

PRIME MINISTER

JOINING THE EMS

You asked about the letter, attached, in yesterday's FT, drawing attention particularly to the statement that the EEC accounts for only 39% of our manufactures compared to over 50% of larger imports.

The figures are correct. ("Larger" I take here to mean that our imports are larger than our exports!) Our deficit with the Community is of course reduced by a surplus on oil and invisibles. Our overall current account deficit with the Community in 1984 was £1.3 billion.

I am not entirely sure what the author is driving at, but taken with the final paragraph, he perhaps means that joining the EMS at the present exchange rate would lock in the present imbalance in manufactures.

If this is the argument, it fails both because there is no necessary reason why we should have a balance with the EC in our trade in manufactures (bearing in mind oil, invisibles etc.) and also no reason why we should be in balance with any particular area of the world. Bilateral trade positions, at least between us and the EC, in any case probably only have a small influence on bilateral exchange rates: confidence, investment flows etc. are much more important.

There is perhaps one point in favour of the letter writer, though rather low in importance. If a benefit of joining the EMS is exchange stability, importers of manufactures from the EC will gain more than exporters of manufactures to the EC in a crude sense, simply because there are more of them.

DN
(David Norgrove)

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(DCAAWO)

Joining the EMS

*From the Treasurer,
Labour Economic Policy Group*

Sir,—Why does Sir Terence Beckett rejoice (November 22) because Mr Samuel Brittan has now joined those who want us to charge over the cliff by joining the European Monetary System now or in the foreseeable future?

The evidence which the Confederation of British Industry gave to the Treasury Committee on this question was astonishing for its lack of perception. It did not realise that British industry was bound to suffer under a fixed exchange rate limited to the Ecu because importers would gain far more than exporters. The EEC accounts for only 39 per cent of our exports of manufactures compared to over 50 per cent of our larger imports. It then proceeded to blame its members for the mess we are in by attributing much of this to "non-price-competitiveness," not realising that there is no such thing as a free lunch in business and that as an explanation of what has happened since 1979 it could only stand up if the situation had actually got worse under the Government!

The truth it ignores is that all factors of production have to be paid for and that firms which are fighting for survival as a result of an increase in the real exchange rate cannot match the competition in every respect.

The reality the CBI must face is that in the absence of tariff protection against imports from the EEC the real exchange rate against the D-Mark has got to fall by 30 to 35 per cent to enable us to get back to full employment. The policies which the CBI favours were tried and failed in the 1920s. The policies we need are those of the 1930s—a competitive exchange rate backed by an accommodating money supply. We became the most instead of the least successful industrial country in the world. We could do the same again, particularly if we followed the advice of Lester Thurow in again putting an end to free trade with the Continent.

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