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PRIME MINISTER

MEETINGS IN WASHINGTON

The discussions I attended in Washington last week were on the whole successful, and produced some pointers for Williamsburg.

Development Committee

2. The joint IMF/IBRD Development Committee meeting, primarily on North/South and Aid issues, was fairly low key, reflecting the tone of recent statements from meetings of developing countries in New Delhi and Buenos Aires. Developing countries have not moderated their demands, but they do seem to be advancing them less stridently than in the past.

3. The key issue was, of course, whether the US will honour its financial commitment to IDA. This depends on Congress, and the meeting recognised that the Administration (Shultz and Regan) have now started to pitch in on the Hill. But delivering the IDA VI appropriation may require pressure from the President, and it might well be right to raise this with him at Williamsburg.

G.7 Meeting

4. Finance Ministers and Central Bank Governors of Summit countries plus the Commission met to approve publication of the "Jurgensen Report" on exchange rate intervention, and contrived to avoid a Franco-American row. The agreed covering statement is constructive and should, I think, be welcomed at Williamsburg. It accepts that intervention can have a legitimate, though modest, role, but recognises the importance of trying to achieve greater exchange rate stability through better-matched policies, and contains the statement: "In the formulation of our domestic economic and financial policies, our countries should have regard to the behaviour of our exchange rates, as one possible indication of need for policy adjustment."



5. This goes further than the Americans have previously, and it is valuable to have their acceptance of it. But what is needed now, if this step towards agreement is to have the desired effect on business confidence around the world, is stronger evidence that they accept some of its implications.

G.5 Meeting

6. The main G.5 business, for which the IMF Managing Director was present, was "surveillance" of progress in our several economies. Larosiere did an excellent job of analysis and criticism, and attention quickly focussed on the United States position: very high real interest rates (unless one assumes an early move back to much higher inflation), closely associated - in the view of all but the Americans - with the high \$ exchange rate against the yen and deutschemark, which is one cause of poor US international trade performance and resulting pressures for protectionism, the whole deriving from an excessive public sector deficit imposing too heavy a burden on interest rates to maintain discipline over monetary growth. One other disturbing consequence of the high deficit is the fact that the US - the richest country in the world - is now a substantial importer of capital.

7. The US reaction was unimpressive. Don Regan tried to deny the causal relationship between high interest rates, a strong dollar and high deficits. He did acknowledge that the deficit must be reduced: but he spoke without conviction about how this might be done, and was inclined to blame Congress.

8. I am convinced that it would be valuable if you would tackle the President about the deficit - on the lines of your previous talks with Shultz and Volcker. The right time to do it would be in Washington on 27 May, rather than more publicly at Williamsburg. As Feldstein suggested to me the other day, the key may be to point out to the President the gains - economic and political - which have accrued to us from our demonstration, in the 1981 Budget, of our commitment to reduced borrowing. We might have a word about this.

Trade

9. The US took the opportunity in the G.5 meetings to urge again the importance of resisting and reducing protectionism. This will be discussed further at the OECD Ministerial meeting in Paris next week.

10. I also took the opportunity of pointing out to Don Regan the damage which could be done to relations in the Western Alliance by the measures proposed in the draft Export Administration Act. Subsequently, in the G.5 meeting, Regan mentioned this legislation, said that there was some possibility of fairly rapid passage through Congress, and suggested that countries which disliked it should "speak loudly in the Paris meetings next week." I am sure that we should take the hint.

Williamsburg

11. The key pointers for Williamsburg perhaps are:-

- i. general agreement that the recovery is in train. This is tempered with caution, and insistence that the objective must remain sustainable, and therefore non-inflationary, growth, not "concerted deflation."
- ii. on debt, agreement that, while we can take credit for speedy and effective action already taken, there remains a need for continuous monitoring, on a case-by-case basis, with financial help available conditional on appropriate adjustment policies. (Incidentally, US representatives hoped that the GAB and IMF Quota increases might be approved by Congress just before Williamsburg.);
- iii. agreement that the slightly more moderate tone of recent ldc meetings (contrasting with earlier years) deserves a sympathetic response, eg. at UNCTAD; that IDA and IBRD must not be starved of resources; but also that the best way to help the developing countries is for industrial countries to promote sound and sustainable recovery;



iv. widespread concern that high interest rates could weaken or abort recovery, while a strong dollar feeds protectionist tendencies. The prospect of future US public sector deficits equalling or exceeding total US private sector savings is one that causes universal concern, but has as yet produced no convincing counter-action from the Administration. It would be wrong to envisage public criticism of the President at Williamsburg - as the French may -but equally wrong to imagine that the subject of the deficit will not be discussed there. The best way of helping to defuse the issue might, as I say, be for you to take it up with him in advance.

12. I am copying this minute to the Foreign Secretary, the Secretary of State for Trade and Sir Robert Armstrong.

(G.H.)

4 May 1983