

PRIME MINISTER'S  
PERSONAL MESSAGE  
SERIAL No. ....



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10 DOWNING STREET

From the Private Secretary

25 February 1981

Dear Francis,

Telephone Conversation with Chancellor Schmidt

The Prime Minister rang Chancellor Schmidt last night to discuss her forthcoming visit to Washington.

The Prime Minister listed the main items on the agenda for her talks with President Reagan and asked Chancellor Schmidt whether he thought there were any subjects on which she should lay particular stress or on which she should be reticent. Chancellor Schmidt said that his main concern was with the international economic situation. In his view we were facing not a recession but a global depression on a much larger scale than that of 1975. He did not think the US Administration understood this. He had no recipe to advance but believed that "economic concertation" was now more important than ever. The world faced a dangerous situation which would not respond to a policy of benign neglect. The various Heads of Government would have to be active. Failing such consultation, there would be a temptation for individual countries to go it alone with the consequent risk of a relapse into protectionism. Against this background, it was very appropriate that the Prime Minister and the President were meeting now to exchange views.

The Prime Minister commented that one of the difficulties was that neither the United States nor the United Kingdom had exercised in recent years the financial discipline shown by the Federal Republic. Neither country was yet down to German levels of inflation. In getting it down it had been necessary, for instance, to maintain very high interest rates with all that this implied for exchange rates. Presumably Chancellor Schmidt would not advise either Government to ease up on inflation? Chancellor Schmidt confirmed that he would not do so but commented that nonetheless the present situation inhibited the capital investment now required.

Turning to President Brezhnev's recent speech, Chancellor Schmidt noted Secretary of State Haig's cautious reaction. He did not think it was appropriate for Heads of Government to get involved in detailed analysis of the speech. He thought that their reaction should rather be to take President Brezhnev at his word and to seek to negotiate an arms control agreement. What the

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Western world needed now was a strong statement, perhaps from the Prime Minister and President Reagan, urging negotiation with the objective of securing an "broad balance" between East and West. The Prime Minister said that the concept of balance was crucial. It suited President Brezhnev to have a moratorium at present since the Soviet Union had the lead in various areas. She was therefore wary of his proposals. Nonetheless she recognised the political point.

Chancellor Schmidt said that he hoped the necessary equilibrium could be maintained in the West's defence policy. The NATO double decision was of great importance. Chancellor Schmidt asked the Prime Minister to reassure President Reagan that the German Government would stick to that decision provided that everyone stuck to both halves of it. Willingness to negotiate was the essential concomitant of willingness to deploy. It was essential that the US Government should not give the impression that the negotiating part of the decision did not matter. If they were to give this impression, then the deployment of theatre nuclear forces in Germany would "not be swallowed". The essence of NATO defence policy had to be to secure a balance in the military field and then to stabilise it by negotiation. Failure to pursue a policy on these lines could deal a fatal blow to NATO. The Prime Minister indicated that she accepted Chancellor Schmidt's thesis.

The Chancellor enquired about the line the Prime Minister would take on the situation in Central America. The Prime Minister said that clearly the Americans wished to prevent further penetration by the Soviet Union and Cuba in Central and South America. She agreed with them. In pursuit of their objective, the Americans might have to supply arms to regimes that were unattractive to Western European Governments. But she understood their position and did not see any alternative. Chancellor Schmidt said that he accepted what the Prime Minister had said. However, it was important that in the effort to prevent Cuba taking over, the Americans should avoid becoming too closely linked with extremist right-wing regimes. He hoped that the new Administration would be able to distinguish between the Communists and the rest of the political spectrum. There was an underlying tendency in Washington to judge Caribbean and Central American issues in excessively black and white terms and to exclude intermediate points. He did not wish to be placed in a position where he had to choose between the extremes of left and right. The Prime Minister, while agreeing about the desirability of avoiding choice, said that she thought the Americans probably knew more than the Europeans about the problems in their own immediate vicinity. Chancellor Schmidt noted that the Administration probably still had a good deal to learn.

Chancellor Schmidt said that the only EEC issue which, he imagined, might come up in Washington was the question of trade relations with the United States and Japan. He thought it would be useful to get across the point that the United States should not try to solve its problems with Japan at the expense of Europe. The Prime Minister and the Chancellor agreed on the need to bring pressure to bear on the Japanese to open up their domestic market to their trading partners.

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/On the question

On the question of relations between the United States and the EEC, the Prime Minister said that there was no question in her mind of being either pro-American or anti-EEC or that a relationship with the one in some way excluded a relationship with the other. Everyone had to stick together both within the European Community and with the United States. This was our only hope. Chancellor Schmidt said that he had nothing to add to what the Prime Minister had said or to criticise in it.

On Community issues, the Prime Minister told Chancellor Schmidt that she thought the Community was facing a number of big decisions. It was essential that our approach should be to tackle the basics and to avoid tinkering. Chancellor Schmidt did not respond. But he did comment that the difficulties over fish were causing "very sour emotions" in the Federal Republic. He personally did not understand why, for the sake of 1500 tonnes of cod, HMG were preventing the Canadian Agreement going through.

The Prime Minister did not mention Mr. Franklin's recent mission to Paris. You may therefore wish to arrange for the Federal Government to be informed about this in some other way.

I am sending copies of this letter to John Wiggins (HM Treasury), Brian Norbury (Ministry of Defence), Kate Timms (Ministry of Agriculture, Fisheries and Food), Stuart Hampson (Department of Trade) and David Wright (Cabinet Office).

*Yours ever*

*Michael Alexander.*

Francis Richards, Esq.  
Foreign and Commonwealth Office.

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PRIME MINISTER'S

PERSONAL MESSAGE

SERIAL No. T 348/81

TELEPHONE CONVERSATION BETWEEN THE PRIME MINISTER AND CHANCELLOR SCHMIDT : TUESDAY 24 FEBRUARY 1981 AT 2020 HOURS

copy taken to America

SUBJECT

copy to ops + master

ka. [Signature]

Prime Minister Hello

Chancellor Schmidt Hello Margaret

PM Hello, how are you?

CS All right, thank you very much. How are you?

PM Oh I'm fine, but I have to be fine. There are so many problems that I have to keep fit to tackle them. Helmut, I was ringing because I am going to the United States tomorrow to see President Reagan and we'll be talking about the big international issues. I wondered if there was anything you would like to advise me on, to be either forthcoming or to be reticent. We will of course be talking about big things like the Middle East, about their attitude to Southern Africa, about their attitude to arms control and East/West relations generally, and particular to Brezhnev's speech. And also I think he will probably want to say to me something about their approach to El Salvador and Central and Southern America. I doubt whether they will have worked everything out yet but I was wondering, I really am seeking your views Helmut, on anything that I should say or that I should avoid.

CS Let me try to answer the points that you have mentioned so far Margaret. One of my main concerns right now is the impression that we are dealing with a world depression, much more than just a recession, that is much bigger than '75 and that the leaders of the free world and the biggest economy in the United States just do not understand what we have at hand. I have no recipe so far but my feeling is that never since the middle of the 70s has economic consultation been more important than just now. And my feeling is that we are in a dangerous situation. If any of us plays it cool and with benign neglect to the growing figures of unemployment and inflation at one time.

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PM Yes I have that.

CS I have no recipe, but I think that it is appropriate that leaders like you and Ronald Reagan should exchange preliminary thoughts on that. I have the feeling that in the next three months or so we have to become rather active in consultation, otherwise we will be tempted to go at it alone, each of us, and possibly lapse into protectionism of beggar my neighbour policy.

PM Yes. If I might say something, I think one of the problems is that neither the United States nor we have had over the years your measure of financial discipline and therefore we are not down to the levels of inflation which are common to you. We are trying to get down to them, you have already reached them. In the process of getting down to them we have very high interest rates, and that is aggravating the exchange rate problem.

CS And the high exchange rate is of course detrimental to capital expenditure and private investment.

PM Yes. I don't think you could advise us not to tackle inflation.

CS No, certainly not. But I am concerned, I am rather sorrowful, I must say. As regards arms control and East/West, I haven't seen the full text of Brezhnev's speech - I have seen a rather cautious public evaluation by Alexander Haig. Both Genscher and I have made some noises about it. I think one should not, as a head of Government or a head of State, one should not ..... into the details of that speech, but taken by his words where he says he wants to negotiate arms control, I think it is necessary that the United States of America makes it clear that this is just what they want to do. Another question is when, where and about what subjects but the Western world needs a very strong statement by Ronald Reagan and by you - a joint statement I think - saying we are for negotiations and arms control with the broad balance between East and West.

PM

PM Yes I think it is precisely that which is in issue - it is precisely the balance point that is in issue, because when you have a very powerful adversary, who has become very powerful on nuclear weapons, it suits him to have a moratorium now. And particularly when he is in Afghanistan. I am very wary, but I recognise the political point with which you have to deal, and we all have to deal - that we must respond but make certain that they actually come down on the amount of arms they have already.

CS I think the concept of equilibrium ... on military power are to be mentioned and underlined very strongly. Also as regards the so called <sup>bonfire</sup> ~~Dublin~~ decision of NATO of December '79, please tell Ronald Reagan that he can rely on the German Government despite ..... I would stick to that decision and make it stick. But please in order to make it stick I have to be sure that the United States and the rest of our allies .. would stick to the words of that decision. Number one to the deployment of such weapons in Europe and number two to the invitation and the will of the West towards the Soviet Union to negotiate mutual balance - ceilings - or whatever you call them. Both are necessary and the Americans must not give the impression to the European public, neither to the Dutch, nor the Belgians, nor the Germans, nor the Italians that the second half of the decision does not really matter and ~~just~~ what matters is <sup>just</sup> the first half. This would make it very, very difficult to get this 'swallowed' domestically. I almost predict that it will not be swallowed in this country, as it will not be swallowed in Belgium or in Holland. It is a very important thing. I have just called, in front of my Parliamentary Group, I have called it the typical element of NATO's grand strategy as a whole - on the one hand to make for equilibrium in military means, that is the first half of that decision, and secondly to try to stick, to <sup>stabilize</sup> ~~civilize~~ it, by negotiation and if we fail to realise that decision I think NATO will suffer a major blow from which it might not easily recover.

PM I got the point Helmut, and certainly I understand in particular your problem - this is all our problem - we all have to get these two things, the balance and the agreement to stabilize the balance. But is there anything particular apart from Ronald Reagan, with

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the Community, because I saw an account of what you and Oliver Wright talked about and I am very concerned that we have some very big decisions ahead of us in the Community on fish and agricultural prices and on the budget and we really must make some fundamental decisions and not just resort to tinkering with the problem.

CS I think these subjects including agriculture prices do not now raise major questions between the EEC and the United States of America. I think that they are more subjects to be dealt with among ourselves, especially fish which is a subject of very sour emotions in Germany and perhaps I might take the opportunity to tell you that I don't understand why <sup>for</sup> 1500 tonnes of cod fish you cannot allow the Canadian agreement to become valid, but all the other points which you mentioned including fish - I do not see any necessity to mention them viz a viz Reagan. Earlier on you mentioned El Salvador and I would be very much interested in hearing Margaret your judgement on Salvador and Nicaragua.

PM I think that the views that our American friends take is that they do not want any further penetration of either Soviet forces or Cuban forces in Central America or Southern America. Neither would I and they would take the appropriate steps to prevent that happening and that is the view that we must keep in mind because it might mean that they supply arms or assistance to regimes that you and I would not necessarily like, but in politics the question is what is the alternative. And if the alternative is Cuban or Soviet influence in Central or Southern America, then I would in fact expect our American friends to react to try to prevent that and I could understand that.

CS I have listened carefully to Mr. <sup>a</sup>Egelburger and as far as I can see these talks went rather well at least in Bonn, and there is one point I would like to add. While fully accepting Margaret what you have just stated, I would like to add that in order to prevent Communist overtaking and Soviet influences it is not necessary and not really desirable to link oneself up with extremist reactionary forces on the right wing of military governments because this in the long run is a provocation for the Communists and would serve

as a provocation for uprisings from the left. In other words I hope our American friends are able to distinguish between Communists on the one hand and the rest of the political spectrum which in itself in most of these countries is a different grain and shape. At least this seems to be true in Salvador and it may be true in Nicaragua. I think there is an underlying tendency in some Americans to judge Central American and Caribbean problems just by 2 different yardsticks. Either somebody is white or black and there's nothing in between. And there is a little danger that they are excluding possibilities and possible developments in between. I don't really wish to be put in positions to choose between communists and military dictators.

PM The view that I take is that just as you know your problems, living fairly close to the Warsaw Pact border, so I think Reagan probably knows his problems with the communists in Central America fairly close to him, and I would expect that the view that he would take would be that he does not want either the Soviets or the Cubans to make a great advance in Central America.

CS I fully agree. I doubt whether they have a clear picture of the situation because they are rather new in office. But they may get a better picture from week to week. I wouldn't have made my remarks if you hadn't mentioned Salvador.

PM I think it's going to be raised with me.

CS Let me come back to EEC. There might perhaps - one point has come to my mind Margaret - one point as regards the trade relations between the United States and Japan in connection with the trade relations between the EEC and Japan. There's a certain danger I am told that the people in the United States would like to solve their Japanese import problem at the expense of the European Community. I don't know how much of this is true, but I'm told there's a certain danger. Perhaps you're going to talk about Japan. I wanted to talk about this line with you.

PM Yes. I know you keep/<sup>a</sup>very open trading system. But you have problems with/<sup>our</sup>Japanese friends and so do we. But they are being now monitored by the Commission for 3 months. I think the problem that  
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many of us have is that those who preserve an open trading system do not necessarily meet with the same openness from other countries.

CS The Japanese ought to be put under pressure for opening up the country.

PM Right. Otherwise the burden on those of us who try to preserve and open trading system is intolerable, and we get the unemployment.

CS I do agree.

PM I don't want there to be any question that being pro-American means being anti-EEC. I want to say that I think that we all have to stick together both within Europe and between Europe and the United States. And I think that is our only hope. And so to me there is no difference between the two.

CS I understand you. I have nothing to add or to criticise.

PM Good. We are trying to do our best to try to get an agreement on fisheries and on agricultural prices, and we'll return to that when we meet in March.

CS When do you come back from America?

PM I'm back on Sunday and will let you know what happened.

General chat and farewells.