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OF 061641Z NOVEMBER 90
INFO ROUTINE UKREP BRUSSELS, PARIS, ROME
INFO SAVING BERLIN, FRANKFURT

FRAME ECONOMIC

POEHL'S CALL ON THE PRIME MINISTER

SUMMARY

1. POEHL IS CRITICAL OF THE OUTCOME OF THE EUROPEAN COUNCIL AND WORRIED ABOUT THE COST OF UNITY. HE IS BEING CAREFUL ABOUT WHAT HE SAYS IN PUBLIC IN THE RUN UP TO THE ELECTIONS, BUT HIS DIFFERENCES WITH THE FEDERAL GOVERNMENT ARE NONETHELESS APPARENT. THE BUNDESBANK PROBABLY SEE THE UK AS POTENTIAL ALLIES IN SLOWING DOWN THE EMU BANDWAGON, THOUGH THEY DO NOT SHARE OUR ULTIMATE AIMS.

DETAIL

2. THE PRESIDENT OF THE BUNDESBANK WILL CALL ON THE PRIME MINISTER AT 5.30 ON 8 NOVEMBER. YOU MAY THEREFORE WELCOME THE FOLLOWING SUMMARY OF HIS VIEWS.

3. AS PREVIOUSLY REPORTED BY LETTER, POEHL WAS HIGHLY CRITICAL OF THE OUTCOME OF THE EUROPEAN COUNCIL WHEN HE SPOKE AT AN EVENT ORGANISED BY THE FRANKFURTER ALLGEMEINE ZEITUNG ON 31 OCTOBER IN BERLIN. HE SAID THAT IT WAS NOT IN HIS OPINION A PROPER BASIS FOR SUCH A FAR REACHING DECISION AS THE INTRODUCTION OF MONETARY UNION IN EUROPE. IN PARTICULAR HE FOUND THE WAY THE COMMUNIQUE DESCRIBED THE SECOND STAGE OF MONETARY UNION ALMOST INCOMPREHENSIBLE. HE WAS SCORNFUL OF THE PASSAGE ON OVERSEEING THE DEVELOPMENT OF THE ECU: IN HIS VIEW THERE WAS NO NEED FOR A NEW INSTITUTION TO SUPERVISE THE DEVELOPMENT OF THE ECU OR TO CO-ORDINATE MONETARY POLICY BECAUSE 'WE ARE ALREADY ABLE TO DO THAT TODAY'.

4. POEHL AVOIDED DIRECTLY CRITICISING THE DECISION OF ELEVEN HEADS OF GOVERNMENT TO SET A DATE FOR THE START OF STAGE 2. HE SAID HOWEVER THAT THE SUBSTANCE WAS MORE IMPORTANT THAN THE DATE. THE COMMUNITY HAD OFTEN SET DEADLINES WHICH IT FAILED TO MEET. IT WAS

NOT A MATTER OF DELAYING OR ACCELERATING, BUT SIMPLY A MATTER OF TAKING THE RIGHT DECISIONS. THE SECOND STAGE DEPENDED ON THREE ELEMENTS: PREPARATION OF THE CONSTITUTION OF A CENTRAL BANK TOGETHER WITH A DECISION ON ITS LOCATION: ADAPTION OF NATIONAL LEGISLATION TO PROVIDE FOR THE HANDING OVER OF MONETARY RESPONSIBILITY OF THE CENTRAL BANK: AND THE ACHIEVEMENT OF THE NECESSARY ECONOMIC CONVERGENCE, ON WHICH THERE WAS A LONG WAY TO GO.

5. POEHL THOUGHT THAT THE LITMUS TEST OF THE COMMUNITY'S READINESS TO MOVE TO STAGE 2 WOULD BE WHETHER IT ACCEPTED THE NEED TO TRANSFER SOVEREIGNTY TO A TRULY INDEPENDENT EUROPEAN CENTRAL BANK. HE HAD NO INTENTION OF BEING A BRAKE ON PROGRESS, BUT THE START OF STAGE 2 WOULD BE A POINT OF NO RETURN, AND THE ESSENTIAL ELEMENT WAS THAT A EUROPEAN CENTRAL BANK SHOULD BE NO LESS EFFECTIVE IN THE CONTROL OF INFLATION THAN THE BUNDESBANK.

6. COMMENTING ON THE COST OF FINANCING GERMAN UNITY, POEHL SAID THAT HE WAS OPPOSED TO AN UNRESTRICTED CALL ON THE CAPITAL MARKET. 'IF TAX INCREASES AND OVERSTRETCHING THE CAPITAL MARKETS ARE TO BE AVOIDED, OTHER FORMS OF FINANCING GERMAN UNITY MUST BE BROUGHT INTO PLAY', IE CUTS IN GOVERNMENT EXPENDITURE. A SUBSEQUENT SPEAKER CONCLUDED THAT THE LOGIC OF POEHL'S APPROACH WAS THAT HE FAVOURED TAX INCREASES BUT WAS NOT PREPARED TO SAY SO. A BUNDESBANK OFFICIAL SUBSEQUENTLY TOLD US THAT POEHL WAS HESITANT ABOUT ADVOCATING TAX RISES, PARTLY BECAUSE OF THE PROXIMITY OF THE FEDERAL ELECTIONS, PARTLY BECAUSE TAXATION WAS NOT DIRECTLY HIS FIELD OF RESPONSIBILITY AND PARTLY BECAUSE SOME FORMS OF INCREASED TAXATION WOULD RISK REDUCING THE ABILITY OF THE PRIVATE SECTOR TO INVEST IN THE GDR.

COMMENT
7. POEHL IS BEING CAREFUL ABOUT WHAT HE SAYS IN PUBLIC IN THE RUN UP TO THE GENERAL ELECTION. HE HAS NOT THEREFORE DIRECTLY CRITICISED THE SETTING OF A DATE FOR STAGE 2 OF EMU NOR HAS HE REFERRED OPENLY TO WHAT IS THOUGHT TO BE HIS VIEW THAT TAX INCREASES WILL BE NEEDED TO FINANCE UNIFICATION. HIS OFFICIALS HAVE PLAYED DOWN THE RECENT ADJUSTMENT OF THE LOMBARD RATE (MY TELNO 1393) AS A PURELY TECHNICAL MEASURE. A GAP BETWEEN THE FEDERAL GOVERNMENT AND THE BUNDESBANK ON SOME CENTRAL ISSUES IS NEVERTHELESS BECOMING APPARENT.

8. WE HAVE NO RECENT INFORMATION ON HOW POEHL CURRENTLY SEES THE BRITISH POSITION. A PREVIOUS SPEECH IN BERLIN ON 25 OCTOBER, BY

FAX TO ECD(I), SPELLED OUT IN DETAIL HIS DOUBTS ABOUT THE HARD ECU PROPOSAL. FOLLOWING THE EUROPEAN COUNCIL TIETMEYER (MEMBER OF THE CENTRAL BANK COUNCIL) TOLD OUR CONSUL-GENERAL IN FRANKFURT THAT HE WAS AFRAID THAT THE BRITISH WOULD HAVE ISOLATED THEMSELVES. IT WAS IMPORTANT THAT THE BRITISH SHOULD REMAIN IN THE DEBATE IN ORDER TO HAVE A CHANCE OF INFLUENCING IT. IN THOSE CIRCUMSTANCES HE IMPLIED THAT IT WOULD BE POSSIBLE TO COOPERATE IN MAKING SURE THAT THINGS DEVELOPED SENSIBLY. THE BUNDESBANK PROBABLY SEE THE UK AS POTENTIALLY USEFUL ALLIES IN SLOWING DOWN THE EMU BANDWAGON TO AN ACCEPTABLE PACE, EVEN IF WE DISAGREE ABOUT THE DIRECTION IT SHOULD BE GOING.

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