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Dec 14, 1971

MEMORANDUM OF CONVERSATION

Subject: Meeting between Mr. Pompidou and Dr. Kissinger, Azores

Date and Time: 14 December 1971; 0830

Present: President Pompidou
Dr. Kissinger
Mr. Andronikof
Major General Walters

DECLASSIFIED

E.O. 12356, Sect. 3.4

MR NLN 95-3/8

BY JAR NARA, Date 7-25-95

Dr. Kissinger opened the conversation by thanking President Pompidou for the arrangements for him to have breakfast with him.

President Pompidou said he had spoken to Secretary of the Treasury Connolly and after that he believed Mr. Connolly had spoken to Dr. Kissinger. He had found someone who had firm ideas. He had said that the U.S. would defend the dollar after devaluation. As one knew this was like going to confession. The U.S. had the firm purpose of defending the dollar after a deal had been made but not the means and did not seem disposed such means as it had.

Dr. Kissinger said he understood what President Pompidou was saying. After talking to him he had spoken to the President and the President's view is that when we speak of defending the dollar, as he understood it, we are talking about what happens in the new monetary system. The President believes that as long as there is the expression on our part that is what President Pompidou described as defending the dollar, but President Pompidou seemed to feel that there were others. Leaving aside the present balances, the way to defend is to buy when it falls.

President Pompidou said that this was so. He drew on his experience with the French Franc. When the franc lost value, no one in the world, no central bank kept francs and the French had to give hard currency to bolster it (dollars). When the French found that they had exhausted their special drawing rights at the International Monetary Fund, their reserves and loans, all of which were insufficient, then they devalued. Afterwards, with the French franc at a correct level Central Banks still did not keep French Francs and if there were too many and we had a negative balance of payments the French had to give foreign currencies. This applied to the U.K. as well as to France. This is the process which he thought would be applied to the devaluation of the dollar. He understood that present dollar balances would not be included as they were too big. The President apparently felt we were

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Dr. Kissinger said that his impression after talking to Secretary Connolly is that the Secretary feels if the exchange alignment is correct then we will be prepared to operate the system, if what we had already talked about was not enough. Secretary Connolly preferred to delay the final commitment until the final settlement of the new international system. Dr. Kissinger said he would read what we were prepared to do as part of a general package on margins and rates. This was the formulation:

"Discussions will promptly be undertaken in the appropriate forums to resolve the longer term issues of the International Monetary Reform. Attention should be directed to appropriate means and division of responsibilities for defending established exchange rates; the proper role of gold, reserve currencies and special drawing rights in the operation of the system; the volume of liquidity and reexamination of permissible margins in established exchange rates and other means of establishing suitable flexibility in exchange rates. It is recognized that the decision in each of these areas will be interdependent." That was Secretary Connolly's formulation.

President Pompidou said he understood it but it was difficult for him.

Dr. Kissinger said that the President's view was that one way of proceeding would be the following: If President Pompidou thought it was reasonable, he and President Nixon could agree today on the approach to both the interim and long-term solution. They both, France and the U. S., could support that position in the negotiations in the following week. President Nixon and President Pompidou could agree to a certain devaluation of the dollar. If President Pompidou desired margins and a restart of the Trade Negotiations as well as the clause which we had given him, we could then support the definition of the exact rates between the French Franc and the German Mark which President Pompidou had indicated he desired on the previous day. Alternatively, the Presidents could turn the matter over to the Finance Ministers for discussion the following week. The President believed that he and President Pompidou approached the discussion in a broader spirit.

President Pompidou said it was difficult for him to react immediately on the first point, that is, the clause Dr. Kissinger had read. The rest he understood. If he had correctly understood what Dr. Kissinger said,

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there would first be a realignment of currencies, a certain devaluation of the dollar to be discussed and a reevaluation in fact of all of the other currencies in relation to the dollar. In that phase which was interim we should set certain margins.

Dr. Kissinger said that we were ready to do so.

President Pompidou said that if the U.S. maintained its formula, it would undertake to defend the rate without defining the defense .

Dr. Kissinger said that since he was honest he could not say that he was sure that Secretary Connolly's definition was the same as President Pompidou's. There was a difference in the way Texans bargained.

President Pompidou said he was not a Texan. President Nixon had told him on the previous day that he could not go further. Having had the Congress already vote a certain devaluation, he could not say that he would hold it or he would be in a difficult political position. As he was not a Texan, he would say that having had Congress vote a rate of gold and the dollar and whatever was said, he did not see how the President of the U.S. could come back to get another vote because he could not defend the dollar.

Dr. Kissinger said that he was not a good negotiator because he would tell President Pompidou what he really thought. Three months ago Secretary Train argued with equal vehemence for convertibility. Dr. Kissinger believed, as did the President, that the realities of the new situation will bring what President Pompidou had described. In fact, one argument advanced by Secretary Connolly as to why he is so tough is that it is so much harder for the U.S. to change the rate than it is for others.

President Pompidou said that in regard to the statement Dr. Kissinger had read he could not give agreement. He would have Giscard d'Estaing speak to Secretary Connolly. He did want to make two or three observations. In the statement he could not accept the absence of any mention of fixed parities and perhaps the problem of the substance of the role of reserve currencies. He had thought that in the last few months that the U.S. Government had admitted that in the new monetary system, at least in the final settlement, in reality that no currency should have this theoretical privilege. The reserve role of the dollar is actually a burden. Rather in parts of special drawing rights there is something similar for the reserves of Central Banks, including gold. The Central Banks agree to keep a certain percentage of currencies. This is not a privilege. They would be considered reserve instruments. President

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Pompidou said he wished to stress the matter of flexibility of currency rates. This was a very serious matter involving the whole concept of the role of margins. If it means that in the light of the evolving situation with its ups and downs that margins make living possible, he would agree. If it means that margins are a means of perpetuating revaluations and devaluations, with no fixed parities and flexible rates, then he could not agree.

Dr. Kissinger said the whole idea was based on fixed parities, otherwise it would make no sense.

President Pompidou said that referring to what Dr. Kissinger had said about the new parities, he wished to emphasize the French point of view. No European currency would follow the dollar. He would pass over the Benelux. He was concerned that the DM should be 6 percent over the franc. Seven percent was too much. Five percent not enough. The French had made precise calculations just as we had done with Canada, with whom we did half our trade.

Dr. Kissinger said that Secretary Connolly had told him that according to his information, Schiller said 3 or 4 percent and Brandt said 5 percent would be negotiable.

President Pompidou said 5 percent would be the absolute minimum. Schiller was a Texan. He was more stubborn than Brandt. To move to the question of the dollar rate and margins, the French position was for the narrowest margins possible. The trend was towards wide margins. We could not return to 1 and the trend was towards 3.

Dr. Kissinger said that Secretary Connolly asked him to say that this was not unsurmountable.

President Pompidou said that 2 would be acceptable. He knew that the Germans were for 3. Brandt said that was too much. The Gilstra report explains how with 3 two currencies could not be reserve. It would be an encouragement to speculation. Suppose movement capital believed that the dollar would move down 3 points and the DM up 3 points.

Dr. Kissinger said that he had talked to Secretary Connolly about margins. He would prefer to wait on this until the end of the meeting. He would be prepared to handle this if we settled the other matters. The President was prepared to split the difference between 2 and 2 1/2.

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President Pompidou asked what we should say if the Ministers agree.

Dr. Kissinger said that we had not settled the matter of devaluation.

President Pompidou said he would prefer to speak in terms of the price of gold, 5 percent to 7 percent, even if this is what the public is told. For the Congress it appeared it would be \$37 per ounce. The French preferred 37.50. He believed that we could go to \$38 an ounce. It would not be hard.

Dr. Kissinger said that what was really meant was a percentage.

President Pompidou said he felt it should be \$38.00 an ounce.

Dr. Kissinger said that we would not raise our voices on that.

President Pompidou said to the U.K. and Italy it would be 8 percent.

Dr. Kissinger, to speak with the same frankness, it was Secretary Connolly's view that he must never accept less than 10 or 9 percent devaluation in fact. But what President Pompidou and President Nixon decided would go. What did President Pompidou have to say.

President Pompidou said that above all they must not unleash speculation. How far could they go in the statement.

Dr. Kissinger said that it should be a general statement, that they had requested the Finance Ministers to look into the matter. If questions were asked about their meeting (President Pompidou and Dr. Kissinger), they should say that they had been discussing the Agenda.

President Pompidou agreed and said that they should leave for the meetings at the Junta Geral.