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17th September 1980

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*Dear Michael,*

ANGLO-FRENCH SUMMIT: PRIME MINISTER'S MEETING WITH M. BARRE

In his letter to you of 11 September, Stephen Gomersall reported that M. Barre would, among other things, want to talk about the handling of national economic problems in the current international situation. Given the similarities between the domestic economic policies of the two Governments, this should provide a good opportunity to establish some common ground.

.... Attached is a note we have prepared bringing out these similarities. The Prime Minister might like to draw upon it in her talk with M. Barre.

I am copying this letter to Paul Lever and Stephen Gomersall at the FCO.

*Yours ever*

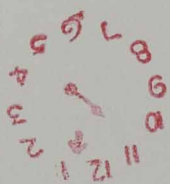
*John Wiggins*

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COPIES OF THE REPORT  
The current financial situation of the State is  
of concern to all citizens and it is the duty of  
the Government to provide a full and frank  
account of the position. The following report  
sets out the main features of the current  
situation and the measures being taken to  
bring about a more balanced and sustainable  
financial position.



18 SEP 1980

ANGLO-FRENCH SUMMIT

PRIME MINISTER'S MEETING WITH M. BARRE

Introduction

1. There are many similarities between the economic policies of the French and British governments. Though M. Barre no longer combines the Finance portfolio with that of Prime Minister, he is still considered to be the central figure in French economic policy-making. The meeting with M. Barre provides an excellent opportunity to stress what the two countries have in common to set against differences on Europe, North/South questions etc.

Points to make

2. Although the French government has not set out a medium term framework like the Medium Term Financial Strategy, policy has shown remarkable constancy over more than 4 years, despite the intervention of one election and the approach of another. Policy has been deliberately gradualist.
3. Despite rising unemployment, now over 6%, the containment and reduction of inflation remains the first priority. M. Barre has consistently rejected short-term palliatives; unemployment can only be reduced and kept down in a healthy economy.
4. The main features of economic policy, many of which find direct parallels in the UK, have been:
- (a) Tight control of the money supply, achieved through the setting of monetary targets.
  - (b) Recognition that fiscal policy must be consistent with monetary targets. This has required small public sector deficits and tight control over public expenditure.
  - (c) Belief in the value of a strong exchange rate.
- M. Barre recently stated "It is not a question of adapting the franc to the needs of business, but one of business adapting its requirements to the needs of the franc".

(d) Advocacy of wage restraint without recourse to formal incomes policies. Recognition of the need for government to give a lead with public sector pay.

(e) Promotion of a greater role for market forces eg removal of price controls and opening up of capital markets.

(f) Acceptance of the need for structural change in declining industries eg steel and textiles.

(g) Need to restore the profitability of industry.

5. There are a number of important differences:

(a) The main instrument of monetary control has been the "encadrement du credit" ie a system of ceilings on bank credit. There has been much less reliance on high interest rates. Can this be continued indefinitely without cumulative distortions?

(b) Credit flows are much more fragmented, with many of the channels being controlled by the government eg the medium term credit institutions like Credit National.

(c) France has to contend with a large current account deficit, estimated at \$7-10 billion this year. So far it has been financed without difficulty, partly by a large public sector borrowing overseas.

(d) Though there have been some relaxations, there is an extensive system of exchange controls.

(e) Unions are weak and divided.

#### Background

6. The French government has recently announced its budget for 1981. The deficit is set at F29 billion (1 per cent of GNP), slightly less than the expected outturn for this year. With the exception of defence and research and development, substantial cuts have been made in public expenditure plans. A five year programme