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DOCUMENT NO. AND TYPE	SUBJECT/TITLE	DATE	RESTRICTION
1. Memo	Henry Nau to William Clark, re: A Strategy for East-West Issues at the Summit, 9 p.	3/28/83	P1/F1
2. Cable	#312355Z Mar 83, 1 p. D 2/9/02 F99-0801, #156	3/31/83	P1/F1 , B3
~~3. Memo~~	~~Donald Regan to Reagan, re: Interest Rates in the Summit Countries, 1 p.~~ R 5/2/01 F99-0801, #157	~~3/31/83~~	~~P1/F1~~
~~4. Paper~~	~~"The Search for Discipline," 5 p.~~ R " " #158	~~n.d.~~	~~P1/F1~~
5. Cable	#010132Z Apr 83, 5 p.	4/1/83	P1/F1
6. Memo	Nau to Bailey, Dennis Blair, et al., re: [E-W Studies], 1 p.	4/4/83	P1/F1
7. Paper	COCOM High Level Meeting, 2 p.	n.d.	P1/F1
8. Paper	Export Credit Arrangement, 1 p.	n.d.	P1/F1
9. Paper	OECD Ministerial, 2 p.	n.d.	P1/F1
10. Paper	NATO Ministerial, 2 p.	n.d.	P1/F1
11. Paper	COCOM High Level Meeting, 3 p.	n.d.	P1/F1
12. Memo	Bailey to Nau, re: April 5 Summit Planning Meeting, 1 p.	4/5/83	P1/F1

RESTRICTION CODES

Presidential Records Act - [44 U.S.C. 2204(a)]
- P-1 National security classified information [(a)(1) of the PRA].
- P-2 Relating to appointment to Federal office [(a)(2) of the PRA].
- P-3 Release would violate a Federal statute [(a)(3) of the PRA].
- P-4 Release would disclose trade secrets or confidential commercial or financial information [(a)(4) of the PRA].
- P-5 Release would disclose confidential advice between the President and his advisors, or between such advisors [(a)(5) of the PRA].
- P-6 Release would constitute a clearly unwarranted invasion of personal privacy [(a)(6) of the PRA].
- C. Closed in accordance with restrictions contained in donor's deed of gift.

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- F-1 National security classified information [(b)(1) of the FOIA].
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- F-6 Release would constitute a clearly unwarranted invasion of personal privacy [(b)(6) of the FOIA].
- F-7 Release would disclose information compiled for law enforcement purposes [(b)(7) of the FOIA].
- F-8 Release would disclose information concerning the regulation of financial institutions [(b)(8) of the FOIA].
- F-9 Release would disclose geological or geophysical information concerning wells [(b)(9) of the FOIA].

NATIONAL SECURITY ~~COUNCIL~~

Bailey

3/28/83

Please note change
in time of our meeting
with Clark.

Nau

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Bailey

MEMORANDUM

NATIONAL SECURITY COUNCIL

ACTION

March 31, 1983

W Summit

MEMORANDUM FOR WILLIAM P. CLARK

FROM: HENRY NAU HN

SUBJECT: Give-and-Take Session with the President on Summit Issues -- Monday, April 4, 1983, 2:30 p.m., Oval Office

At Tab I is the memo from you to the President with background materials for the President's review before our give-and-take session on Monday, April 4, 2:30 p.m. in the Oval Office. It should be sent immediately to Darman (or whomever in California) for the President's reading on the flight back to Washington.

If you give this to the President personally, explain to him the value we place on his questions and reactions to these background materials. We are making an effort to explain these issues in the manner in which they are likely to be discussed at the level of heads of state or government. I drafted a more extensive cover note this time because the Treasury material did not incorporate clarifications which I gave them by phone. What we do not need in these materials is technical language or shortcuts that no one understands but the Treasury specialists.

If the President prefers to ask his questions in a one-on-one situation, we could also use the 9:30 briefing on Monday to see if he is comfortable with everything he has read in the background papers.

RECOMMENDATION

1. That you sign the memo to the President at Tab I and send it immediately to Darman (or whomever in California) for the President.

Approve _____ Disapprove _____

2. That you consider asking the President at the 9:30 a.m. briefing on Monday if he has understood all the points in the background papers.

Approve _____ Disapprove _____

Attachments
Tab I - Memo to the President
Tab A - Brief Analysis and Charts
Tab B - Background Paper

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SYSTEM II
90410

THE WHITE HOUSE

WASHINGTON

ACTION

March 31, 1983

MEMORANDUM FOR THE PRESIDENT

FROM: WILLIAM P. CLARK

SUBJECT: Give-and-Take Session on Summit Issues, Monday, April 4, 1983 - 2:30 p.m., Oval Office

Issue

This is the second of a series of give-and-take sessions on Summit issues. The first one dealt with economic policies and prospects of the other Summit countries. The second one deals with the search for discipline and compatibility among the domestic economic policies of the major industrialized (currency) countries. In many respects, this issue constitutes the core problem of the international economic and monetary system, whether that system is based on the gold standard, fixed or floating exchange rates.

Discussion

Don Regan has provided you with two background papers. At the last give-and-take session, you expressed an interest in the pattern of interest rate developments among the Summit countries since your Administration took office. Tab A provides a brief analysis and charts showing this pattern.

At Tab B is the background paper for your session on Monday, April 4. Several points should be highlighted:

-- The discussion of the international monetary system in historical perspective (pp. 1-2) makes clear that although the gold standard system exerted strong discipline over national economic policies, even this system failed when countries were unwilling to accept this discipline and maintain complementary economic policies aimed at low inflation and sustainable growth.

-- The loss of discipline in U.S. policy in the late 1960s was the root cause of the demise of the fixed exchange rate system established at Bretton Woods. All of this occurred before the first oil shock of fall 1973.

- -- The French have been the strongest advocates of going back to a fixed rate exchange system, yet ironically are one of the countries least willing to maintain disciplined domestic policies necessary to assure exchange rate stability.

- -- The multilateral surveillance initiative which we proposed and which was agreed to at the Versailles Summit has the great virtue of addressing the core problem of the international monetary system, namely discipline and complementarity among the domestic economic policies of the major industrialized countries (which are also the major currency countries) aimed at low inflation and sustainable growth.

- -- Strengthening this initiative at Williamsburg is timely because it will reinforce the success of anti-inflation policies just as the economic situation begins to improve -- precisely the point in the past when the emphasis on fighting inflation has been lost.

- -- If the Summit countries cannot make progress on this core problem of discipline and convergence of their economic policies toward low inflation and sustainable growth, other steps -- exchange market intervention, going back to fixed exchange rates or even restoring the gold standard -- cannot make any difference. The European Monetary System is a classic example of what happens when you try to achieve discipline through intervention or other secondary means without attacking the central problem of discipline and convergence of domestic policies around low inflation. The EMS has experienced seven realignments of exchange rates in four years, hardly a success for a so-called fixed exchange system.

RECOMMENDATION

That you read the papers at Tab A and B before our meeting on Monday and begin the meeting with your questions or observations.

Approve _____ Disapprove _____

THE SECRETARY OF THE TREASURY
WASHINGTON 20220

March 31, 1983

MEMORANDUM FOR THE PRESIDENT

Subject: Interest Rates in the Summit Countries

Following up on our discussion last Friday of economic conditions in the Summit countries, George Shultz suggested that we prepare charts on interest rate developments since your Administration took office. Two charts are attached. The first shows percentage changes in short-term rates since January 1981; the second shows short-term interest rate levels since the same date. In sum:

-- Interest rates have fallen sharply in the group of countries that has pursued successful anti-inflation policies. U.S. rates have been cut in half, from 18 percent to 9 percent. U.K., German and Japanese rates have fallen by between 2 and 6 percentage points.

-- Interest rates in France and Italy remain above their January 1981 levels (though they have been trending down over the past 1 to 1-1/2 years) and remain above rates in the other Summit countries.

-- Canada is something of a special case, in that they have broadly followed U.S. interest rate trends, maintaining a somewhat higher Canadian rate in order to attract funds and support the Canadian dollar. Since the Canadian shift toward anti-inflation policies in mid-1982, however, the difference between Canadian and U.S. rates has narrowed.

The implications are clear. The countries recording the most success on the anti-inflation front have been able to get interest rates down. The others -- France and Italy -- still face relatively high interest rates. This reflects their relatively poor inflation performance and, closely related, their efforts to use interest rates as a defense against downward exchange market pressures on their currencies.

Don

Donald T. Regan

Attachments

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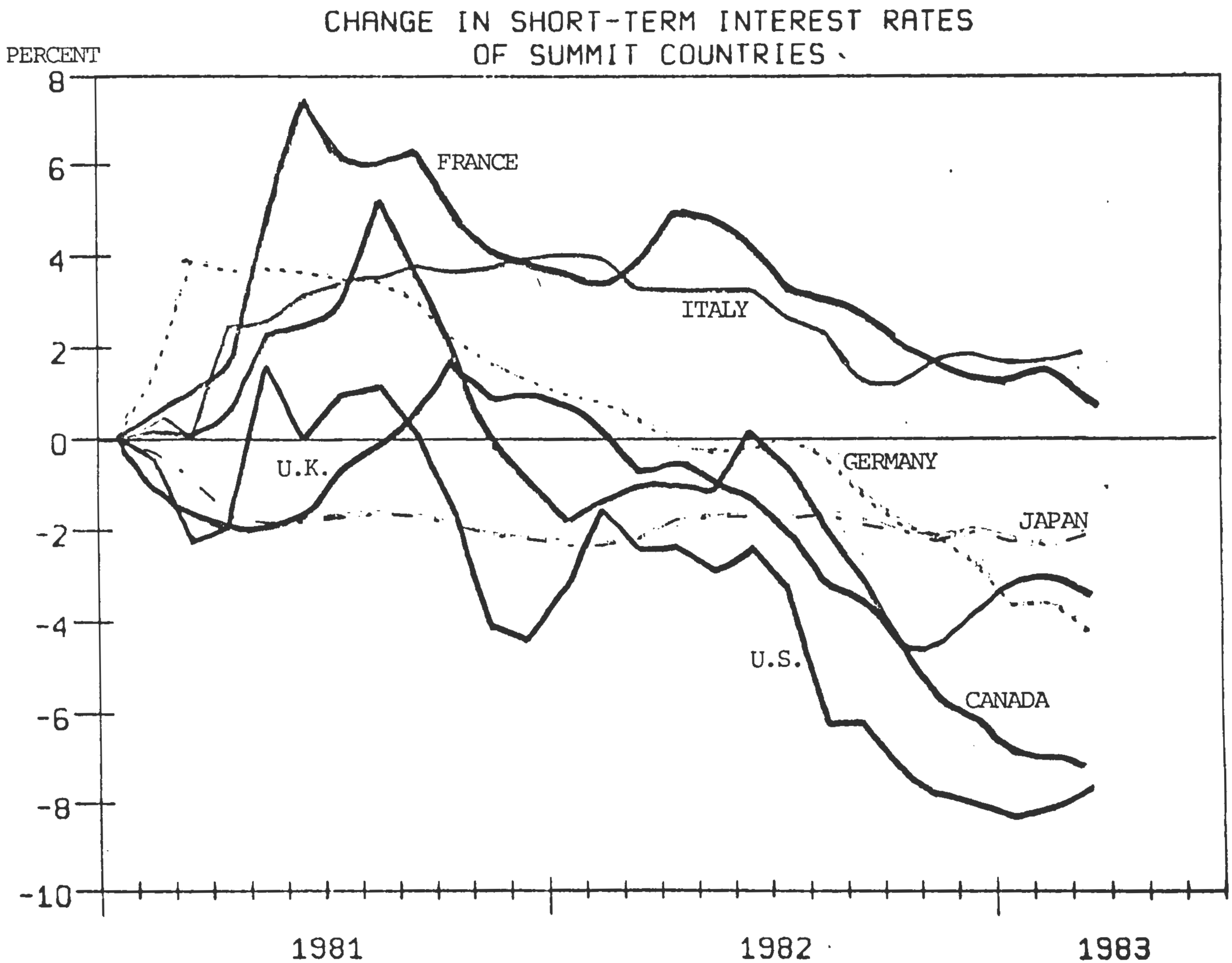

NOTE: Change is difference between observation and rate of January 1981. Short-term interest rates used are monthly averages of three-month rates on Wednesdays, except latest observation which is March 28, 1983. Short-term interest rates shown are: U.S. - New York C.D.; U.K. - London Interbank; France - Paris Call Money; Italy - Milan Money; Canada - Canada Finance Paper.

TAB B

March 31, 1983

MEMORANDUM FOR THE PRESIDENT

SUBJECT: Williamsburg Summit Briefing

Attached is a background paper that discusses the issue of Multilateral Surveillance. The Multilateral Surveillance initiative--the effort to get coordinated and complementary economic policies among the Summit participants--was first raised at the Versailles Summit and will be a topic of discussion at Williamsburg. This will be the subject of your next regular Williamsburg Summit preparatory briefing.

Don

Donald T. Regan

Attachment

Historical Perspective

° The post-World War II fixed exchange rate system established under the Bretton Woods Agreement was preceded intermittently in the late 1800's and early 1900's by the classical gold standard. The gold standard system exerted strong discipline over national economic policies, because a country's money supply was directly linked to changes in the gold stock brought about by trade or current account imbalances. If a country's balance of payments was in deficit, an outflow of gold occurred, the money supply then declined; growth and inflation slowed until balance in external accounts was restored. It broke down because it ultimately required either deflation or inflation on a scale that national authorities would not tolerate.

° The Bretton Woods system of fixed exchange rates (par values) was not as binding; it assumed basic stability in world economic conditions; looked to countries to adjust domestic policies as needed to maintain exchange rate stability; and provided for exchange rate changes only in instances of "fundamental disequilibrium."

° Par values were defined in terms of gold. The U.S. undertook to buy and sell gold freely at the par value for the dollar, and other currencies maintained their par values by buying and selling U.S. dollars. In this way, the whole system was linked to gold.

° The system worked well in the early postwar decades, which were characterized by dominance of the U.S. economy and by general price stability in the United States and most other major countries. Exchange rate changes were frequent, but tended to be isolated to one country at a time.

° The system began to come under increasing strain in the latter 1960s.

- -- The rigidity of exchange rates tended to delay or prevent changes needed to reflect evolution of countries' relative economic positions.
- -- The resurgence of inflationary pressures, particularly in the United States, undermined the U.S. competitive position and led to increasing divergences of economic performance among the major nations.
- -- These factors led to increasing world payments imbalances, pressures on the dollar, and ultimately to collapse of the fixed rate system.

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and early 1973, the new structure of exchange rates came under attack and could not be sustained. The period of generalized floating began in March 1973.

-- Discussions were continued during this period on the reforms of the international monetary system, focusing on reestablishment of some kind of fixed, but adjustable, exchange rate system.

-- Following the oil shock of late 1973/early 1974, which abruptly caused massive balance of payments deficits for oil importing countries, it was agreed to abandon efforts to reestablish a fixed rate system. This was motivated in part by recognition that efforts to maintain fixed rates in the face of the huge oil deficits would likely lead to an increasing spiral of protectionist steps and harsh domestic economic measures, as each country tried to improve its trade and balance of payments position -- and thus "protect" its exchange rate -- at the expense of others.

-- Subsequent discussions of the international monetary system focused on the operation of a flexible rate system, and culminated at the first Economic Summit in Rambouillet, France in 1975.

° The Rambouillet Summit understandings, later incorporated in amended IMF Articles of Agreement, reaffirmed the desirability of exchange rate stability, but recognized explicitly that the achievement of exchange rate stability depends on development of orderly underlying economic and financial conditions in the major nations.

° In essence:

-- The Bretton Woods system had attempted to exert discipline over national economic policy through the mechanism of fixed exchange rates, but had failed -- both to foster orderly economic conditions and to provide needed scope for change in response to evolution of world economic conditions.

-- The Rambouillet Summit and subsequent amendment of the IMF Articles of Agreement retained the strong emphasis on discipline, but placed responsibility directly on national economic policy-makers and gave the IMF new authority -- called "surveillance" -- to oversee the operations of the international monetary system and the compliance of its member countries with their undertakings to achieve orderly growth with reasonable price stability and to promote stability by fostering orderly underlying economic and financial conditions.

countries, notably France, advocated increased governmental intervention in exchange markets as a route to greater exchange rate stability. The United States, convinced that large-scale governmental intervention in markets is neither desirable nor an effective substitute for proper economic policy:

- -- proposed a study of the impact of past exchange market intervention; and

- -- proposed a major strengthening of "surveillance," with the objective of fostering better convergence of economic performance among the major countries and thus providing the underlying basis for greater exchange market stability.

° In an annex to the Versailles Communique ("Statement on International Monetary Undertakings"), the Summit countries accepted joint responsibility to achieve stability in the international monetary system through better convergence of policies aimed at producing lower inflation, economic recovery and higher employment; and agreed to strengthen surveillance of economic policies.

- -- The IMF's existing surveillance of countries' policies, performance and prospects tended to look at each country in isolation from others. One aim of the Summit agreement was to broaden the procedure to review a group of important countries simultaneously (multilateral surveillance) -- to compare and contrast their policies, performance and prospects; to identify which countries are moving in the "right" direction; and to determine which are "out of line" and hence likely to be subject to pressure in the exchange markets.

- -- The group agreed to cooperate with the IMF, with multilateral surveillance focused primarily on the five major countries (the G-5 -- the U.S., Germany, Japan, France and the U.K.) -- in the expectation that intensified international consultations on, and examination of, policies and performance would encourage better convergence of economic conditions and thereby greater international monetary stability.

° The first meeting of G-5 finance ministers and central bank governors for this purpose was held in September 1982. IMF Managing Director de Larosiere (in his private capacity) prepared a discussion paper and participated in the exchange, giving his assessment of major policy changes needed in various countries to improve convergence.

- -- Talks were frank. Pointed up policy and performance differences. Showed France as being "out of line" in medium-term policy stance and economic performance. Suggested exchange rate pressure would continue.

the April talks to focus on policy differences and their near-term implications; exchange rate pressures stemming from relatively poor performance in some countries; and need for "out of line" countries to move toward others in both policies and performance if greater stability for their currencies is to be achieved.

Our Aims at Williamsburg

° We remain convinced that the lasting way to achieve greater stability in exchange rates is to move toward better convergence of economic conditions among the major economies. (This is an essential conclusion of the intervention study referred to above, although the Summit countries have varying views on the utility and desirability of shorter-term intervention. This will be the subject of a later briefing.)

° We want the Summit to reaffirm and strengthen multilateral surveillance. Specifically, we are working toward:

-- reaffirmation of the objectives of the surveillance effort;

-- elaboration of policy goals by the major countries;

-- definition by each country of the policy approaches it intends to follow to achieve its goals; and

-- establishment of agreed criteria for assessing progress.

° This approach confirms the need for discipline and underlying stability and exerts that discipline by forcing key policy-makers to specify goals and policies; to collectively consider their likely effects, including exchange rate effects; and to assess their results.

° Such an agreement at the Williamsburg Summit would represent a concrete and useful initiative in the economic policy area.

° A more upbeat economic setting at time of May Summit will also provide the opportunity to highlight the success of anti-inflation policies: a number of the Summit countries have reduced inflation substantially; recovery is already under way; conditions have been established for sustained, noninflationary growth.

-- With inflation under better control in these countries, logical to shift emphasis to sustaining growth; reaping employment gains; expecting more stable international monetary conditions.

-- Those that have succeeded in reducing inflation and building recovery can expect more stability for their currencies; exchange rate pressures will remain for those that don't get inflation under control.

particularly France, have called for systematic intervention in foreign exchange markets to stabilize exchange rates. With policies and performance out of step with others, they face exchange market pressures on their currencies and want to try to force exchange rate stability through such government intervention.

2. The recent realignment of the European Monetary System -- preceeded by massive speculation, official intervention, and market disruption -- is strong evidence of the futility of intervention and of the inability of the exchange rate system to impose discipline and order.

3. Attempts to broaden the EMS-type experience, to try to deal with basic problems through market intervention, must be resisted. The debate needs to be shifted to fundamental policy approaches and problems -- including exchange market problems -- resulting from differences in approach. (Our resistance to solving exchange market problems through intervention does not apply to our commitment to intervene if necessary to counter serious episodes of exchange market disorder in fulfillment of our IMF Article IV obligations.)

4. Strengthening "surveillance" provides a desirable alternative to expensive -- and ultimately fruitless -- exchange market intervention. The only way to obtain meaningful and lasting exchange market stability is through convergence of policies and performance, and that is where the focus of our efforts should be.

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