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RECORD OF A DISCUSSION BETWEEN THE CHANCELLOR AND MR EDWIN MEESE,
COUNSELLOR TO THE US PRESIDENT, AT 5.30PM ON 6 MAY
AT No 11 DOWNING STREET.

Present:	Chancellor	Mr Meese
	Mr Littler	Mr Streator (US Embassy)
	Mr Kerr	

The meeting considered the economic issues for the Williamsburg Summit.

Intervention

The Chancellor thought the G7 statement of 28 April a helpful development, which the Summit might note. Intervention had a legitimate role at the margin; but its efficacy should not be exaggerated. It could help trim over- or under-shoots, unjustified by relative national economic performance. Concerted intervention might be appropriate in such circumstances. But no amount of intervention could stop exchange rate movements where economic performance differed widely: convergence of national economic policies must therefore be the primary aim.

2. Mr Meese agreed with the Chancellor's analysis, but asked about the French attitude. Had they reacted to the final paragraph of the G7 statement? The Chancellor said that they had reacted to the interpretation which Secretary Regan, at his press conference on 28 April, had put on that paragraph.

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3. Mr Meese said that it was his impression that Finance Ministers of the Summit countries were meeting more frequently than before. The Chancellor confirmed this: G5 Ministers had met in Canada and in Germany in the autumn, and in Washington twice this year. The presence of the IMF Managing Director at certain of these meetings, and the circulation by him of papers analysing differences in national economic performance, was helping to encourage the development of a form of "group therapy". But the issue causing most concern was undoubtedly the scale of the prospective US deficit.

US Deficit

4. Mr Meese agreed that the deficit must be one of the factors keeping interest rates up and the dollar strong. It was hard to judge the performance of the monetary aggregates. The President's proposed stand-by taxes should ensure that the deficit was in due course put on a declining path, and eliminated by 1989 or 1990. Interest rates seemed for the present to be on a plateau.

5. The Chancellor said that the problems facing the US administration were in some respects reminiscent of those encountered in the UK in 1980. We too had then experienced difficulty in interpreting the monetary aggregates; together with a rising deficit. It had taken the stringent measures in the 1981 Budget - "double-indexation" of indirect taxes, and no indexation of personal allowances - to convince the market of our determination to hold to policies which would reduce both inflation and interest rates. The PSBR as a percentage of GNP had fallen from almost 6 per cent in 1980-81 to 3½ per cent in 1981-82, 3¼ per cent in 1982-83, and a planned 2¾ per cent in the current year.

/6. Mr Meese said



6. Mr Meese said that perhaps the Chancellor should show Congress these figures. The Administration recognised the need to reduce the deficit: their difficulty lay on the Hill. The Chancellor thought that the effect on the world economy if Congress could be persuaded to act in such a way as substantially to reduce US, and hence world, interest rates would be hardly less dramatically beneficial than those of the Marshall Plan.

East/West Issues

7. Mr Meese hoped that East/West trade issues would not dominate the Williamsburg Summit. The Chancellor and Mr Littler agreed, though drawing attention to our concern about the Export Administration Act.

8. Mr Meese said that European concerns were well understood in Washington, and had been taken into account in recent proposed amendments. The intention was that the Act should affect only key strategic items; and the right to restrict imports into the US would be used only in the very limited, and he hoped, infrequent circumstances in which the foreign company concerned was engaged in selling to the Soviet Union items whose export violated US national security. He had himself produced the language about national security, and had insisted on the limited use which was to be made of this particular provision.

9. The Chancellor said that Mr Meese, as a lawyer, would understand his own lawyer's concern about legislation which could be widely used, however limited the use its drafters had in mind. Moreover, the extraterritoriality inherent in the scope of the Act was profoundly unsatisfactory to us. The UK Government certainly did not wish to see Western military technology fall into Soviet /hands; but ~~all~~



hands; but Western governments were entitled to handle their own economic relations with the Soviet Union, as, for example, the US Government did with its grain sales. It should be possible to find through discussion a satisfactory accommodation with the US Administration on the Act: it would certainly be most unfortunate if there were to be a reprise of the 1982 "pipeline" crisis. But we remained profoundly unhappy with the Act in its present form.

North/South Issues

10. The Chancellor thought that the climate of relations between the industrialised and developing countries had somewhat improved. Certainly developing country representatives at the April Development Committee meeting had been surprisingly restrained. It was recognised that the Administration were working for congressional approval of the increase in the IMF quota, and the IDA VI appropriation. It was important that these go through. But developing countries could be best helped by a fall in interest rates.

Anti-Inflationary Policies

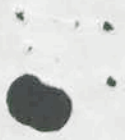
11. Mr Meese said that a main theme at Williamsburg should be re-commitment to the counter-inflationary strategy. The Chancellor agreed, pointing out that the history of past Summits illustrated the dangers of alternative strategies. The Germans still regretted their acceptance of the "locomotive" theory at the 1978 Bonn Summit. At Venice in 1980 Trudeau had argued for reflation, but by Ottawa 1981 he had reversed engines. At Ottawa it had been Mitterrand who argued for giving primacy to reducing employment; but by Versailles 1982 he had been converted by experience to the necessity of restraining budgetary deficits. The Summit Seven were now in broad agreement on economic strategy; but the key to the speed of world recovery lay in the level of US interest rates.

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6 May 1983

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Walter P. H. M.

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With the Compliments
of the
Chancellor of the Exchequer's
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