

CONFIDENTIAL  
SUBJECT

at Home



JD  
HCC: Mr. Walker

10 DOWNING STREET

From the Private Secretary

26 May, 1982.

Dear John,

Versailles Summit

During their conversation yesterday evening, the Prime Minister and the Chancellor had a word about the issues raised in the Chancellor's minute of 20 May on the world economic outlook and the Versailles Summit.

The Prime Minister recalled her conversation with George Shultz, and said that she had been impressed by his argument that the right course for the President to take was to reduce the budget deficit by reducing expenditure, and not by increasing taxation. The Prime Minister said that she had indicated to Mr. Shultz her support of this line. The Chancellor said that he believed that Britain should join in urging President Reagan to do his utmost to secure a resolution of the US budget argument before the summer legislative recess. He believed that it was in the UK national interest that the US Administration should settle this matter and produce a declining sequence of budget forecasts, even if they had to accept tax increases as well as expenditure cuts in order to achieve it. Cutting spending was much the best means, but it was crucial that they bring deficit under control: and if this required tax increases, the President must not shirk them any more than the Prime Minister and the Cabinet here had shirked them. The Chancellor said that he thought it most important that the Prime Minister herself should make these points to President Reagan.

The Prime Minister said that she had difficulty with the idea of urging the Americans to increase taxes. She also had great sympathy with the President's objectives on expenditure; she thought that his social security proposals were courageous. She took, however, the Chancellor's point about the importance to the rest of the world of a declining sequence of US budget deficits. Perhaps the best formulation would be to say that we thought it most important that the deficits should decline, and that we wished them every success in their efforts to reduce expenditure.

I am sending a copy of this letter to Brian Fall (Foreign and Commonwealth Office) and David Wright (Cabinet Office).

John Kerr, Esq.,  
HM Treasury.

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Yours sincerely,

Michael Scholer

BK