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From the Private Secretary

21 March 1990

PRIME MINISTER'S TALK WITH THE NETHERLANDS PRIME MINISTER

Mr. Lubbers telephoned the Prime Minister this morning and they talked for some 15 minutes or so, mostly about aspects of German unification but also about the EBRD.

Mr. Lubbers asked how the Prime Minister read developments in Germany. He was a bit uncertain about the way ahead after the East German elections. Would EC Heads of Government be expected to reach decisions in Dublin on the EC aspects of unification for instance? The Prime Minister said that she was pleased with the outcome of the East German elections. She had been concerned that an SPD victory would have tilted the balance towards socialism in a united Germany. As it was, we could now be reasonably sure that a united Germany would remain in NATO. She did not think that the informal meeting of EC Heads of Government in Dublin should be the occasion for decisions. Rather, there should be a general discussion, with guidelines set for future work. The one essential principle to be agreed was that the Federal Republic should finance the costs of changes in East Germany. We could not have the Structural Funds denuded for this purpose. Mr. Lubbers agreed.

The Prime Minister asked what Mr. Lubbers thought would be the implications of German monetary union for the Deutschmark. Mr. Lubbers said that the Federal Republic was taking a risk by offering a 1:1 conversion rate between the DM and the Ostmark. It would also be a very difficult operation technically to convert some Ostmarks now, while spreading conversion of the remainder over a period of years. On the other hand, Germans were natural savers and this would reduce the risk of inflationary consequences. Before unification had become a real possibility, there had been pressure for the Deutschmark to be revalued within the ERM. The prospect of unification had taken off some of the pressure for this. In short, he did not see any insuperable difficulties for the ERM from German monetary union, provided the East Germans did not go and splash out their new DMs on consumption.

The Prime Minister said that we had done quite a bit of work on the EC aspects of unification and identified a considerable number of problems, particularly over monitoring East German observance of the EC's rules in the absence of any sort of border controls. Mr. Lubbers said this was a problem with which the Community was already familiar because of the inner-German trade agreement. But he very much agreed it would be necessary to find some way of preventing cheap goods being brought into the Community through East Germany, particularly in the period before unification. This could be an argument for speeding up unification under the Article 23 procedure, so as to establish the Eastern border of East Germany rapidly as the Community's outer border. But he was not keen on other grounds to see this happen too quickly. The short answer was probably to obtain some sort of guarantee from the Federal Republic to protect the EC market. He very much agreed with the Prime Minister that it would be too early to try to reach decisions in Dublin.

Mr. Lubbers asked next about the NATO aspects of the unification. The Prime Minister said that Chancellor Kohl had been commendably firm about the membership of a united Germany in NATO. Our aim should be to see Articles 5 and 6 of the Brussels Treaty extended to the GDR. A particular difficulty would be the status of the former GDR. It would probably be necessary to provide for Soviet troops to remain there for a transitional period. Apart from anything else, this would be necessary from the point of view of Mr. Gorbachev's own position. Mr. Lubbers said that he agreed with this and hoped the Federal Republic would accept it. The Prime Minister said she understood early Dutch anxiety about the Four plus Two group. Mr. Lubbers said that they were no longer worried, but had been keen at an earlier stage to put pressure on the Federal Republic to take account of their neighbours' interests.

Mr. Lubbers asked how the Prime Minister saw developments in Lithuania. The Prime Minister said we had reacted with caution. The Lithuanians had expressed their view, and this should now be resolved in discussions with Mr. Gorbachev. We had not openly supported independence, not least because we would not be able to give the Lithuanians much practical help. Mr. Lubbers said that he thought some arrangements could be worked out which would give the Lithuanians the appearance of sovereignty, while giving the Soviet Union a special position in Lithuania. We had to take every opportunity to signal our support for Mr. Gorbachev, whose position seemed to be at some risk.

Mr. Lubbers said that he wanted just to mention the European Bank for Reconstruction and Development. The Prime Minister's message of 30 January had kindly offered support for the candidacy of Mr. Ruding to be President of the Bank. We had to find a way to bring this matter, and the site of the Bank, to a head. The Prime Minister said we took the view that the President must come from an EC country. We hoped the Community would identify a single candidate at the informal ECOFIN meeting on 31 March. We would certainly support Mr. Ruding and hoped that a majority could be found for him. But if there was not such a majority, the position would be open. Mr. Lubbers said that he was not pessimistic. Monsieur Attali's candidature had the personal support of President Mitterrand, although Monsieur Rocard was uneasy about it. The fact was that Attali was not a banker and not really qualified for the job. We had to find some way of helping President Mitterrand off this hook. Anyway, the

French had far too big a share of international posts already. The Prime Minister said that we believed that London was the best site for the Bank, but did not want to have to pay the price of having Attali as President to secure that. It really ought to be someone with experience as a Finance Minister or central banker. She and Mr. Lubbers should keep in touch as the game unfolded.

The Prime Minister wondered afterwards whether Mr. Lubbers might have been trawling for an invitation to come over here for talks. It would genuinely be very difficult to fit this in to the diary at present. But if there is reason to think that he would like to come, she would of course do her best to fit something in before the meeting in Dublin on 28 April. Perhaps our Ambassador in the Hague could take some discreet soundings, without actually precipitating a request for a meeting.

I am copying this letter to John Gieve (H.M. Treasury), Martin Stanley (Department of Trade and Industry), Simon Webb (Ministry of Defence) and Sonia Phippard (Cabinet Office).

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