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MDHIAN 7966

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MIPT: GEMU: TALK WITH POEHL

SUMMARY

1. POEHL SAYS HE SUPPORTS THE FEDERAL GOVERNMENT'S NEW OFFER TO GDR ON EXCHANGE RATES, COMMENTING THAT KOHL HAD NO OTHER CHOICE. HE CLAIMS THAT, PROVIDED GDR INCOMES ARE FROZEN BEFORE A 1:1 EXCHANGE, THE EFFECTS CAN BE CONTAINED. HE REGARDS THE DOUBLING OF THE CEILING FOR CONVERSION OF SAVINGS AT 1:1 AS JUST TOLERABLE. HE PROFESSES OPTIMISM ABOUT INFLATION BUT DOES NOT EXCLUDE SOME FURTHER INCREASE IN INTEREST RATES.

DETAIL

2. I HAD OVER AN HOUR WITH BUNDESBANK PRESIDENT POEHL THIS MORNING, IN THE COURSE OF WHICH HE WAS TELEPHONED BY TIETMEYER WITH THE NEWS OF THE GOVERNMENT'S DECISION TO MAKE THE ANNOUNCEMENT IN TUR. HE WAS EVIDENTLY NOT SURPRISED AND SAID THAT, WHILE IT WAS IN ONE WAY NOT SENSIBLE TO ANNOUNCE THE FRG'S PROPOSAL ON EXCHANGE RATES BEFORE NEGOTIATIONS WITH THE GDR BEGAN, THERE WAS EVERY LIKELIHOOD THAT THE COALITION AGREEMENT WOULD HAVE LEAKED IN ANY CASE.

3. ON WAGES AND PENSIONS POEHL EMPHASISED THAT THE FRG'S OFFER OF A 1:1 EXCHANGE RATE WAS CONDITIONAL UPON INCOMES MEANWHILE BEING FROZEN AT THEIR PRESENT LEVEL. (HE WAS PRESUMABLY REACTING TO DE MAIZIERE'S STATEMENT ON 19 APRIL THAT WAGES WOULD NEED TO BE SUBSIDISED BEFORE PRICES WERE DECONTROLLED.) ON THIS BASIS THE FRG'S PROPOSAL WOULD NOT BE VERY DIFFERENT IN ITS EFFECT ON GDR INCOMES FROM THE BUNDESBANK'S EARLIER PLAN OF ALLOWING WAGES TO RISE BEFORE CONVERTING THEM AT 2:1. POEHL ADMITTED THAT THE BUNDESBANK'S PROPOSAL HAD BEEN TOO COMPLEX FOR GDR CITIZENS TO UNDERSTAND. IN THE END GDR FIRMS WOULD HAVE TO DECIDE WHAT THEY COULD PAY IN TERMS OF PRODUCTIVITY. INEVITABLY THERE WOULD BE BANKRUPTCIES AND UNEMPLOYMENT AND CONTINUING MIGRATION TO THE FRG.

4. I PRESSED POEHL ON THE POSSIBLE INFLATIONARY CONSEQUENCES OF THE FEDERAL GOVERNMENTS'S POSITION. HE SAID THAT HE WAS NOT PESSIMISTIC

ABOUT INFLATION. IF WAGES WERE FROZEN UNTIL CONVERSION, THERE WOULD BE JUST ENOUGH FOR PEOPLE TO LIVE ON AND NO GREAT INCREASE IN DEMAND. THE FEDERAL GOVERNMENT'S DECISION TO EXCHANGE AT 1:1 THE FIRST DM 4000 OF PERSONAL SAVINGS, DOUBLE THE FIGURE PROPOSED BY THE BUNDESBANK, WOULD ADD DM 8 BILLION TO LIQUIDITY. THAT WAS AT THE LIMIT OF THE TOLERABLE. BUT HE DID NOT THINK THAT PEOPLE WOULD USE MUCH OF THEIR SAVINGS ON CONSUMPTION. INCREASED DEMAND WAS LIKELY TO DRAW IN ADDITIONAL IMPORTS. SOME OF THESE WOULD COME FROM THIRD COUNTRIES AND THERE WOULD BE OPPORTUNITIES FOR BRITISH FIRMS AMONG OTHERS. SOME WOULD COME VIA THE FRG, AND THIS WOULD HELP TO REDUCE THE FEDERAL REPUBLIC'S TRADE SURPLUS WITH THIRD COUNTRIES.

5. I ASKED WHETHER THE INCREASED DEMAND FOR CAPITAL FOR INVESTMENT PURPOSES MIGHT DRIVE UP THE DM INTEREST RATE. POEHL SAID THAT THIS WAS INDEED A PROBLEM. REAL INTEREST RATES WERE ALREADY VERY HIGH AND MIGHT GO A BIT HIGHER. OVER-HEATING OF THE FEDERAL GERMAN ECONOMY WAS A POTENTIAL WORRY, PARTICULARLY IF THE METAL WORKERS UNION KEPT ON TRYING TO DRIVE UP WAGES.

6. POEHL SAID THAT HE UNDERSTOOD KOHL'S POLITICAL PROBLEM OVER THE EXCHANGE RATE. IT WAS POLITICALLY DIFFICULT TO EXCHANGE INCOMES AT ANY RATE OTHER THAN 1:1 INDEED THAT HAD PROBABLY BEEN THE ONLY POSSIBLE DECISION. HE THOUGHT KOHL HAD GAINED CONSIDERABLY IN STATURE RECENTLY. IT WAS TRUE THAT THE FEDERAL GOVERNMENT'S PROPOSAL WOULD LEAD TO GREATER UNEMPLOYMENT IN THE GDR IN THE SHORT TERM. BUT WAGE DIFFERENTIALS BETWEEN THE FRG AND GDR WOULD HAVE CAUSED A CONTINUING PROBLEM OF MIGRATION WHATEVER THE EXCHANGE RATE. A CERTAIN AMOUNT OF DESTRUCTION OF GDR INDUSTRY WAS ESSENTIAL TO ACHIEVE RECOVERY. HE THOUGHT THAT THIS WOULD BE FAIRLY RAPID. THE GDR WAS A RELATIVELY SMALL PROBLEM COMPARED WITH THE REST OF EASTERN EUROPE AND WITH THE SOVIET UNION IN PARTICULAR.

7. POEHL SAID THAT THE INSTITUTIONAL SIDE OF GERMAN MONETARY UNION WAS NOT YET AGREED. HIS POSITION WAS THAT THE DM WOULD REMAIN THE CURRENCY OF THE FRG UNDER THE CONTROL OF THE BUNDESBANK. THE GDR WOULD BE ALLOWED TO USE THE DM BUT WOULD NOT HAVE CONTROL OVER IT. THE BUNDESBANK WOULD HAVE SOME 15 BRANCHES IN THE GDR WHICH WOULD BE COORDINATED FROM WEST BERLIN. IF HE HAD HIS WAY, THE GDR STATE BANK, WHICH HE SAID WAS FULL OF EX-STASIS, WOULD BE LIQUIDATED. HE REFUSED TO DEAL WITH IT. THE BUNDESBANK ALONE WOULD DECIDE ON LIQUIDITY AND INTEREST RATES. THE GDR GOVERNMENT WOULD NO LONGER HAVE RECOURSE TO THE PRINTING PRESS TO FUND EXPENDITURE. I ASKED WHETHER THERE WOULD HAVE TO BE LIMITS ON BORROWING BY THE GDR GOVERNMENT. POEHL SAID THAT THIS WAS A CRITICAL POINT WHICH SO FAR HAD ATTRACTED LITTLE

ATTENTION. THE FRG DRAFT FOR THE STATE TREATY ON GEMU PLACED BINDING LIMITS ON SUCH BORROWING. HE DID NOT KNOW WHETHER THE GDR WOULD ACCEPT THIS TOUGH POSITION IN THE NEGOTIATIONS. THE NEW MINISTERS (''PRIESTS AND PROFESSORS'') WERE DIVORCED FROM REALITY. (POEHL'S PRIVATE SECRETARY TOLD ME THAT THE GDR STATE BANK WAS RESISTING ITS OWN ABOLITION AND INSISTING ON REPRESENTATION ON THE BUNDESBANK COUNCIL. THIS WAS UNACCEPTABLE AS AN INTERIM SOLUTION AND WOULD PREJUDICE ARRANGEMENTS AFTER STATE UNITY.)

8. I ASKED POEHL ABOUT THE BUDGETARY COST OF GEMU TO THE FRG. HE SAID THAT THE WEIGHT OF SUPPORTING THE GDR AFTER GEMU WOULD FALL ON THE FEDERAL BUDGET IN TENS OF BILLIONS OF DMS ANNUALLY. HIS GUESS WAS ABOUT DM 40 BILLION NET. THIS WAS MANAGEABLE, WHEN ONE CONSIDERED THAT THE BERLIN SUBSIDY ALONE WAS DM 20 BILLION.

9. POEHL'S EXPECTATION WAS EVIDENTLY THAT MONETARY UNION WOULD BE EFFECTED ON 1 JULY. HIS PRIVATE SECRETARY TOLD ME THAT ANYTHING EARLIER THAN THAT WOULD BE EXTREMELY DIFFICULT ADMINISTRATIVELY.

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