

31 January 1985

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PRIME MINISTER

AT 3/1

EMS

Joining the EMS would not solve the currency problems we  
have been experiencing.

Oil has a substantial impact upon sentiment towards  
sterling. This makes sterling unlike the other member  
currencies of the EMS.

If we joined the EMS, speculators would still put pressure  
on sterling. But we would have to defend the rate. We  
could no longer allow a gentle depreciation of the currency.  
Each time the currency was under pressure you could  
guarantee headline treatment and a sterling crisis. It  
would be like the sterling crises which beset the Labour  
Government of the late 1960s, and we would be forced into  
regular devaluations or revaluations against the EMS  
currencies, and would doubtless lose on intervention on the  
way.

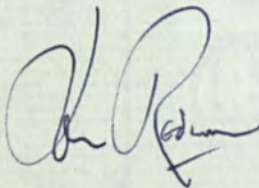
You cannot have both an exchange rate target and a monetary  
target. You have to decide what is most important and stick  
to it. You can only defend raising interest rates in recent  
weeks on the grounds that you had accepted the market's

verdict that money policy had become a little lax - and it  
had become too lax - and that speculators had gone too far  
and needed correcting.

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If we wish to retain sovereignty over our economic policy;  
if we wish to avoid being constantly up-ended and caught  
between different targets; and if we wish to avoid a series  
of sterling crises; we should not join the EMS. A more  
honest policy line than saying we would join when the time  
is right would be to drop all reference to the EMS at all.

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JOHN REDWOOD