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RECORD OF A CONVERSATION BETWEEN THE PRIME MINISTER AND THE PRESIDENT OF THE COUNCIL OF MINISTERS OF ITALY, SIGNOR GIOVANNI SPADOLINI, AT 10 DOWNING STREET ON 9 NOVEMBER AT 1210 HOURS

Present

The Prime Minister
Mr. M.O'D.B. Alexander

Signor Spadolini
Signor Berlinguer

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The Italian Economy

After an exchange of courtesies, the Prime Minister asked Signor Spadolini about the economic situation in Italy. Signor Spadolini said that, as he had explained to the Prime Minister in Ottawa, his main task was the fight against inflation. He was close to agreement with the unions on wage levels. There had been many frustrations and disappointments but by the end of the year he hoped to have got the figure for inflation down to 16 per cent - as opposed to the 20 per cent which had obtained when he took office. The importance of this was that wages in Italy were indexed. A reduction in the level of inflation would therefore reduce claims in the next wage round. He hoped to get the claims down to an average increase of 14 or 15 per cent. He was also hoping to hold down the prices of gas and electricity and to change the country's fiscal structure so that workers would have more take-home pay. This meant reducing the public sector deficit, i.e. cutting expenditure.

The aim was to reduce current expenditure by 10 per cent (or 10,000 billion lira). The Prime Minister commented that most governments seemed to be experiencing similar problems for the same reasons. People had been led to expect more money than could be justified by their own output. Parliaments were not prepared to see expenditure cut severely enough to permit tax cuts. Would Parliament in Rome allow Signor Spadolini's programme through? Signor Spadolini said that there was no

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general pact but there was a measure of agreement on specific points and an understanding about the need to resist inflation. He was planning to make cuts in expenditure on health and welfare; prescription charges would be increased and expenditure on social security would be reduced by 2,500 billion lira. This would primarily be achieved by increasing individual contributions. There would also be a reduction in transfers from central government to local authorities. The Prime Minister said that it sounded as though a heavier burden would be placed on wage earners generally. Signor Spadolini said that his measures were designed to affect the self-employed rather than employees. None the less, noisy polemics would undoubtedly result, e.g., as a result of the increases in prescription charges. The trade unions were taking a different line in public from that which they took in private. However, the measures should be through by Christmas. If so, new ground would have been broken. It would be the first time there had been agreement on a planned inflation rate.

The Prime Minister and Signor Spadolini agreed that much would depend on the dollar rate. Some reduction in the value of the dollar was essential. The Prime Minister commented that the British economy had been hit by the higher dollar. It had fed through in the shape of increases in the price of oil. Fortunately US interest rates now seemed to be coming down. Signor Spadolini commented that President Reagan had been telling the truth in Ottawa. None the less, the cost of money remained very high in Italy, prohibitively so for some small firms. This in turn affected unemployment. Although the official figures for unemployment in Italy were under 10 per cent, this was misleading. There was a great deal of hidden unemployment in the country. The Prime Minister asked whether it was not the case that Italian exports were rising? Signor Spadolini said that this was the case in some sectors but by no means all. He described the overall export situation as "reasonable but not good". The Prime Minister said that Signor Spadolini's basic message appeared to be that the world economic prospects would improve if the American economy improved and provided no extraneous political crisis drove up the price of oil. Signor Spadolini

/ said that

said that this was exactly right. Against this background, the role of the European Community was important. A firm line-up in the Community helped the Italian Government. The Prime Minister asked whether he meant by this that the European Council should declare its intention to continue the fight against inflation? Signor Spadolini said this was indeed what he had meant.

European Council: 30 May Mandate

Signor Spadolini said that the European Council should try to reach agreement on all three aspects of the 30 May Mandate. The Prime Minister said that this was her intention. She agreed that all three aspects of the Mandate had to be treated together. But it was proving difficult to make progress, and still more to reach agreement, in advance of the meeting. There seemed to be a general desire to make progress on Chapter 1 measures. (Signor Spadolini agreed.) There was a desire to make progress on reform of the CAP but Member States' ideas on how to achieve this tended to conflict. In particular, those of France were distinctive. As regards the Budget, progress would have to be made. Clearly the Federal Republic did not intend to go on paying at the present rate. However, again, it would not be easy to reach agreement on restructuring. Signor Spadolini said that the psychological effect of a failure at the Council would be considerable. It was essential that the Council should give the "idea of Europe" a boost. He hoped that it would be possible to make progress with President Mitterrand when he visited Paris the following week. The wine war showed the difficulties which existed but the "principle of progress" had to be accepted.

The Prime Minister said that the resource costs of the CAP were very heavy for the United Kingdom. We had to buy a great deal within the Community which we could obtain more cheaply from outside. This was a problem, she thought, which the United Kingdom and Italy had in common. (Signor Spadolini indicated agreement.) France's present efforts to change the system in order to help the small producer at the expense of the more efficient were unlikely to be helpful. What would the Italian

Government like to achieve in regard to the CAP? Signor Berlinguer said that Italy would, in the first place, like to see the package of Mediterranean products which had been agreed three years earlier reaffirmed. Secondly, they wished to see adjustments made in the CAP so that those agricultural producers, e.g. of cereals and dairy products, who were not responsible for producing surpluses, would not be penalised. At present, Italy was being "punished" for the surpluses being produced by other countries. The Prime Minister commented that an approach on these lines would mean treating surpluses as a national, rather than as a Community, problem. Signor Berlinguer said that this was so. The Prime Minister said that she agreed with this approach. However, she wondered whether the French would agree.

Signor Spadolini said that as one of the measures under Chapter 1, he wished to see the Ortolli facility enlarged. It must be used for structural investment and not merely to relieve crises. Initially, the increase might be of the order of 1,000 mua. It was for Italy an "absolute necessity" that more investment should be channelled into the field of nuclear energy. Italy, with only three nuclear power plants, had fallen far behind other Community Members, such as France.

In the course of a brief discussion on the length of the draft conclusions being considered by officials (Signor Berlinguer referred to a draft of 55 pages), the Prime Minister said that she intended to cut it down very radically. She added that she had no intention of approving a communique referring to matters which had not been discussed by the Heads of Government.

Sinai

Signor Spadolini asked whether the Prime Minister thought the current difficulties over Sinai and the Sinai MFO could be resolved. The Prime Minister said that she was very distressed at the turn which events had taken. Our intention had been to assist the United States without alarming the moderate Arabs who would be dismayed if we departed from the Venice Declaration.

We owed it both to the Arabs and to the United States to produce a clear and distinctive statement on our position. She had been "amazed and sad" when Mr. Haig had told our Ambassador that our proposed statement would cause difficulties. The statement said nothing new. It did not criticise Camp David. It did not ask for American agreement. It merely reiterated our adherence to our own views. If the United States could not go along with our preferred procedure, we would have to make a statement in Parliament. There would have to be a statement in one form or another. Failing this, the Arabs would be disillusioned and ultimately difficulties would be caused for Egypt.

Looking further ahead, it seemed unlikely that there would be much progress until Sinai had been returned to Egypt. Once this had taken place, there might be room for new discussions and for modifications in the attitude of the United States. The possibilities opened up by Prince Fahd's eight points would also become important. But the next stages would not be easy. As regards the autonomy talks, for instance, there was no known constitutional arrangement whereby a people could be given autonomy without obtaining at the same time control of the land in which they were to exercise that autonomy.

Signor Spadolini said that he agreed with the Prime Minister that the public argument between Mr. Haig and Europe was regrettable and indeed dangerous at the present time. There was much instability in the Middle East. Colonel Qadhafi was unpredictable. The position of Egypt in the aftermath of President Sadat's death was uncertain. The establishment of the MFO might help President Mubarak. Signor Spadolini agreed that until Sinai was returned to Egypt, there was no chance of further progress. This made it even more important that Sinai should be given back on time. It was to be hoped that national statements, confirming the Venice Declaration, would prove sufficient. Only Arab extremists were objecting to the MFO. The Prime Minister commented that moderate Arab rulers understood the rationale of the MFO but it was less clear that this understanding extended to their peoples.

/The Prime Minister

The Prime Minister went on to comment on the increasing importance of the role of the Saudi Government. Prince Saud had elaborated on the seventh of Prince Fahd's eight points in a way which made it clear that the language was meant to include Israel. They were now clearly trying to persuade other moderate Arabs of the need to accept Israel's right to exist. It was therefore satisfactory that the Senate, in the end, let the AWACS deal go through. Failure to do so would have been an unacceptable humiliation for the Saudis. The Israeli reaction to the AWACS decision had been very unwise. Israel was in general over-reacting at present. This accounted for the line they were taking on the MFO and for their efforts to tie us into Camp David. It was necessary for the Ten to keep calm. Certainly HMG did not intend to react with angry words to what had been said in Washington. Signor Spadolini commented on the importance of giving the Americans, the Arabs and the Israelis, a sense of a European presence in the matter. The Prime Minister said that the enunciation of the eight points should make possible eventual Arab involvement in a comprehensive statement. The eight points could not be ignored. They had been initially welcomed by President Reagan. The President was undoubtedly anxious "to do the right thing" but the strength of the Israeli lobby in the United States would always give him problems.

Mrs. Gandhi

Signor Spadolini said that he had been able to greet Mrs. Gandhi on her arrival in Rome before his departure for London. The Prime Minister said that relations between the United Kingdom and India at present were very good. She liked Mrs. Gandhi and liked what she was doing in India. Signor Spadolini said that Mrs. Gandhi had told him that she had "won the battle for survival". By this he had assumed that she meant the battle to solve India's food problems. The Prime Minister commented that consideration of India's problems helped to put the problems of Europe in perspective.

/ Cancun

Cancun

Signor Spadolini asked about the Cancun Conference. The Prime Minister said it had gone very well. It had been wise not to arouse exaggerated hopes in advance of the meeting. Despite a certain amount of argument behind the scenes, agreement had been achieved to continue the global negotiations in a United Nations framework and to protect the position and independence of the major financial institutions. There had been some discussion of the energy affiliate. The Saudis had said the idea was worthy of further consideration and had appeared to mean this. More generally, the developing countries had shown a clear understanding of the importance to them of the defeat of inflation in and by the developed countries. All the participants had considered the meeting worth while. It would help to advance matters in the future.

The meeting ended at 1310.

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10 November 1981