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Treasury Chambers, Parliament Street, SW1P 3AG
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25 November 1981

M. O'D B. Alexander, Esq.,
Private Secretary,
10, Downing Street

Dear Michael,

EUROPEAN COUNCIL: ECONOMIC AND SOCIAL SITUATION

Earlier this week the Prime Minister and the Chancellor of the Exchequer discussed the handling of this item on the European Council agenda in relation to the draft conclusions on Chapter I of the Mandate and the Commission paper which is attached as an Addendum to Brief No.6. They agreed that the Commission paper provided an opportunity to strengthen the references in the Mandate conclusions to the need for strong economic disciplines.

*m. hardly
brief folder* I attach a brief which suggests how the Prime Minister might handle the discussion of this item so as to lead up to an amendment to the opening paragraph of the conclusions on Chapter I of the Mandate.

Copies of this letter and enclosure go to Brian Fall (FCO), Richard Dykes (Department of Employment), and to Sir Robert Armstrong and Michael Franklin (Cabinet Office).

Yours sincerely,

Jim Rutter

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EUROPEAN COUNCIL

ECONOMIC AND SOCIAL SITUATION

Handling Brief

Objective

1. To secure endorsement by the European Council of the helpful reference to the need for tight fiscal and monetary policies and competitive labour costs on page 6 of the Commission document on this subject (text attached to EHG(L) (81)6 Addendum).

Opening Statement

2. Commission have circulated a helpful survey of economic developments since the last European Council in June. On the last page of their document they have suggested some guidelines which the Community might set itself. This is a helpful document. Invite Commission (either Thorn or Ortoli) to introduce it.

Handling

3. Probable that, following Commission introduction, a number of Heads of Government will wish to intervene. Important to ensure that Schmidt contributes to the debate - not necessarily at the outset but preferably after anyone who wishes to advocate reflation has spoken.

UK Point to make

4. Very much agree with the point that the Commission make in their first guideline. Determined policies to bring public deficits under control and to keep monetary policy within limits and to control wage costs are necessary to provide the conditions for sustainable growth and the reduction of unemployment. European Council has a role to play in convincing public opinion of the positive contribution that such policies can make to the achievement of the goals that all share, namely lower inflation and less unemployment.

5. More detailed UK points to make are in brief EHG(L)(81)6, if required.

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Summing-up

6. We have identified an important feature of our policies which is not perhaps brought out as fully as it might be in the draft conclusions on Chapter I of the Mandate that we considered yesterday. I think that it would reflect our discussion under this item of the agenda if we added the following sentence after the first sentence of the draft paragraph on overall Community economic strategy:-

"Such a strategy requires for its success a strict control of public deficits, sound monetary policies and competitive labour costs."

This sentence is a summary of what the Commission say in their first guideline. Can we agree to record the conclusions of our discussion in that way?

[The relevant paragraph of the draft Mandate conclusions, with the new sentence inserted and underlined, is attached as an annex.]

7. [If Mitterrand resists this insertion] The sentence I have suggested is very close to what we agreed at Ottawa. For example:-

"We need in most countries urgently to reduce public borrowing" (paragraph 5 of the Ottawa communique)

"We see low and stable monetary growth as essential to reducing inflation" (paragraph 6 of Ottawa communique).

8. [If Mitterrand tries to exploit the references to falling interest rates in the Commission guidelines on page 6 of their document] I suggest we invite the Finance Council to consider Community interest rate policies at their December meeting. It is a topic to which I know they have been giving attention at successive meetings.

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Paragraph 1 of the draft conclusions on Chapter 1 of the Mandate if revised as suggested in the brief.

1. The European Council agreed that an overall economic strategy in the Community is essential to combat unemployment and inflation and to encourage convergence. Such a strategy requires for its success a strict control of public deficits, sound monetary policies and competitive labour costs. Priority should be given to encouraging productive investment and raising competitiveness as a basis for creating durable jobs, bringing about sustainable economic growth and reducing unemployment. At the same time the Community should pursue the reduction of its dependence on external sources of energy, in particular oil.

I. DEVELOPMENT OF COMMUNITY POLICIES (OTHER THAN THE CAP)

Overall Community economic strategy

(to be completed, as necessary, after the European Council's discussion of the economic and social situation)

1. The European Council agreed that an overall economic strategy in the Community is essential to combat unemployment and inflation and to encourage convergence. Priority should be given to encouraging productive investment and raising competitiveness as a basis for creating durable jobs, bringing about sustainable economic growth and reducing unemployment. At the same time the Community should pursue the reduction of its dependence on external sources of energy, in particular oil.
2. In addition to measures taken at a world-wide level in pursuit of these common objectives, the European Council underlined the contribution that Community policies can make especially in all the areas set out below.
 - A. Employment policy
3. The European Council agreed that as a complement to macro-economic policy decisions effective action in the social field to alleviate unemployment should be taken at both the Community and the national level.
4. At the Community level full use should be made of all appropriate Community instruments and policies, as set out in succeeding sections of these conclusions.
5. It agreed that the Council (Social Affairs) should review as a matter of urgency the various existing means of consulting the social partners with a view to making them a more effective channel for a genuine dialogue. (See also paragraphs 18 and 19.)

F. Economic policy

6. The European Council agreed that the achievement of the Community's overall objectives would require stronger economic disciplines and concertation. The Community should ensure, through a careful comparison of national policies, that the main economic and sectoral objectives of the Member States are consistent with the maintenance and strengthening of the Community as well as with the object of consolidating the EMS. It therefore called for a more effective coordination of national economic policies and invited the Commission and the Council (ECOFIN) to make fuller use of the machinery set up for that purpose and to consider whether it needed strengthening.

C. Monetary policy

7. The European Council welcomed the success of the EMS in creating a zone of currency stability in Europe. It agreed that it should be further developed both as a key element in progress towards economic and monetary union and the creation of a European Monetary Fund, and to encourage a more stable international economic environment. It invited the Council (ECOFIN) to take stock during 1982 of the preparatory work done on these matters and in particular to take the necessary steps:

- to achieve greater concertation of national monetary policies;
- to encourage the use of the ECU for Community loans and on financial markets by both public and private borrowers;
- to seek improvements in monetary co-operation with the Community's principal partners, in particular insofar as exchange rate and interest rate policies were concerned.

D. Borrowing and Lending policy

8. The European Council welcomed the moves recently made to expand the scope of the Community's financial instruments, (EIB, ECSC, EURATOM and the NCI) in order to promote investment

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