)
- the Chancellor's minute on conditions to the attached to EMU
- the Foreign Secretary's note on Chancellor Kohl's current position
- the Governor's letter.

C.D.T

CHARLES POWELL

4 December 1989

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Sam
PRIME MINISTER

STRASBOURG: ECONOMIC AND MONETARY UNION

You have a meeting on Tuesday afternoon to discuss how to handle the economic and monetary union debate at Strasbourg with the Chancellor and the Foreign Secretary. Would you like to add the Governor of the Bank of England (in the light of his letter to you this weekend)?

C.D.P.
CHARLES POWELL
3 DECEMBER 1989

CONDITIONS FOR AN IGC

DRAFT

*More democratic accountability -
through the national parliaments*

The European Council:-

(a) noted that the provisions necessary for the launch of Stage I, the full implementation of which would bring substantial benefits to the Community and constitute a major step towards Economic and Monetary Union, were now ready for adoption, and accordingly confirmed that Stage I would start on 1 July 1990;

*Full
program*

(b) noted that all member states now agreed that further measures in addition to those outlined in the Delors Report's prescription for Stage I would be required; and noted that the documents before the Council, including the UK's paper entitled 'An Evolutionary Approach to Economic and Monetary Union', identified a number of questions and issues which would require further analysis both before and during an Inter-Governmental Conference;

*Proper
study
All
possibilities*

(c) in the light of (b) above, invited the competent bodies to continue their analysis of the questions and issues raised by these documents; and confirmed the need for full and adequate preparation for such a Conference;

(d) noted the need to take full account during an Inter-Governmental Conference of progress in implementing Stage I measures, and the effects of these measures, including liberalisation of the insurance, banking and investment services sectors, and strengthening of competition policy; recalled that progress towards Economic and Monetary Union requires a high degree of convergence of economic performance between member states; recalled also the need to take full account of the principle of subsidiarity; and agreed that the effects of Stage I measures would be relevant to subsequent decisions on the timing of later moves;

*Full
clear
measures
- experience
stage 2**Improved
competition
policy**(c) See overpage.*

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(e) on the above basis, and on the assumption that actions required by then on the Capital Movements Liberalisation Directive 1988 would have taken place, agreed in principle that it would then be appropriate to convene such a Conference.

EMU: STATEMENTS BY KARL OTTO PÖHL

Statements helpful to UK line

1. The President of the Bundesbank has made a number of recent statements helpful to the UK line on EMU:

- Article in Handelsblatt, 30.12.88: "Economic and Monetary Union cannot be achieved by revolution, but by an evolutionary process [which, although it will not be without its setbacks, is already irreversible]."

"Today, however, the creation of supra-national institutions able to make binding decisions in the most important areas of economic and monetary policy appears visionary. This includes the goal of a European Central Bank System."

"The next steps towards a new European future do not require drastic institutional changes [nor should they lead to dangerous detours such as a parallel currency]."

- Interview in "Le Figaro", 11-12 March: "To move from the EMS to a new monetary Europe will require Treaty change. But the road will be long, and it will be wholly premature to expect the creation of a European Central Bank in the near future."

- Press Conference, 18.4.89: "In Germany and some other countries capital movements have been free of restrictions for a long time. Other countries, however, still impose considerable restrictions on money and capital movements. Before one considers a European monetary union, all existing restrictions should first be lifted. I find it somewhat astonishing that the countries which are making the strongest calls for an economic and monetary union.... are the very countries which are unable to observe the comparatively easy rules of the European Monetary System."

Central Bank Governors, EMS Treaty). No new Treaty and no new institutions are required for the time being."

← - Speech in Munich, 22.6.89: "I myself doubt whether the time has come for such a comprehensive renunciation of sovereignty, namely the transfer of monetary powers to supra-national institutions. I can only repeat what I said a little while ago. Neither a single currency nor a European Central Bank is necessary for an economic and monetary union to function... As I see it, there are two risks associated with a premature and badly prepared "Inter-Governmental Conference" on such a Treaty: it could lead to considerable tension and conflict within the EC. Worse still is the possibility of failure."

- Interview in FT, 1.7.89: "I think one should not start on such a venture [an IGC/Treaty change] unless there is a good chance of finishing the process. If the danger of failure was judged relatively great - and it is my view that it is relatively great, to start with, at least - then it would be better to wait."

← - Speech in Frankfurt on 7.11.89: Pöhl repeated his criticism of pressure for an IGC in the second half of 1990 and said that in the view of the Bundesbank there was no obvious reason to move quickly to a common EC monetary policy. He said he was very sympathetic towards the British paper, which he described as "a realistic and sensible description of what monetary policy should concentrate on in future years."

Others Statements

2. M Delors commented during his meeting with the Prime Minister on 1 December that Herr Pöhl tended to make conflicting statements. There is some truth in this:

- In a speech on 26 January, Pöhl said: "I am wholly in favour of the creation of a European Central Bank and a

My thoughts in the this connection go particularly to Italy and Spain."

"In the interest of European integration, which I personally advocate most strongly and which I gladly support, one should warn against false expectations. Failure would be the worst thing that could happen to us. You know what became of the Werner Report and similar expert reports."

- Interview in Le Monde, 23.5.89: "Whether or not there will one day be a decision-making institution involving, as Mrs Thatcher rightly said, a far-reaching transfer of sovereignty, is a political decision."

- Speech to German Saving Banks' Congress, 8.6.89: "The British Government is not the only one which has difficulties in accepting the transfer of sovereign rights to supra-national institutions. That goes for the Federal Republic too. For example, the creation of a European Central Bank System equipped with real monetary policy powers... would require far-reaching changes to the Bundesbank and I do not know whether there would be broad agreement for such changes in the Federal Republic in the foreseeable future."

"In my opinion, it would be a serious mistake to begin inter-Governmental negotiations on this at an early stage as some people have suggested... if we advise caution, this does not mean we are against economic and monetary union, but that we assess the chances realistically."

"More important than amendments to the EC Treaty and the creation of new institutions is the need to expand existing developments towards an economic and monetary union and to implement those decisions which have already been taken.... The institutional prerequisites for closer economic, financial and monetary cooperation among EC member states already exist (ECOFIN, Monetary Committee, Committee of EC

European currency". He went on, however, to say that "the enormous practical and political difficulties involved are obvious to anyone who is familiar with the material. A European Reserve Bank and a European currency would also, as the British Chancellor of the Exchequer has recently pointed out, involve Governments giving up important areas of financial sovereignty. This may be desirable, but it is for the foreseeable future impracticable."

- At his press conference on 18 April, Pöhl said: "One can only enter the first stage if it is agreed that at the end of the first stage there is the second and then the third stage. One cannot start a journey without knowing the destination."

3. Herr Pöhl is also a leading advocate of UK membership of the ERM, for which he called in virtually all of the statements listed above.

Others' Objectives

- France, supported by most other states: to secure agreement that an IGC will start in autumn 1990; and not to constrain the work of that conference by setting advance conditions.
- Germany: to ensure that there is thorough preparatory work for an IGC by the competent ECOFIN organisations, with the aim of achieving a consensus before an IGC begins. Germany may also seek agreement on a date by which any Treaty amendments should be ratified at both Community and national level (possibly the June 1994 European Parliament elections).
- Some member states: may seek a wider remit for an IGC: for example to introduce qualified majority voting on environmental and social issues (Denmark); and to strengthen further the powers of the European Parliament (Germany and some southern states).
- Various member states: may put pressure on the UK to join the ERM at an early date.

Order of Peace
in Europe in which
the German people
refuse its unity
through
free

self-determin.

les machinations
les machinorage

*A sufficient majority
emitted for the calling of IGC
(which will establish its agenda -
the calendar for it).*

Our Response

- As stated, the UK does not believe that Treaty change is necessary. The approach explained in our paper does not require this. It is therefore premature to call an Inter-Governmental Conference until all approaches have been thoroughly analysed.
- Repeat that UK could not vote in favour of a decision to call an IGC. But welcome any recognition that further work is needed, both before and during any Conference. Strongly agree that work should take place in the ECOFIN-based bodies, especially the Monetary Committee. Reject any suggestion that an end-date should be set for an IGC or ratification by national parliaments. Cannot and should not pre-judge that now. No need for rush: Stage I has not even started yet.
- It would certainly not be appropriate to broaden the remit of an IGC. Institutional matters were fully discussed at the time of the Single European Act: it is far too soon for further change. [If a second IGC in 3-4 years' times on non-EMU matters is suggested: premature to take such a decision now.]

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- The UK will join the ERM when the level of UK inflation is significantly lower, when there is capital liberalisation in the Community and when real progress has been made towards completion of the single market, freedom of financial services and strengthened competition policy.

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