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RECORD OF A DISCUSSION BETWEEN THE PRIME MINISTER AND THE CHANCELLOR
OF THE FEDERAL REPUBLIC OF GERMANY, HERR HELMUT SCHMIDT, AT CHEQUERS
ON MONDAY 11 MAY 1981 AT 1800 HOURS

~~SUBJECT~~

Present

The Prime Minister	Herr Helmut Schmidt
Foreign and Commonwealth Secretary	Herr Genscher
Chancellor of the Exchequer	Graf Lambsdorff
Secretary of State for Industry	Herr Ertl
Minister of Agriculture, Fisheries and Food	Herr Schulmann
Secretary of State for Trade	Herr Kurt Becker
Sir Robert Armstrong	Herr Hans-Jürgen Rohr
Sir Michael Palliser	Herr Jürgen Ruhfus
Sir Brian Hayes	Herr Herrmann Heick
Sir Jock Taylor	Herr Per Fischer
Mr. Julian Bullard	Herr Franz Pfeffer
Mr. Michael Franklin	Herr Otto von der Gablentz
Lord Bridges	Herr von Alten
Mr. Gordon Manzie	Herr Gero Mocklinghoff
Mr. Robin Gray	Herr Klaus Zeller
Mr. Clive Whitmore	Herr Waldemar Müller-Thuns
Mr. Bernard Ingham	Herr Merkel
Mr. D.J.S. Hancock	Herr Reinhold Frickhinger
Mr. Michael Alexander	Herr Wilfred Heck
Mr. George Walden	Herr Reinhold Schenk
Mr. David Gladstone	Herr Walter Rode
	Herr Karl Paschke
	Herr Kiewitt

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Summing up her discussions with Chancellor Schmidt, the Prime Minister said that their talks had been dominated by the outcome of the French Presidential election. They had noted that the next European Council seemed likely to fall the day after the second ballot of the French Legislative elections, which would make it very difficult for Heads of Government to take decisions.

On CAP reform and budget restructuring, the Prime Minister said that they had agreed that M. Thorn should stick to the

/ timetable

timetable for submitting proposals for reform. The British and German Government positions were very much the same: we must stick to the 1 per cent VAT ceiling and find methods to reduce surpluses. Co-responsibility levies, which amounted to another way of raising finance, could frustrate our joint aim of holding to the 1 per cent ceiling. National aids should not be allowed to encourage surplus production. They had agreed on the importance of finding a solution to the problem of steel. On trade with Japan, they had agreed that there must be discussion at the next Heads of Government meeting.

The Prime Minister said that on defence, she and the Chancellor had noted the problem posed by collaborative ventures, especially if there were no agreement on whom the products could be sold to. They had compared notes on their visits to Saudi Arabia and her own visits to the Gulf and India. On Arab/Israel they had agreed that the Camp David process would continue to the point where the remainder of Sinai had been handed back to Egypt. There would probably be further activity by the US before that time, but no major new European initiative. The implementation of the Venice Declaration would continue. On East/West relations, they had noted that Herr Schmidt would be seeing President Reagan shortly and that the latter had sent a hand-written message to Mr. Brezhnev. They had endorsed the NATO communique with special reference to the passage on TNF negotiations.

The Foreign and Commonwealth Secretary said that he and Herr Genscher had agreed that the NATO meeting, which the Europeans had approached with some trepidation, had turned out very satisfactorily, both for the US and for Europe. They could only speculate about the foreign policies of the new French government, which would depend partly on the personality of the new Foreign Minister. He and Herr Genscher were agreed on the following likely consequences of the election outcome: East/West relations would be little changed; the essentials of French defence policy would not change (especially on the nuclear side); in the third world France might wish to adjust her policy towards, e.g.

/ black Africa

black Africa and Central America. This could have some impact on the policies of the West as a whole: it was, for example, not certain that France would again join the US and the UK in vetoing resolutions on South Africa. The new French Government might also give higher priority to her relations with Israel as opposed to those with Arab governments. As to the Community, a decision on restructuring, which was badly needed by the end of the year, would now be harder to reach. Every effort must be made to press ahead after the French Legislative elections.

Turning to the third world, the Foreign and Commonwealth Secretary said that there was an obvious danger of conflict between Israel and Syria if Israel "took out" the Syrian Surface to Air Missiles in the Lebanon. Both sides would probably seek to avoid conflict, though Mr. Begin might go too far. Only the US had the influence to affect Israeli decision-making substantially. Asked by Herr Schmidt about the future of Namibia, the Foreign and Commonwealth Secretary drew attention to the South African Foreign Minister's visit to the US the following week. It was not clear whether South Africa seriously wanted a settlement. He hoped that the Washington meeting at the end of the month would be able to devise constitutional safeguards which would secure the support of the internal parties while being acceptable to the Front Line States. Herr Schmidt said that President Eanes on a recent private visit had warned strongly of the need to abstain from "fiddling around" with UNITA. Eanes thought this would be disastrous.

Asked to report on his discussions with Herr Schulmann, the Chancellor of the Exchequer said that the UK and FRG shared interests as the joint paymasters of the Community. They were at one on the importance of the 1 per cent VAT ceiling and reform of the CAP. On the latter, they stressed the need for a prudent price policy leading to a reduction of surpluses and supplemented by the right kind of co-responsibility measures. Changes would be needed in intervention techniques to reduce the cost to the Community. It was necessary to hold the rate of increase in

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guarantee expenditure markedly below the rate of increase in own resources. Structural fund expenditure should be expanded within the 1 per cent ceiling and concentrated on the areas of greatest need. The administrative costs of Community institutions should be held down. To the extent that CAP reform and other policies did not succeed in preventing the development of unacceptable situations (in response to an intervention by Herr Schmidt, the Chancellor of the Exchequer explained that this meant Britain and Germany having to pay too much), it would be necessary for the Community to take conscious decisions on the shape of the budget and devise mechanisms to prevent such situations arising. There would be further exchanges of views with the German Government on possible mechanisms.

Herr Schmidt asked whether the British Government were contemplating unilateral action to achieve their ends. The Chancellor of the Exchequer said that decisions would have to be taken by the Ten. The Prime Minister commented that Herr Schmidt and M. Giscard had spoken earlier of the possible need to set a limit on payments to and benefits from the Community budget. This would not be easy to achieve. Herr Schmidt recalled that at Maastricht he had said he would propose a limit on the FRG contribution. The Chancellor of the Exchequer said that this would require a mechanism. The Commission must put forward options for consideration at the next European Council. The British Government would then make their position clear so that others could not evade the issue. The Prime Minister asked whether the timing of the European Council might be affected by the French Legislative elections. Herr Schmidt agreed that it might be difficult for President Mitterrand to attend a Council the day after the second ballot. However, any proposal for a postponement must come from the French Government. Taking up the Chancellor of the Exchequer's point, Herr Schmidt said that the mandate given to M. Thorn required him to put proposals to the European Council: we should not make it too easy for him by allowing him simply to put forward a large number of options. The Chancellor of the Exchequer said that the Council should have before it clear proposals of the kind they had discussed.

Reporting on his discussion with the Secretary of State for Industry, Graf Lambsdorff said they had concentrated on three issues: steel, textiles and trade with Japan. On steel, they expected that the Council of Ministers on 25 May would be able to confirm the voluntary producers agreement. This covered 95 per cent of the market; what was needed was an interim solution on the basis of Article 95 to cover the German firm Klöckner. As a last resort, this firm could be forced into the system by applying quotas under Article 58 to the product they made - hot rolled coil. This arrangement could be policed by the Commission. There would be a difficulty if the position of France changed following the election: this could affect the timetable for phasing out subsidies. It was very important to reach a result on 25 May, otherwise the third quarter of 1981 could be chaotic: steel producers faced great losses. The British and German governments agreed that subsidies must end; he himself now accepted that restructuring in the UK had come later than in the FRG. He understood that Sir Keith Joseph had told BSC that there would be no further subsidies and that the UK would henceforward follow the new aids decision.

Herr Schmidt asked whether this meant that Ministers had found a way of including Klöckner in the proposed arrangements such as would be acceptable to the Commission and valid before the Court. If so, it was good news. What would be said in public? Graf Lambsdorff said that the arrangement must remain confidential pending final scrutiny by the Legal Advisers. But everyone agreed that it was feasible. He explained that Article 58 could be applied to one product but not to a single company. The problem was that one producer of the magnitude of Klöckner could wreck the whole system if it remained outside. Herr Schmidt said he found interesting the spectacle of a neo-liberal forcing a private company into a cartel.

On trade with Japan, Graf Lambsdorff criticised the 'voluntary' US/Japan agreement on cars. The Europeans would have to live with this agreement but an agreed line must be prepared in the Article

113 Committee for Sir R. Denman's use in Tokyo. This should cover four main issues:

- a) the Japanese argument that protection for the US motor industry was justified since that industry, unlike its European equivalent, was restructuring itself;
- b) the European expectation that there would be no diversion to Europe of cars which would now not be sold in the US market;
- c) the European insistence that there should in any case be no increase in 1981 imports over the 1980 figures (while avoiding putting precise figures to the Japanese since the differing practices of member states needed to be disguised);
- d) the necessity for Japan to open their market and change their import structure (at present finished goods accounted for only 30-40 per cent of imports).

The Secretary of State for Trade concurred: he hoped that the Japanese could be persuaded to restrict the volume of motor exports without detailed figures having to be discussed. Graf Lambsdorff suggested that Foreign Ministries could help by taking parallel action through the Ambassadors of the Ten in Tokyo after the decision of the Council.

On textiles, Graf Lambsdorff said there was agreement that the multifibre agreement must be prolonged. In an ideal world he would prefer to have no such agreement, but he accepted that it was a practical necessity. The difficulty would be obtaining the signatures of the developing countries for a new agreement given that the existing bilateral agreements did not expire until December 1982. The FRG believed that Singapore, the Philippines, South Korea and Hong Kong should receive less favourable treatment than India, Sri Lanka and others but had noted the UK arguments that Hong Kong was an open market and deserved special consideration. As to duration of a new agreement, the FRG thought that three years was long enough but

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would compromise on five. The Secretary of State for Trade noted the difference of emphasis between the British and German Governments on this issue. The UK Government tended to take a more restrictive view but he thought agreement could be reached that the new agreement should not run for more than five years; and that a distinction should be drawn between the poorest developing countries and the others. Hong Kong should not be penalised.

Graf Lambsdorff said that the British position on outward processing was not acceptable. There was also still disagreement over origin marking. The German Government had asked the Commission to review the question under Article 30 of the Treaty since they regarded a requirement for marks of origin as equivalent to an import restriction with a similar effect as quotas. The Secretary of State for Industry said that as regards telecommunications, the British Government were removing the monopoly on telephones. British exporters were facing difficulties in the German market and he had agreed with Graf Lambsdorff to provide the latter with details.

Asked to report on his discussions with Herr Ertl, the Minister of Agriculture said that it was proving difficult to tackle the problem of surplusses since all ten members of the Community had different views. The British proposal for a superlevy was unacceptable to the FRG whose milk producers were less efficient. The UK for its part was a net importer and did not wish to reduce production. Any mechanism would thus affect the two countries quite differently. The UK objected to co-responsibility levies because they passed the extra cost on to the consumer. British and German views on cereals also differed. The British side thought it important to take a long term view of acceptable production levels but Herr Ertl had pointed out that attempts to tackle the problem had always failed in the past. The problem would, however, get worse when there were ten beneficiaries from the system instead of eight as at present.

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Turning to fish, the Minister of Agriculture said that it was agreed that the outcome of the French elections would make it impossible to reach a solution in June. In the light of M. Mitterrand's pre-election comments it seemed likely that any solution acceptable to the UK would not be acceptable to France. The British and German Governments both deeply wanted a settlement and would remain in close contact with a view to bringing influence to bear on France.

On enlargement, Herr Ertl commented that every new member cost the Community money. The Prime Minister said this had not been true of the UK. Herr Ertl said that Greece, Spain and Portugal wanted to improve and increase their farm production with Community finance. The Prime Minister said that Ministers of Agriculture were good at analysing the problems of the CAP. But when was Herr Ertl, with so many years of experience, going to produce solutions? Herr Ertl said that depended on the Ten and not on the FRG alone.

Summing up, the Prime Minister said it would be impossible to sort out all these problems in the next six months. A period of uncertainty in the Community was now inevitable. We must seek to make the best of it and if possible turn it to mutual advantage. There were no undue differences between the British and German positions and contact would be maintained. It had been a very useful day's work.

The meeting ended at 1900 hours.

And

13 May 1981

Schmidt
Genscher
Lambsdorff
Ertl
Schulmann
Becker
Hans-Jurgen Rohr
Rhufus
Heick
Fischer
Pfeffer
von der Gablentz
von Alten
Mocklinghoff
Zeller
Muller-Thuns
Merkel
Frickhinger
Heck
Schenk
Rode
Paschke
Kiewitt