SECRET Prime Minister (2)

Econ Pol.

29 October 1982
ALAN WALTERS

MES 29/10

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PRIME MINISTER

MONETARY AGGREGATES: PROVISIONAL FIGURES

(attached) The first guesses of the monetary expansion during October suggest that there has been a rapid expansion in both broad and, a fortiori, narrow aggregates during the month. The expansion of M3 is put at about 1.8% and the expansion of M1 provisionally at 2.9%.

However, it is quite clear that some of the expansion, and probably much of it in M1, is due to the stagging of the STC issue. I suspect that there has been at least an additional £0.5Bn (ie about 1.3% of M1) due to this factor - but that is only a guess. The underlying rate for the month of M1 would then go down to 1.5% or less. Still rather high, but consistent with our policy.

I have been expecting some considerable increase, particularly in the M1 figure and it is not surprising. As inflation and interest rates have fallen, so one would expect a once-and-for-all adjustment of stocks of narrow money. These once-and-for-all increases will be reflected in a high percentage increase for some months. But they are the consequence of our success in reducing inflation and are not the monetary fuel for future inflations.

It is likely that with the development of more and more confidence in the fact that inflation is down for a considerable time, we shall experience quite a rapidly growing demand for money - and not merely for on-going stagging! People will be happy to hold sterling if they believe the value is going to be maintained, not eroded. So we should expect a fairly high monetary growth for some months.

However, I do believe that our caution in not reducing interest rates below 9% is still justified. We need to let the consequences of our very rapid reduction of interest rates, and inflation, work through the system. We should not try to force the pace at all. In other words, I see no reason at all for increasing interest rates, and precious few reasons for reducing them at present. I have discussed this attitude briefly with Peter Middleton and Eddie George and they both concur.

/Bank lending

SECRET

Bank Lending and Funding

Bank lending during the month is provisionally put at £1.4Bn - but as you know, there is very considerable uncertainty in these first guesses. I suspect also it is over-estimated because of borrowing for the stagging of STC, and I would guess the corrected figure to be around £1Bn.

Funding is proceeding quite satisfactorily. There are a substanital number of instalments from part payment gilts which will fall due over the next few months, and provide substantial sums to absorb the large maturing gilts. And we are continuing in a quiet way to convert some long-dated conventionals into a mixture of long indexed gilts and short conventionals.

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