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British Embassy
Dublin

1 January 1987

The Rt Hon Sir Geoffrey Howe QC MP
Secretary of State for Foreign and
Commonwealth Affairs
London S W 1

Sir

REPUBLIC OF IRELAND: ANNUAL REVIEW FOR 1986

1. "This year slips into the next with few regrets, surely marking a bedraggled end to an inadequate government" (Irish Times, 23 December). "At year's end we have a political crisis compounding an economic crisis, throwing a dark shadow of uncertainty over the prospects for 1987" (Sunday Independent, 21 December). Few Irishmen would quarrel with these assessments. A discredited coalition is clinging to power by manoeuvre and prayer. During the last week of the parliamentary session they survived by the casting vote of the Speaker no fewer than five times.

2. The events of the year that led up to this crisis are chronicled in the enclosed memorandum. Since I arrived in post only on 7 December, I am indebted to my Counsellor, Mr Robert Stimson, for preparing this paper which contains the substance of our annual review. The covering despatch draws attention to the main feature which strike a new-comer. I shall reserve more considered comment for my First Impressions Despatch.

3. As Mr Stimson says, the year opened well enough for the government - but everything then seemed to go wrong, from the disastrous divorce referendum in June to Ireland's ludicrous and lonely failure to ratify the Single European Act by the end of the year.

4. The heart of the failure is economic: high interest rates, low investment and low growth; punitive taxation and patchy social welfare; high prices, high unemployment and high emigration; above all a heavy burden of private debt and a public foreign debt per capita which is the fourth highest in the world. Garret FitzGerald still appeals for prudent economic management but after four years of power he cannot escape some responsibility for this state of affairs.

5. The political crisis stems directly from the failure to solve these economic problems. The Coalition's performance does not inspire confidence. MPs defect from the governing parties and the slender parliamentary majority evaporates. Almost everybody now expects a General Election early this year, probably next month.

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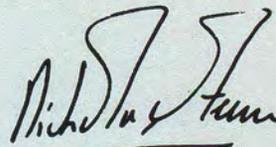
6. Irish elections are notoriously difficult to predict. This one is more difficult than most because of the uncertain impact of the new Progressive Democratic Party and the decision of Sinn Fein to abandon its traditional policy of abstentionism. Only Fianna Fail has a chance of governing alone. Their victory is predicted by the polls. Their weakness is that if they fail to win an overall majority, no other major party will enter a coalition led by Charles Haughey. The most plausible alternative is a coalition between Dr FitzGerald's Fine Gael and the Progressive Democrats with tacit support from a depleted Labour Party. The election will be fought on economic issues. It will be close and probably dirty.

7. The one success of this melancholy year has been the steady progress on Northern Ireland under the Anglo-Irish Agreement. Fear-some problems persist in the North, but the experience of 1986 has confirmed that the Agreement is an historic watershed in the relations between London and Dublin. It does not satisfy Irish aspirations, but it contains them: and its mechanisms make possible real co-operation between us. Dr FitzGerald's return to power would enable this co-operation to continue. A victory for Mr Haughey would mean a change of style. He criticises the present government for not being sufficiently "forceful or difficult or awkward" in defence of Irish interests. Mr Haughey would be all these things. He might seek to renegotiate the Agreement. More probably, he would assume personal direction of Anglo-Irish affairs and press for more rapid changes in the North. He would be a more angular partner than Garret FitzGerald. But he is a realist as well as an opportunist and would still have an interest in making the Agreement work. The Anglo-Irish process would become noisier with a Fianna Fail government in Dublin, but it would continue. There are interesting prospects for 1987.

8. I am sending copies of this despatch and its enclosure to the Secretary of State for Northern Ireland, to Her Majesty's Representatives at European Community Posts, at Washington and at the Holy See, and to the Governor of the Bank of England.

I am, Sir,

Yours Faithfully



N M Fenn

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REPUBLIC OF IRELAND: ANNUAL REVIEW FOR 1986

MEMORANDUM

1. 1986 was the year when Murphy's Law applied for Dr FitzGerald's Coalition Government: almost everything that could go wrong, did go wrong.
2. The year started auspiciously enough. The Anglo/Irish Agreement had just been signed. The punters, on the whole, were pleased. Dr FitzGerald's personal popularity was high, and the Coalition trailed the Fianna Fail opposition in the polls by only 10%, compared with 18% the previous summer. Moreover, the Agreement precipitated the formation of a breakaway party from within Fianna Fail, the Progressive Democrats. In January the Fianna Fail lead was as low as 6%. By December it was 21%. What went wrong?
3. Certainly not the Anglo/Irish Agreement. However hard they push us through the mechanisms established under that Agreement for more and speedier reforms in Northern Ireland, privately Irish Ministers and officials are well satisfied with what has been achieved this year. The trouble is that the man in the Dublin street is not really interested in the problems of Northern nationalists. What worries him most is the prospect of getting a job, and having got one, seeing how much of his pay vanishes in tax and social security contributions before he gets a chance to spend what is left on increasingly expensive necessities. A typical Dublin bus conductor, married with several children, earns Ir£150 a week but takes home only Ir£117. Of each extra pound earned in overtime he keeps only 56.5p. It is on the economic front that the idealistic Dr FitzGerald himself an economist, pre-occupied with the trials of Northern Ireland and with social reform, is perceived by many to have failed.
4. For events early in the year obliged him to concentrate on social and political rather than on economic issues. The year began with much excitement about the new political party. The Progressive Democrats held their first public meeting in January. Funds began to roll in. The original gang of two rapidly became a gang of four, as two further deputies defected from Fianna Fail. Meanwhile, against the advice of Fine Gael officials, the Taoiseach brought in an unpopular budget. A February poll showed the new party eating into popular support for the Government as well as for Fianna Fail. The Labour Party tried to steal Fine Gael's social reforming clothes by introducing in February a divorce bill into the Dail. The Taoiseach reacted to these pressures by reshuffling his Cabinet, which did nothing either to improve the Coalition's popularity or to satisfy disgruntled Fine Gael backbenchers eager for office. In April,

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after minimal consultations with the Catholic Hierarchy, he announced his intention to introduce his own Bill to remove the constitutional prohibition on divorce. The ensuing national debate was bitter and divisive. Mr Peter Barry masterminded the Fine Gael campaign in favour of reform with a canny and untypical lack of energy. The opponents of reform were uninhibited. The proposal was defeated in the Referendum of 26 June by the unexpected majority of 63% to 36%. This damaged the Taoiseach's standing, set back his hopes for the evolution of a pluralist society in the Republic and diminished his moral authority in addressing the Northern Unionists (Sir Alan Goodison's despatch of 10 July 1986).

5. On 9 April a Fine Gael backbencher had defected to the Progressive Democrats, reducing the Coalition's overall majority to one. On 10 June the resignation of an aged Labour TD left it without a majority at all. The recess of 4 July for the long summer break could not come soon enough for Dr FitzGerald. Coalition backbenchers were grumbling, and the opposition leader, Mr Haughey, was complacent.

6. The summer was wet and miserable, though the marching season in Northern Ireland was less violent than had been feared here. The farce of Mr Robinson's invasion of Clontibret awaits its final act in a Dublin court. With the exception of a single public protest about the routing of Orange parades, Mr Barry managed to appear to leave the handling of the marching season to the RUC's good sense. The Minister for Agriculture, Mr Deasy, incensed farmers with his unresponsive reaction to their claims that Irish agriculture was (yet again) in crisis. He said there was no money. But the tail end of Hurricane Charlie came to the rescue, destroying many crops and enabling the Government to make a case in Brussels for EC help. A long sunny Autumn brought further relief. Irish farmers this year have at last begun to realise that the CAP gravy train is running down and that they must do something to help themselves. The gradual decline in the influence of the farm lobby was reflected in the generally muted reaction to the package agreed at the December Agriculture Council.

7. The Taoiseach also had one stroke of luck when Mr Haughey unwisely announced on 3 September that Fianna Fail would put down a motion of no-confidence in the Government when the Dail resumed. Under the Irish rules, one can do this only once every six months. Mr Haughey was over-confident. The Government survived by a narrow margin, on 23 October, and the Coalition was still in office at the end of the year. In spite of the parliamentary arithmetic, they piloted through the Bills to ratify the European Convention on the Suppression of Terrorism and the Single European Act, and survived the Adjournment Debate. The signing on 18 September of the bilateral Anglo/Irish Agreement on the International Fund for Ireland provided a welcome distraction from domestic economic gloom, but the Irish remain disappointed that a way has yet to be found to overcome our technical objections to accepting some money for the Fund from the European Community. And a final embarrassment came at the year end when, in the best traditions of Irish democracy, a private citizen challenged in the courts the constitutionality of the Single European Act, and prevented an eager Government from ratifying it.

8. Throughout the year the economy stagnated, visibly so. More than

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600 businesses closed under a crushing burden of high interest rates and other overheads. The Government was reduced to offering cash bribes to people to buy unsold houses. But there were few takers. Consumers tightened their belts and increasingly fell into debt because of high personal taxation. Although inflation has come down to a satisfactory 3%, people became ever more disinclined to pay high prices in the shops. There was a mini spending boom over Christmas, but much of this money has been spent in Northern Ireland where prices are lower. Unemployment has risen to 18%. The figure would be worse if an estimated 35,000 people (net) had not emigrated this year. GNP has grown by only about 1%. Both individuals and the country remain heavily in debt. The national debt is IRE20 billion, nearly half of it foreign borrowing. Not all of these woes can be blamed on the Coalition. They inherited an economic mess four years ago from a free-spending, happy-go-lucky foreign-borrowing jam -today Mr Haughey. Exchange Rate management is not entirely within Irish control because of the close economic links with the United Kingdom with the Punt inside the IMS Exchange Rate Mechanism and the Pound outside. But Dr FitzGerald cannot claim success in the management of the nation's economic affairs.

9. Against this depressing economic background, we still managed to sell about IRE3.5 billion worth of a wide variety of goods to the Republic. Our market share is currently 42%. With sterling relatively weak, we are well placed to improve on these figures. We shall be looking at ways of encouraging British exporters, especially the smaller ones, not to neglect the many opportunities in this open and relatively easy market.

10. Our bilateral relations are probably in a happier state than they have ever been. In the improved atmosphere political relations are cordial, economic and cultural relations flourish, and it has even been possible to initiate discreet contacts between the Irish and British Armies. After a shaky start, the Irish, so well used to blaming the British for all their woes, are learning what it means to share responsibility. How far this continues will depend in large measures on the outcome of the 1987 general election in Ireland.

11. That election will be fought mainly on economic issues, although we can expect flak from all parties over Sellafield. In October the Coalition looked as though it might break up over its economic differences. But following a long and stormy Cabinet session on 15 October, the Government deferred an inevitable row over spending priorities by publishing a set of agreed parameters within which the 1987 budget will be framed. The main parameters are:

- a. No increase in the overall level of taxation in 1987;
- b. No further devaluation of the punt within the EMS (an 8% devaluation in August proved ineffective);
- c. 1987 Exchequer Borrowing Requirement to be lower than the 1986 target of 11.8% of GNP;
- d. 1987 Budget Deficit to be held at 7.4% of GNP, that is 1.1% lower than the 1986 figure of 8.5%

These imply large-scale spending cuts, probably of the order of IRE250 million. The difficulty lies in agreeing where the cuts

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should fall. This was being argued in the Cabinet at the end of the year. No Labour Minister will want the cuts to fall on his Department. The Tanaiste will do his best, but the chances of Ministers agreeing a budget are no better than evens. The crunch will come this month. Even if a budget is agreed, it will not be easy to get it through the Dail. All the signs point to a general election in February 1987.

A handwritten signature in black ink, appearing to be 'R F Stimson', written in a cursive style.

R F Stimson

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Dublin

1 January 1987

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