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CHANCELLOR'S PAPERS ON MONEY FIGURES AND INTEREST RATES

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PART C

91G.SCB.3455.6

SECRET AND PERSONAL
UNTIL 11.30 AM ON FRIDAY 29 APRIL 1988

FROM: M H WHEATLEY

DATE: 28 April 1988

MR SCHOLAR

cc PPS
PS/Chief Secretary
PS/Economic Secretary
Sir P Middleton
Sir G Littler
Sir T Burns
Mr R I G Allen
Mr Peretz
Mr Grice
Miss O'Mara
Mr Pike
Mrs Ryding
Ms Bronk
Mr Cropper

FULL MONEY FIGURES: MARCH

I attach the Bank's press release on the full money figures which will be published at 11.30am on Friday 29 April.

2. Small changes to note from the provisional figures are:

- the percentage rises in the measures of broad money are all slightly higher.

- the PSBR for 1987/88 now rounds to a surplus of £3.5 billion (rather than £3.6 billion).

- "other counterparts" are £0.3 billion less negative, because of revisions to the banking external's and sterling net non-deposit liabilities.

3. We now have more information on the high lending figures. 1988 Q1 figures to be published in the May BEQB provide evidence of higher bank borrowing by companies which supports the view that companies have been switching from equity financing to bank

borrowing in the changed stock market conditions following the October fall. The Press Office will not be able to refer to the unpublished figures explicitly but we have amended the briefing line in DEFENSIVE (iii) to refer generally to this point. We have also added two quotations from the Chancellor's "This Week Next Week" interview to FACTUAL (vi) (recent statements on Monetary Policy).

4. The Bank will also be publishing at the same time a new quarterly press release (attached) giving a more detailed analysis of bank lending for house purchase. We do not expect any adverse press comment.

MW

MARTIN WHEATLEY
MG1

SECRET AND PERSONAL
UNTIL 11.30 AM ON FRIDAY 29 APRIL 1988

MR GEORGE | Copies to | Mr Coleby
Mr Flemming
Mr Plenderleith
Mr Foot
Mr W A Allen
Mr Warland
Mr Mann
Mr Midgley
Mr Pennington

Mr M St J Wright
Groups 2/2
2/3
2/4

Miss O'Mara)
Ms Ryding) HMT
Mr C Mowl)

FINAL MONEY PRESS RELEASE FOR MARCH 1988

I attach a draft of the covering text for the full press release for publication at 11.30 am on Friday, 29 April. Please may I have any comments by noon on Thursday, 28 April.

The percentage rises in the measures of broad money are all 0.1 to 0.2% points higher than in the provisional press release. In the counterparts the main revision is that "other counterparts" are £0.3 bn less negative, because of revisions both to the banking externals and sterling net non-deposit liabilities. The PSBR for the financial year now rounds - just - to a surplus of £3.5 bn rather than £3.6 bn.

Financial Statistics Division BB-1
26 April 1988

J W Thorp (4764)

Monetary aggregates & banking statistics: March 1988

1 The changes in the monetary aggregates are summarised below:

% changes	12 months to March 1988 not seasonally adjusted	March 1988 not seasonally adjusted	 seasonally adjusted
M0	+ 6.4	+1.8	+0.8
M1	+20.8	+6.0	+4.0
of which, non-interest-bearing M1	+15.0	+5.2	+1.5
M2	+13.5	+2.5	+1.6
M3	+20.9	+4.9	+3.2
M3c	+18.9	+3.9	+2.5
M4	+16.8	+3.3	+2.3
M5	+16.7	+3.5	+2.4

2 Tables A-G and I show the components and counterparts of the monetary aggregates. Tables K-N show details of the banks' and discount market's balance sheets; transactions of the consolidated UK monetary sector, excluding interbank items and valuation changes on foreign currency items, are shown in Table H. Details of the building societies' balance sheets are shown in *Financial Statistics*, Tables 7.6-7.8, published by the Central Statistical Office. An article in the May 1987 *Quarterly Bulletin* discussed the construction of the broad monetary aggregates.

3 Estimated seasonal movements in April 1988

The provisional seasonal movements are shown below. Because of the difficulties referred to in the December 1986 *Quarterly Bulletin* (page 519), the figures should be regarded as more uncertain than were the figures formerly given for banking months. They remain subject to revision.

£ millions	
M0	+ 140
M3	−1670
M4	−1450
M5	−1130
M3 counterpart: banks' sterling lending to UK private sector	−1710
M4 and M5 counterpart: bank and building society sterling lending to the rest of the UK private sector (see footnotes to Table G)	−1730

The seasonally-adjusted changes are obtained by subtracting (with due regard to sign) the seasonal movement from the unadjusted changes.

Bank of England
29 April 1988

1st Proof

NOT FO[illegible] 11.30 HOURS 29 APR 1988

Bank of England

Banking statistics

March 1988

A Public sector borrowing requirement, and other counterparts to changes in M3

£ millions

	Public sector borrowing requirement (surplus–): Central government borrowing requirement	Public sector borrowing requirement (surplus–): Other public sector contribution	Purchases (–) of public sector debt by UK private sector (other than banks): Other public sector debt	Purchases (–) of public sector debt by UK private sector (other than banks): Central government debt [a]: British government stocks	Purchases (–) of public sector debt by UK private sector (other than banks): Central government debt [a]: Other	External and foreign currency finance of public sector (increase–): Purchases of British government stocks by overseas sector	External and foreign currency finance of public sector (increase–): Other	Banks' sterling lending to UK private sector [b]	External and foreign currency transactions of UK banks: Sterling deposits from, net of market loans to, banks abroad (increase–)	External and foreign currency transactions of UK banks: Other overseas sterling deposits (increase–)	External and foreign currency transactions of UK banks: Other sterling lending to overseas sector[c]	External and foreign currency transactions of UK banks: Banks' net foreign currency liabilities (increase–)	Net non-deposit sterling liabilities (increase–)	M3 (columns 1-13)
	1	*2*	*3*	*4*	*5*	*6*	*7*	*8*	*9*	*10*	*11*	*12*	*13*	*14*
Calendar month (unadjusted)														
1987 Mar.	+ 4.312	– 1.025	+ 359	+ 746	– 282	– 719	+ 942	+ 3.433	+ 1.395	– 742	– 496	+ 811	– 1.885	+ 6.849
Apr.	+ 2.459	– 431	+ 265	– 202	– 63	– 590	+ 1.788	+ 1.118	– 724	+ 195	– 16	– 559	– 74	+ 3.166
May	+ 1.623	– 1.746	+ 482	– 813	– 454	– 12	+ 2.854	+ 2.346	– 982	– 767	– 31	+ 1.432	– 634	+ 3.298
June	– 38	– 466	+ 89	– 56	– 598	– 1.123	– 597	+ 4.712	+ 946	+ 430	– 300	– 224	– 868	+ 1.907
July	– 299	– 138	+ 266	+ 639	– 121	– 1.209	+ 403	+ 4.599	– 492	– 489	+ 573	– 1.133	+ 1.663	+ 4.[illegible]62
Aug.	+ 815	162	+ 428	+ 279	– 233	– 533	– 321	+ 1.134	+ 955	– 183	– 521	+ 533	– 1	+ 2.220
Sept.	– 189	+ 406	– 197	+ 259	– 83	– 589	+ 188	+ 5.519	+ 117	– 239	– 37	– 1.140	– 2.345	+ 1.670
Oct.	– 660	– 376	– 11	+ 121	– 69	– 979	+ 3.754	+ 2.963	– 1.281	– 718	+ 129	+ 2.507	+ 310	+ 5.690
Nov.	– 477	– 1.099	+ 325	– 1.437	– 247	+ 514	– 186	+ 3.303	+ 1.538	– 286	+ 216	– 1.294	+ 386	+ 1.256
Dec.	– 462	+ 651	– 335	– 653	– 180	– 80	+ 2.284	+ 5.455	+ 476	– 1.401	+ 276	– 1.815	– 1.636	+ 2.580
1988 Jan.	– 5.873	– 502	– 132	– 423	+ 223	– 238	+ 366	+ 5.084	– 2.002	– 674	+ 558	+ 464	+ 1.000	– 2.149
Feb.	+ 151	– 585	+ 111	– 791	– 54	– 306	– 39	+ 2.509	+ 556	– 199	– 207	– 627	+ 37	+ 556
Mar.	+ 3.649	+ 170	– 166	+ 634	– 232	+ 179	+ 1.345	+ 5.893	– 65	+ 445	+ 726	– 1.325	– 2.206	+ 9.047

B Public sector borrowing requirement, and other counterparts to changes in M4 and M5

£ millions

	Public sector borrowing requirement (surplus–)	Purchases (–) of public sector debt by UK private sector (other than banks and building societies): Other public sector debt	Purchases (–) of public sector debt by UK private sector (other than banks and building societies): Central government debt: British government stocks	Purchases (–) of public sector debt by UK private sector (other than banks and building societies): Central government debt: Other	External and foreign currency finance of public sector (increase–)	Banks' sterling lending to UK private sector excluding building societies [b]	Building societies sterling lending to UK private sector	External and foreign currency transactions of banks and building societies [c]	Net non-deposit sterling liabilities (increase–): Banks	Net non-deposit sterling liabilities (increase–): Building societies	M4 (columns 15-24)	Purchases (–) of public sector debt [d]	Bank bills	M5 (columns 25 –16 –17 –18 +26 +27)
	15=1+2	*16*	*17*	*18*	*19=6+7*	*20*	*21*	*22*	*23*	*24*	*25*	*26*	*27*	*28*
Calendar month (unadjusted)														
1987 Mar.	+ 3.287	+ 271	+ 378	– 359	+ 223	+ 3.123	+ 1.180	+ 819	– 1.885	– 335	+ 6.702	+ 359	+ 169	+ 6.940
Apr.	+ 2.028	+ 31	– 623	– 50	+ 1.198	+ 1.258	+ 1.590	– 1.164	– 74	– 676	+ 3.518	– 681	+ 58	+ 3.537
May	– 123	+ 196	– 728	– 417	+ 2.842	+ 2.316	+ 1.295	– 408	– 634	– 849	+ 3.490	– 591	+ 258	+ 4.106
June	– 504	– 136	+ 356	– 506	– 1.720	+ 5.118	+ 1.355	+ 760	– 868	+ 187	+ 4.042	– 15	– 187	+ 4.126
July	– 437	+ 160	+ 842	– 145	– 806	+ 4.403	+ 1.302	– 1.672	+ 1.663	+ 37	+ 5.347	+ 879	+ 112	+ 5.481
Aug.	+ 683	+ 361	+ 416	– 151	– 854	+ 1.023	+ 1.269	+ 718	– 1	– 785	+ 2.679	+ 659	+ 81	+ 2.793
Sept.	+ 217	– 85	+ 167	– 263	– 401	+ 5.429	+ 1.318	– 1.414	– 2.345	+ 369	+ 2.992	+ 117	– 235	+ 3.055
Oct.	– 1.036	– 76	– 610	– 2	+ 2.775	+ 2.519	+ 1.510	+ 523	+ 310	– 546	+ 5.367	– 712	+ 157	+ 5.500
Nov.	– 1.576	+ 380	– 1.467	– 180	+ 328	+ 3.211	+ 1.266	+ 88	+ 386	– 859	+ 1.577	– 937	– 376	+ 1.531
Dec.	+ 189	– 185	– 420	– 184	+ 2.204	+ 5.159	+ 970	– 2.533	– 1.636	+ 1.335	+ 4.899	– 574	+ 95	+ 5.209
1988 Jan.	– 6.375	– 448	– 280	+ 38	+ 128	+ 4.976	+ 1.466	– 1.750	+ 1.000	+ 1.555	+ 310	– 668	– 314	+ 18
Feb.	– 434	+ 253	– 937	+ 14	– 345	+ 2.556	+ 1.385	– 524	+ 37	– 737	+ 1.268	– 764	– 187	+ 987
Mar.	+ 3.819	– 65	+ 427	– 384	+ 1.524	+ 5.697	+ 2.097	– 194	– 2.206	– 658	+ 10.057	+ 326	+ 698	+ 11.103

[a] Purchases (–) of central government debt by the UK private sector (other than banks) are analysed in Table G.

[b] Including net purchases by the Issue Department of commercial bills and of promissory notes relating to shipbuilding paper guaranteed by the Department of Trade and Industry.

[c] Including net purchases of ECGD-backed promissory notes by the Issue Department.

[d] Excluding those instruments included within M5.

C M1, M3 and M3c: amounts outstanding

£ millions

	Notes and coin in circulation with public	UK private sector sterling sight deposits: Non-interest-bearing [a]	Non-interest-bearing M1 (columns 1 + 2): Unadjusted	Non-interest-bearing M1 (columns 1 + 2): Seasonally adjusted	UK private sector sterling sight deposits: Interest bearing	M1 (columns 3 + 4): Unadjusted	M1 (columns 3 + 4): Seasonally adjusted	UK private sector sterling time deposits[b]	M3 (columns 5 + 6): Unadjusted	M3 (columns 5 + 6): Seasonally adjusted	UK private sector deposits in other currencies [b]	M3c (columns 7 + 8): Unadjusted
	1	*2*	*3*		*4*	*5*		*6*	*7*		*8*	*9*
Calendar month												
1987 Feb.	13.113	26.924	40.037	41.642	35.351	75.388	77.058	78.078	153.466	155.439	28.839	182.305
Mar. [c]	12.723	28.354	41.077	41.268	38.648	79.725	79.920	80.443	160.168	159.638	28.586	188.754
Apr.	13.140	28.391	41.531	40.793	38.868	80.399	79.702	82.936	163.335	163.117	29.993	193.328
May	13.391	29.287	42.678	41.632	40.669	83.347	82.379	83.285	166.632	165.471	29.961	196.593
June [c]	12.988	31.135	44.123	43.374	41.327	85.450	84.708	83.090	168.540	167.787	29.452	197.992
July	13.709	30.493	44.202	43.475	42.340	86.542	85.857	86.269	172.811	171.451	31.247	204.058
Aug.	13.730	30.379	44.109	43.632	43.537	87.646	87.254	87.385	175.031	173.779	31.245	206.276
Sept. [c]	13.179	31.312	44.491	43.927	44.718	89.209	88.655	87.425	176.634	176.197	30.943	207.577
Oct.	13.693	30.982	44.675	45.401	47.398	92.073	92.900	90.251	182.324	182.561	31.491	213.815
Nov.	13.598	31.570	45.168	44.361	47.413	92.581	91.950	90.999	183.580	182.437	31.496	215.076
Dec. [c]	14.133	31.427	45.560	44.265	46.844	92.404	91.110	93.837	186.241	185.016	30.770	217.011
1988 Jan.	13.726	30.311	44.037	45.751	47.261	91.298	93.117	92.910	184.208	186.061	32.280	216.488
Feb.	13.445	31.462	44.907	46.435	45.971	90.878	92.614	93.882	184.760	186.818	31.271	216.031
Mar. [c]	14.465	32.761	47.226	47.163	49.150	96.376	96.317	97.430	193.806	192.825	30.673	224.479

D M1, M3 and M3c: changes[d]

£ millions: *percentages in italics*

	Notes and coin in circulation with public	UK private sector sterling sight deposits: Non-interest-bearing [a]	Non-interest-bearing M1 (columns 1 + 2)	Non-interest-bearing M1: 12-month change	UK private sector sterling sight deposits: Interest-bearing	M1 (columns 3 + 4)	M1: 12-month change	UK private sector sterling time deposits [b]	M3 (columns 5 + 6)	M3: 12-month change	UK private sector deposits in other currencies[b]: Transactions	UK private sector deposits in other currencies[b]: Valuation changes [e]	M3c (columns 7 + 8)
	1	*2*	*3*		*4*	*5*		*6*	*7*		*8*		*9*
Calender month (unadjusted)													
1987 Mar.	− 390	+1,430	+ 1,040	+ *10.0*	+ 3,319	+ 4,359	+ *22.5*	+ 2,490	+ 6,849	+ *19.0*	+ 621	− 803	+ 6,667
Apr.	+ 417	+ 36	+ 453	+ *11.5*	+ 220	+ 673	+ *23.1*	+ 2,493	+ 3,166	+ *20.5*	+ 2,215	− 808	+ 4,573
May	+ 251	+ 897	+ 1,148	+ *11.6*	+ 1,801	+ 2,949	+ *23.5*	+ 349	+ 3,298	+ *19.0*	− 419	+ 387	+ 3,266
June	− 403	+1,847	+ 1,444	+ *13.1*	+ 658	+ 2,102	+ *23.6*	− 195	+ 1,907	+ *19.2*	− 711	+ 201	+ 1,397
July	+ 721	− 639	+ 82	+ *11.9*	+ 1,001	+ 1,083	+ *22.6*	+ 3,179	+ 4,262	+ *21.0*	+ 1,586	+ 208	+ 6,057
Aug.	+ 21	− 114	− 93	+ *11.8*	+ 1,197	+ 1,104	+ *23.7*	+ 1,116	+ 2,220	+ *22.2*	+ 368	− 371	+ 2,218
Sept.	− 551	+ 935	+ 384	+ *5.6*	+ 1,195	+ 1,579	+ *20.4*	+ 91	+ 1,670	+ *19.6*	− 78	− 156	+ 1,434
Oct.	+ 514	− 330	+ 184	+ *11.4*	+ 2,680	+ 2,864	+ *24.7*	+ 2,826	+ 5,690	+ *22.4*	+ 1,630	− 1,082	+ 6,238
Nov.	− 95	+ 588	+ 493	+ *10.1*	+ 15	+ 508	+ *21.7*	+ 748	+ 1,256	+ *21.5*	+ 1,260	− 1,255	+ 1,261
Dec.	+ 535	− 144	+ 391	+ *9.9*	− 649	− 258	+ *22.7*	+ 2,838	+ 2,580	+ *22.8*	− 521	− 206	+ 1,853
1988 Jan.	− 407	−1,116	− 1,523	+ *11.4*	+ 417	− 1,106	+ *21.7*	− 1,043	− 2,149	+ *22.3*	+ 306	+ 1,186	− 639
Feb.	− 281	+1,155	+ 874	+ *12.2*	− 1,290	− 416	+ *20.5*	+ 972	+ 556	+ *20.4*	− 851	− 173	− 450
Mar.	+1,020	+1,300	+ 2,320	+ *15.0*	+ 3,173	+ 5,493	+ *20.8*	+ 3,554	+ 9,047	+ *20.9*	+ 859	− 1,525	+ 8,400
Calendar month (seasonally adjusted)				1-month change			1-month change			1-month change			
1987 Mar.	. .	. .	− 379	− *0.9*	+ 3,258	+ 2,879	+ *3.7*	+ 1,474	+ 4,353	+ *2.8*	+ 621	− 803	+ 4,171
Apr.	. .	. .	− 510	− *1.2*	+ 257	− 253	− *0.3*	+ 3,681	+ 3,428	+ *2.1*	+ 2,215	− 808	+ 4,835
May	. .	. .	+ 869	+ *2.1*	+ 1,838	+ 2,707	+ *3.4*	− 317	+ 2,390	+ *1.5*	− 419	+ 387	+ 2,358
June	. .	. .	+ 1,752	+ *4.2*	+ 587	+ 2,339	+ *2.8*	− 3	+ 2,336	+ *1.4*	− 711	+ 201	+ 1,826
July	. .	. .	+ 99	+ *0.2*	+ 1,036	+ 1,135	+ *1.3*	+ 2,527	+ 3,662	+ *2.2*	+ 1,586	+ 208	+ 5,457
Aug.	. .	. .	+ 146	+ *0.3*	+ 1,240	+ 1,386	+ *1.6*	+ 942	+ 2,328	+ *1.4*	+ 368	− 371	+ 2,326
Sept.	. .	. .	+ 294	+ *0.7*	+ 1,120	+ 1,414	+ *1.6*	+ 1,073	+ 2,487	+ *1.4*	− 78	− 156	+ 2,251
Oct.	. .	. .	+ 1,492	+ *3.4*	+ 2,771	+ 4,263	+ *4.8*	+ 2,136	+ 6,399	+ *3.6*	+ 1,630	− 1,082	+ 6,947
Nov.	. .	. .	− 1,010	− *2.2*	+ 90	− 920	− *1.0*	+ 851	− 69	—	+ 1,260	− 1,255	− 64
Dec.	. .	. .	− 94	− *0.2*	− 824	− 918	− *1.0*	+ 3,437	+ 2,519	+ *1.4*	− 521	− 206	+ 1,792
1988 Jan.	. .	. .	+ 1,466	+ *3.3*	+ 521	+ 1,987	+ *2.2*	− 1,061	+ 926	+ *0.5*	+ 306	+ 1,186	+ 2,436
Feb.	. .	. .	+ 667	+ *1.5*	− 1,187	− 520	− *0.6*	+ 1,273	+ 753	+ *0.4*	− 851	− 173	− 253
Mar.	. .	. .	+ 705	+ *1.5*	+ 2,969	+ 3,674	+ *4.0*	+ 2,323	+ 5,997	+ *3.2*	+ 859	− 1,525	+ 5,350

E M2: amounts outstanding and changes [d]

£ millions: *percentages in italics*

	Non-interest-bearing M1: Amount outstanding	Non-interest-bearing M1: Change in month	Other UK private sector sterling retail deposits with banks [f]: Amount outstanding	Change in month	UK private sector retail shares and deposits with building societies [f]: Amount outstanding	Change in month	National Savings Bank ordinary account: Amount outstanding	Change in month	M2 (columns1-4) Unadjusted: Amount outstanding	Unadjusted: Change in month	Unadjusted: 12-month change	Seasonally adjusted: Amount outstanding	Seasonally adjusted: Change in month	Seasonally adjusted: 1-month change
	1		*2*		*3*		*4*			*5*			*6*	
1987 Mar. [c]	41.077	+ 1.040	44.011	+ 791	84.785	+ 1.145	1.666	+ 1	171.539	+ 2.977	+ *12.2*	172.633	+1.747	+ *1.0*
Apr.	41.531	+ 453	44.636	+ 625	85.484	+ 699	1.664	− 2	173.315	+ 1.775	+ *12.4*	173.579	+ 907	+ *0.5*
May	42.678	+ 1.148	45.256	+ 620	85.427	− 57	1.660	− 4	175.021	+ 1.707	+ *12.4*	174.975	+1.418	+ *0.8*
June [c]	44.123	+ 1.444	46.091	+ 835	86.780	+ 1.353	1.660	—	178.654	+ 3.632	+ *11.9*	178.263	+3.294	+ *1.9*
July	44.202	+ 82	46.588	+ 497	87.148	+ 368	1.658	− 2	179.596	+ 945	+ *10.5*	179.150	+ 886	+ *0.5*
Aug.	44.109	− 93	46.778	+ 190	87.663	+ 515	1.655	− 3	180.205	+ 609	+ *10.7*	180.822	+1.664	+ *0.9*
Sept. [c]	44.491	+ 384	47.053	+ 275	88.909	+ 1.246	1.656	+ 1	182.109	+ 1.906	+ *10.0*	182.755	+1.932	+ *1.1*
Oct.	44.675	+ 184	47.612	+ 559	88.674	− 235	1.657	+ 1	182.618	+ 509	+ *9.6*	184.420	+1.680	+ *0.9*
Nov.	45.168	+ 493	48.438	+ 826	90.841	+ 2.167	1.651	− 6	186.098	+ 3.480	+ *10.8*	186.625	+2.231	+ *1.2*
Dec. [c]	45.560	+ 391	47.472	− 966	93.164	+ 2.323	1.670	+ 19	187.866	+ 1.767	+ *10.4*	186.762	+ 130	+ *0.1*
1988 Jan.	44.037	− 1.523	47.740	+ 268	94.662	+ 1.498	1.673	+ 3	188.112	+ 246	+ *11.7*	189.797	+3.006	+ *1.6*
Feb.	44.907	+ 874	47.944	+ 204	95.398	+ 736	1.672	− 1	189.921	+ 1.813	+ *12.7*	191.680	+1.859	+ *1.0*
Mar. [c]	47.226	+ 2.320	49.470	+ 1.526	94.898	− 500	1.670	− 2	193.264	+ 3.344	+ *12.7*	193.332	+1.624	+ *0.8*

[a] After deducting 60% of net debit transit items (see additional notes to Table 6 of the *Quarterly Bulletin*).

[b] Including certificates of deposit.

[c] Changes in the monthly-reporting population occurred in these months.

[d] Changes in the money stock may differ from those which can be calculated by reference to amounts outstanding. (See additional notes to Table 11 of the *Quarterly Bulletin.*)

[e] See additional notes to Tables 6 and 11 of the *Quarterly Bulletin*.

[f] See the June 1982 *Quarterly Bulletin* (page 225) for definitions of retail deposits.

F M4 and M5: amounts outstanding, and changes

£ millions; percentages in italics

	M3	UK private sector holdings of building society deposits: Shares and deposits	UK private sector holdings of building society deposits: Other [a]	Building societies holdings of M3	M4 (columns 1 + 2 + 3 − 4): Unadjusted		M4: Seasonally adjusted		Holdings of money-market instruments by UK private sector other than building societies	National savings deposits and securities	M5 (columns 5 + 6 + 7): Unadjusted		M5: Seasonally adjusted	
	1	*2*	*3*	*4*			*5*		*6*	*7*			*8*	
Amount outstanding														
1987 Feb.	153.466	118.848	2.271	10.317	264.268		266.687		3.907	9.873	278.048		280.929	
Mar.	160.168	119.760	2.135	11.240	270.823		271.110		4.049	9.968	284.840		285.153	
Apr.	163.335	120.715	2.176	11.884	274.342		275.201		3.998	10.039	288.379		288.958	
May	166.632	121.383	2.276	12.460	277.831		277.780		4.552	10.100	292.483		292.394	
June	168.540	122.767	1.996	11.707	281.596		281.560		4.562	10.174	296.332		296.408	
July	172.811	123.819	2.264	11.942	286.952		285.913		4.618	10.252	301.822		300.742	
Aug.	175.031	124.539	2.287	12.226	289.631		289.700		4.669	10.315	304.615		304.611	
Sept.	176.634	125.290	2.744	12.112	292.556		293.073		4.665	10.382	307.603		308.058	
Oct.	182.324	126.348	2.744	13.493	297.923		299.559		4.725	10.455	313.103		314.612	
Nov.	183.580	127.550	2.389	14.019	299.500		300.397		4.588	10.545	314.633		315.483	
Dec.	186.241	130.530	2.714	15.005	304.480		304.302		4.786	10.658	319.924		319.638	
1988 Jan.	184.208	132.717	2.764	14.783	304.906		305.262		4.313	10.832	320.051		320.813	
Feb.	184.760	133.881	2.776	15.247	306.170		308.226		3.928	10.936	321.034		323.588	
Mar.	193.806	135.356	2.742	15.678	316.226		315.392		4.900	11.060	332.186		331.421	
						12-month change		1-month change				12-month change		1-month change
Changes in calendar month														
1987 Mar.	+ 6.849	+ 912	− 136	+ 923	+ 6.702	+ *14.0*	+ 4.568	+ *1.7*	+ 143	+ 95	+ 6.940	+ *13.5*	+ 4.369	+ *1.6*
Apr.	+ 3.166	+ 955	+ 41	+ 644	+ 3.518	+ *14.6*	+ 4.109	+ *1.5*	− 52	+ 71	+ 3.537	+ *14.1*	+ 3.812	+ *1.3*
May	+ 3.298	+ 668	+ 100	+ 576	+ 3.490	+ *13.8*	+ 2.609	+ *0.9*	+ 555	+ 61	+ 4.106	+ *13.5*	+ 3.467	+ *1.2*
June	+ 1.907	+ 1.384	− 2	− 753	+ 4.042	+ *13.9*	+ 4.082	+ *1.5*	+ 10	+ 74	+ 4.126	+ *13.5*	+ 4.298	+ *1.5*
July	+ 4.262	+ 1.052	+ 268	+ 235	+ 5.347	+ *15.0*	+ 4.365	+ *1.6*	+ 56	+ 78	+ 5.481	+ *14.4*	+ 4.330	+ *1.5*
Aug.	+ 2.220	+ 720	+ 23	+ 284	+ 2.679	+ *15.6*	+ 3.797	+ *1.3*	+ 51	+ 63	+ 2.793	+ *15.0*	+ 3.878	+ *1.3*
Sept.	+ 1.670	+ 751	+ 457	− 114	+ 2.992	+ *15.0*	+ 3.446	+ *1.2*	− 4	+ 67	+ 3.055	+ *14.4*	+ 3.522	+ *1.2*
Oct.	+ 5.690	+ 1.058	—	+ 1.381	+ 5.367	+ *15.8*	+ 6.501	+ *2.2*	+ 60	+ 73	+ 5.500	+ *15.2*	+ 6.569	+ *2.1*
Nov.	+ 1.256	+ 1.202	− 355	+ 526	+ 1.577	+ *15.2*	+ 860	+ *0.3*	− 136	+ 90	+ 1.531	+ *14.7*	+ 893	+ *0.3*
Dec.	+ 2.580	+ 2.980	+ 325	+ 986	+ 4.899	+ *16.3*	+ 3.817	+ *1.3*	+ 197	+113	+ 5.209	+ *15.8*	+ 4.066	+ *1.3*
1988 Jan.	− 2.149	+ 2.187	+ 50	− 222	+ 310	+ *16.6*	+ 802	+ *0.3*	− 466	+174	+ 18	+ *16.3*	+ 1.025	+ *0.3*
Feb.	+ 556	+ 1.164	+ 12	+ 464	+ 1.268	+ *16.0*	+ 2.918	+ *1.0*	− 385	+104	+ 987	+ *15.6*	+ 2.729	+ *0.9*
Mar.	+ 9.047	+ 1.475	− 34	+ 431	+ 10.057	+ *16.8*	+ 7.138	+ *2.3*	+ 922	+124	+ 11.103	+ *16.7*	+ 7.755	+ *2.4*

[a] Includes certificates of deposit and time deposits issued by building societies.

G Supplementary detail

Purchases (increase −) of central government debt by UK private sector other than banks (Table A, columns 4 + 5)
£ millions

	Marketable debt: Stocks	Marketable debt: Treasury bills	Tax instruments	National savings	Other	Total	Banks' sterling lending to UK private sector (a): Seasonally adjusted	Bank and building society sterling lending to the rest of the UK private sector (b): Seasonally adjusted	Sterling borrowing by the private sector (c): Seasonally adjusted
Calendar month									
1987 Mar.	+ 746	− 92	+ 89	− 283	+ 4	+ 464	+ 2.529	+ 3.423	+ 3.592
Apr.	− 202	+ 103	+ 57	− 226	+ 3	− 265	+ 2.190	+ 3.874	+ 3.932
May	− 813	− 91	− 184	− 181	+ 2	− 1.267	+ 2.560	+ 3.794	+ 4.052
June	− 56	− 244	− 117	− 244	+ 7	− 654	+ 4.009	+ 5.698	+ 5.511
July	+ 639	− 10	+ 88	− 192	− 7	+ 518	+ 4.486	+ 5.391	+ 5.503
Aug.	+ 279	− 33	+ 20	− 225	+ 5	+ 46	+ 2.633	+ 3.744	+ 3.825
Sept.	+ 259	+ 124	− 98	− 115	+ 6	+ 176	+ 4.329	+ 5.623	+ 5.388
Oct.	+ 121	+ 56	− 167	+ 35	+ 7	+ 52	+ 2.922	+ 3.926	+ 4.083
Nov.	− 1.437	− 279	+ 51	− 30	+ 11	− 1.684	+ 3.276	+ 4.338	+ 3.962
Dec.	− 653	+ 8	− 17	− 171	—	− 833	+ 4.987	+ 5.822	+ 5.917
1988 Jan.	− 423	+ 273	+ 241	− 298	+ 7	− 200	+ 5.581	+ 7.127	+ 6.813
Feb.	− 791	− 23	+ 167	− 200	+ 2	− 845	+ 2.604	+ 4.221	+ 4.034
Mar.	+ 634	− 57	+ 14	− 189	—	+ 402	+ 4.778	+ 6.650	+ 7.348

(a) A counterpart to M3: unadjusted figures appear in Table A (column 8).
(b) A counterpart to M4: unadjusted figures appear in Table B (column 20 + 21).
(c) A counterpart to M5: unadjusted figures appear in Table B (column 20 + 21 + 27)

H UK monetary sector: transactions in liabilities and assets

[Table [illegible] in the *Quarterly Bulletin*]

£ millions

Calendar month	Total	Liabilities: Domestic deposits: Total: Unadjusted	Total: Seasonally adjusted	Public sector: Sterling: Unadjusted	Public sector: Sterling: Seasonally adjusted	Public sector: Other currencies	Private sector: Sterling: Unadjusted	Private sector: Sterling: Seasonally adjusted	Private sector: Other currencies	Overseas sector deposits: Sterling	Overseas sector deposits: Other currencies	Non-deposit liabilities (net)
1987 Apr.	+ 6.554	+ 4.943	. .	− 28	. .	+ 7	+ 2.749	. .	+ 2.215	+ 151	+ 1.731	− 271
May	+ 17.593	+ 3.953	. .	+ 1.343	. .	− 18	+ 3.047	. .	− 419	+ 2.099	+ 11.364	+ 177
June	+ 7.430	+ 1.838	. .	+ 227	. .	+ 12	+ 2.310	. .	− 711	926	+ 5.518	+ 1.000
2nd qtr	+ 31.577	+ 10.734	. .	+ 1.542	. .	+ 1	+ 8.106	. .	+ 1.085	+ 1.324	+ 18.613	+ 906
July	+ 10.402	+ 5.025	. .	− 119	. .	+ 17	+ 3.541	. .	+ 1.586	+ 2.127	+ 3.356	− 106
Aug.	− 5.300	+ 2.125	. .	− 443	. .	+ 1	+ 2.199	. .	+ 368	+ 195	− 8.501	+ 881
Sept.	+ 20.849	+ 2.323	. .	+ 150	. .	+ 30	+ 2.221	. .	− 78	+ 531	+ 15.646	+ 2.349
3rd qtr	+ 25.951	+ 9.473	. .	− 412	. .	+ 48	+ 7.961	. .	+ 1.876	+ 2.853	+ 10.501	+ 3.124
Oct.	+ 18.732	+ 6.938	. .	+ 104	. .	+ 28	+ 5.176	. .	+ 1.630	+ 1.575	+ 10.211	+ 8
Nov.	− 243	+ 3.527	. .	+ 852	. .	+ 64	+ 1.351	. .	+ 1.260	− 257	− 3.199	− 314
Dec.	+ 3.015	+ 769	. .	− 727	. .	− 28	+ 2.045	. .	− 521	+ 634	− 1.023	+ 2.635
4th qtr	+ 21.504	+ 11.234	. .	+ 229	. .	+ 64	+ 8.572	. .	+ 2.369	+ 1.952	+ 5.989	+ 2.329
1988 Jan.	− 4.918	− 1.378	. .	+ 93	. .	− 35	− 1.742	. .	+ 306	+ 3.035	− 5.110	− 1.465
Feb.	+ 7.478	+ 73	. .	+ 73	. .	+ 14	+ 837	. .	− 851	+ 143	+ 6.100	+ 1.162
Mar.	+ 8.536	+ 8.565	. .	− 236	. .	− 85	+ 8.027	. .	+ 859	+ 104	− 2.471	+ 2.338
1st qtr	+ 11.096	+ 7.260	. .	− 70	. .	− 106	+ 7.122	. .	+ 314	+ 3.282	− 1.481	+ 2.035

Calendar month	Assets: Total	Lending to public sector: Sterling: Total: Unadjusted	Sterling: Total: Seasonally adjusted	Sterling: Central government	Sterling: Other	Other currencies	Lending to private sector: Sterling: Unadjusted	Sterling: Seasonally adjusted	Other currencies	Lending to overseas sector: Sterling	Other currencies
1987 Apr.	+ 6.554	− 397	. .	− 265	− 132	− 36	+ 3.305	. .	+ 1.234	+ 557	+ 1.891
May	+ 17.593	+ 433	. .	+ 237	+ 196	+ 62	+ 4.960	. .	+ 2.703	+ 319	+ 9.116
June	+ 7.430	− 546	. .	− 270	− 276	+ 19	+ 3.105	. .	+ 780	+ 150	+ 3.922
2nd qtr	+ 31.577	− 510	. .	− 298	− 212	+ 45	+ 11.370	. .	+ 4.717	+ 1.026	+ 14.929
July	+ 10.402	+ 75	. .	+ 31	+ 44	+ 24	+ 3.225	. .	− 2.234	+ 1.719	+ 7.593
Aug.	− 5.300	− 507	. .	− 402	− 105	− 26	+ 1.483	. .	+ 1.023	+ 446	− 7.719
Sept.	+ 20.849	− 32	. .	+ 53	− 85	− 40	+ 6.049	. .	+ 20	+ 372	+ 14.480
3rd qtr	+ 25.951	− 464	. .	− 318	− 146	− 42	+ 10.757	. .	− 1.191	+ 2.337	+ 14.354
Oct.	+ 18.732	+ 1.265	. .	+ 1.213	+ 52	− 186	+ 3.074	. .	+ 3.459	− 295	+ 11.415
Nov.	− 243	− 782	. .	− 622	− 160	− 54	+ 2.416	. .	− 1.529	+ 1.211	− 1.505
Dec.	+ 3.015	+ 832	. .	+ 561	+ 271	− 322	+ 4.593	. .	− 2.058	− 15	+ 15
4th qtr	+ 21.504	+ 1.315	. .	+ 1.152	+ 163	− 562	+ 10.083	. .	− 128	+ 901	+ 9.895
1988 Jan.	− 4.918	− 1.403	. .	− 1.303	− 100	− 338	+ 1.350	. .	+ 735	− 58	− 5.204
Feb.	+ 7.478	− 217	. .	+ 57	− 274	− 101	+ 1.556	. .	− 956	+ 293	+ 6.903
Mar.	+ 8.536	+ 1.018	. .	+ 440	+ 578	− 301	+ 8.222	. .	+ 2.178	+ 2.185	− 4.766
1st qtr	+ 11.096	− 602	. .	− 806	+ 204	− 740	+ 11.128	. .	+ 1.957	+ 2.420	− 3.067

I M0, the wide monetary base

[Table 2 in the *Quarterly Bulletin*]

£ millions: *percentages in italics*

Monthly-average series

	Notes and coin in circulation outside the Bank of England: Unadjusted	Seasonally adjusted	Bankers' operational deposits with the Banking Department: Unadjusted	M0 (wide monetary base) (columns 1 + 2): Unadjusted	Seasonally adjusted	
		1	*2*	*3*		
Average amount outstanding in calendar month						
1987 Feb.	14.529	14.817	165	14.694	14.982	
Mar.	14.577	14.811	232	14.809	15.043	
Apr.	14.930	14.916	204	15.134	15.120	
May	14.972	14.984	204	15.176	15.188	
June	14.946	15.075	137	15.083	15.212	
July	15.271	15.166	235	15.506	15.401	
Aug.	15.337	15.258	182	15.519	15.440	
Sept.	15.349	15.376	184	15.533	15.560	
Oct.	15.299	15.457	202	15.501	15.659	
Nov.	15.365	15.525	183	15.548	15.708	
Dec.	16.447	15.661	186	16.633	15.847	
1988 Jan.	15.458	15.620	181	15.639	15.801	
Feb.	15.353	15.659	124	15.477	15.783	
Mar.	15.588	15.753	163	15.751	15.916	
Change between average amounts outstanding						
1987 Mar.	+ 48	− 6	+ 67	+ 115	+ 61	*+0.4*
Apr.	+ 353	+ 105	− 28	+ 325	+ 77	*+0.5*
May	+ 42	+ 68	—	+ 42	+ 68	*+0.4*
June	− 26	+ 91	− 67	− 93	+ 24	*+0.2*
July	+ 325	+ 91	+ 98	+ 423	+ 189	*+1.2*
Aug.	+ 66	+ 92	− 53	+ 13	+ 39	*+0.3*
Sept.	+ 12	+ 118	+ 2	+ 14	+ 120	*+0.8*
Oct.	− 50	+ 81	+ 18	− 32	+ 99	*+0.6*
Nov.	+ 66	+ 68	− 19	+ 47	+ 49	*+0.3*
Dec.	+ 1.082	+ 136	+ 3	+ 1.085	+ 139	*+0.9*
1988 Jan.	− 989	− 41	− 5	− 994	− 46	*−0.3*
Feb.	− 105	+ 39	− 57	− 162	− 18	*−0.1*
Mar.	+ 235	+ 94	+ 39	+ 274	+ 133	*+0.8*

J Bank of England transactions in commercial bills and in guaranteed export credit and shipbuilding paper

£ millions

Transactions in:	Banking Department: Commercial bills [a]	Issue Department: Commercial bills [a]	Shipbuilding paper [a]	Export credit paper [b]
Calendar month				
1987 Mar.	− 2.224	− 2.720	− 122	− 790
Apr.	+ 1.078	− 2.184	− 3	− 951
May	− 171	− 2.614	—	—
June	− 47	+ 1.607	—	—
July	+ 515	+ 1.374	—	—
Aug.	− 463	− 349	—	—
Sept.	− 116	− 530	—	—
Oct.	− 83	− 111	—	—
Nov.	− 39	+ 887	—	—
Dec.	+ 452	+ 862	—	—
1988 Jan.	− 129	+ 3.731	+ 3	+ 975
Feb.	+ 35	+ 953	—	—
Mar.	+ 132	− 2.326	− 3	− 975
Amount outstanding at end-March 1988	1.214	8.315	—	—

[a] Included within column 8 of Table A.

[b] Included within column 11 of Table A.

	Notes outstanding	Total deposits	Sight deposits: UK monetary sector	UK public sector	UK private sector	Overseas	Time deposits: UK monetary sector	UK public sector	UK private sector	Overseas	CDs and other short-term paper issued	Items in suspense and transmission	Capital and other funds
Amount outstanding													
1987 Oct.	1.117	300.237	10.082	1.807	79.340	10.121	50.669	4.364	78.271	35.977	29.607	9.233	36.541
Nov.	1.159	303.989	10.273	1.925	80.493	10.679	52.641	5.040	78.819	35.210	28.909	10.240	36.131
Dec. [d]	1.266	304.220	9.306 [c]	2.314	79.101	10.532	52.573	4.097	80.683	35.916	29.697	9.254	38.086
1988 Jan. [e]	1.116	307.417	9.178	2.135	78.347	11.231	53.577	4.472	79.113	37.895	31.469	9.877	37.028
Feb.	1.155	308.394	8.258	2.199	78.526	10.174	54.467	4.563	79.439	39.175	31.594	9.403	36.851
Mar.	1.195	321.250	9.034	2.528	83.530	10.193	56.597	4.052	82.546	39.422	33.348	12.022	38.863

Other currency liabilities

	Total deposits	Sight and time deposits: UK monetary sector	Other United Kingdom	Overseas	CDs etc and other short-term paper issued	Items in suspense and transmission	Capital and other funds	**Total liabilities/ assets**	*of which sterling*: *Liabilities*	*Assets*
Amount outstanding										
1987 Oct.	584.757	96.348	30.752	381.613	76.044	8.867	16.275	957.029	*347.129*	*344.696*
Nov.	555.951	90.163	31.240	365.813	68.735	6.602	15.649	929.721	*351.519*	*350.373*
Dec. [d]	543.860	85.675	30.263	356.647	71.276	4.946	16.773	918.404	*352.826*	*353.493*
1988 Jan. [e]	561.115	87.988	31.758	376.427	64.942	6.917	16.945	940.414	*355.438*	*355.661*
Feb.	560.313	84.488	30.786	376.599	68.440	7.447	17.980	941.544	*355.803*	*356.666*
Mar.	536.707	85.755	30.080	353.073	67.798	5.535	17.501	933.073	*373.330*	*375.545*

Sterling assets

	Notes and coin	Balances with Bank of England: Cash ratio deposits	Special deposits	Other	Market loans: LDMA Secured	LDMA Unsecured	Other UK monetary sector	UK monetary sector CDs	Building society CDs and time deposits	UK local authorities	Overseas
Amount outstanding											
1987 Oct.	2.420	906	—	183	8.126	51	57.191 [c]	10.034	1.265	1.831	18.484
Nov.	2.249	906	—	137	8.058	55	59.070	10.390	1.247	1.765	19.479
Dec. [d]	2.994	906	—	159	7.947	50	58.388	10.409	1.407	1.780	19.199
1988 Jan.	2.284	903	—	142	7.935	85	59.192	11.376	1.504	1.737	19.535
Feb. [e]	2.324	903	—	250	7.540	36	58.836	11.301	1.443	1.712	20.010
Mar.	2.399	903	—	−4	8.914	43	61.425	12.813	1.493	1.724	20.530

Sterling assets *continued*

	Bills: Treasury bills	Eligible local authority bills	Eligible bank bills	Other	Advances: Total	UK public sector	UK private sector	Overseas	Banking Department lending to central government (net)
Amount outstanding									
1987 Oct.	592	474	5.268	1.043	191.086	1.572	176.697	12.817	998
Nov.	1.149	442	4.867	1.024	192.970	1.500	178.453	13.018	551
Dec. [d]	776	433	5.741	665	197.630	1.680	182.803	13.147	820
1988 Jan. [e]	237	449	5.507	916	198.261	1.662	184.455	12.144	538
Feb.	211	429	5.125	999	199.823	1.485	186.348	11.990	684
Mar.	305	504	5.851	1.139	207.667	1.954	192.519	13.194	477

	Sterling assets *continued* — Investments: British government stocks	Other public sector	Other	Miscellaneous assets: Items in suspense and collection	Assets leased	Other	**Other currency assets** — Market loans and advances: Total	*of which advances*	UK monetary sector	UK monetary sector CDs	UK public sector	UK private sector	Overseas
Amount outstanding													
1987 Oct.	8.220	501	12.807	14.617	1.291	7.308	561.459	*180.016*	91.981	10.004	1.363	51.564	406.547
Nov.	7.444	503	13.124	16.287	1.292	7.363	532.082	*122.661*	85.387	9.357	1.271	47.745	388.323
Dec. [d]	7.702	501	13.403	13.967	1.278	7.339	520.210	*118.285*	78.827	9.252	931	45.232	385.968
1988 Jan. [e]	8.060	422	13.175	14.656	1.206	7.542	536.973	*123.354*	82.141	9.149	582	47.881	397.220
Feb.	7.869	431	13.099	14.817	1.183	7.643	536.767	*122.159*	78.641	8.880	461	46.660	402.125
Mar.	8.304	441	13.542	18.153	1.132	7.792	513.155	*117.978*	80.216	8.599	191	46.362	377.787

Other currency assets *continued*

	Bills	Investments: Total	United Kingdom	Overseas	Miscellaneous assets: Items in suspense and collection	Assets leased	Other	*Acceptances* — *Sterling*: *Total*	*of which by eligible Banks*	*Other currencies*	*Eligible liabilities*
Amount outstanding											
1987 Oct.	2.926	37.592	2.567	35.025	7.749	2	2.604	*16.181*	*15.754*	*3.304*	219.058
Nov.	2.694	36.114	2.476	33.638	5.893	2	2.563	*16.542*	*16.083*	*3.224*	220.173
Dec. [d]	2.399	35.390	2.678	32.712	4.179	1	2.732	*18.303*	*17.804*	*3.172*	222.265
1988 Jan. [e]	2.511	36.715	2.896	33.819	5.998	2	2.554	*21.369*	*20.878*	*3.146*	223.723
Feb.	2.511	37.038	2.750	34.289	6.633	1	1.928	*21.547*	*21.077*	*3.057*	225.876
Mar	2.561	35.394	2.643	32.751	4.456	1	1.960	*21.977*	*21.559*	*2.884*	233.080

[a] These tables include all monthly reporting institutions other than members of the London Discount Market Association—see page 562 of the December 1983 *Quarterly Bulletin*.
[b] Four contributors joined the series and four left at end-September, the net effect was a decrease of £235 million in sterling assets and a decrease of £150 million in other currency assets.
[c] The bulk of the movement within this category during October 1987 is due to the restructuring of intra-group funding by one bank.
[d] Four contributors joined the series and two left at end-December, the net effect was an increase of £265 million in sterling assets and an increase of £275 million in other currency assets.
[e] Four contributors left the series at end-January, the effect of which was a decrease of £2.136 million in sterling assets and a decrease of £12 million in other currency assets. The main impact arose within the other British banks group (Table L) as a consequence of a re-organisation within the Lloyds Bowmaker group.

		Notes outstanding	Sterling deposits: Total	of which sight deposits	UK monetary sector	UK public sector	UK private sector	Overseas	CDs etc and other short-term paper issued
British banks: Retail banks	Amount outstanding 1988 Feb.	1.155	158.999	*77.538*	15.993	3.498	113.332	14.720	11.456
	Mar.	1.195	167.191	*83.365*	17.385	3.713	119.431	14.428	12.234
Merchant banks [b]	1988 Feb.	—	19.055	*5.091*	2.911	587	11.360	1.792	2.404
	Mar.	—	19.465	*5.350*	3.085	507	11.642	1.816	2.415
Other British banks	1988 Feb.	—	37.699	*4.507*	14.087	1.881	12.929	4.676	4.126
	Mar.	—	38.053	*4.608*	14.034	1.602	13.298	4.615	4.504
Overseas banks: American banks	1988 Feb.	—	15.269	*3.253*	4.340	24	4.411	5.020	1.474
	Mar.	—	15.868	*3.325*	4.419	15	4.866	5.146	1.423
Japanese banks	1988 Feb.	—	19.285	*861*	7.941	194	3.922	3.296	3.933
	Mar.	—	20.227	*699*	8.144	269	4.489	3.372	3.984
Other overseas banks	1988 Feb.	—	58.088	*7.906*	17.455	578	12.007	19.847	8.201
	Mar.	—	60.446	*7.939*	18.604	476	12.347	20.231	8.788
Total	1988 Feb.	1.155	308.395	*99.156*	62.727	6.762	157.961	49.351	31.594
	Mar.	1.195	321.250	*105.286*	65.641	6.582	166.073	49.608	33.348

		Other currency deposits: Total	UK monetary sector	Other United Kingdom	Overseas	CDs etc and other short-term paper issued
British banks: Retail banks	Amount outstanding 1988 Feb.	45.309	6.737	6.645	27.541	4.385
	Mar.	43.052	6.764	6.228	25.984	4.076
Merchant banks [b]	1988 Feb.	12.874	3.131	2.127	7.122	493
	Mar.	11.932	3.011	2.154		
Other British banks	1988 Feb.	24.293	6.952	1.840	13.296	2.205
	Mar.	22.973	6.703	1.738	12.586	1.945
Overseas banks: American banks	1988 Feb.	79.692	8.106	10.259	46.869	14.459
	Mar.	73.600	8.221	10.296	41.347	13.737
Japanese banks	1988 Feb.	213.462	32.827	3.950	149.747	26.938
	Mar.	205.737	33.597	3.838	141.160	27.143
Other overseas banks	1988 Feb.	184.684	26.950	5.963	131.812	19.959
	Mar.	179.413	27.633	5.827	125.470	20.484
Total	1988 Feb.	560.314	84.703	30.784	376.387	68.439
	Mar.	536.707	85.929	30.081	352.900	67.799

		Sterling and other currency liabilities Items in suspense and transmission, capital and other funds	**Total liabilities/ assets**	**Sterling assets:** Notes and coin	Balances with Bank of England (including cash ratio deposits)	Secured money with LDMA	Market loans: Other UK monetary sector [c]	UK monetary sector CDs	UK local authorities	Overseas
British banks: Retail banks	Amount outstanding 1988 Feb.	39.054	244.517	2.292	734	5.135	18.107	3.220	918	3.739
	Mar.	43.243	254.681	2.368	477	5.910	18.448	3.832	941	4.073
Merchant banks [b]	1988 Feb.	5.368	37.296	3	45	298	7.592	2.381	117	1.510
	Mar.	5.096	36.493	4	47	451	264	2.423	115	1.494
Other British banks	1988 Feb.	11.086	73.078	3	117	306	11.063	1.190	258	1.357
	Mar.	10.977	72.002	3	120	562	11.457	2.422	275	1.385
Overseas banks: American banks	1988 Feb.	4.670	99.631	3	54	395	2.679	311	38	1.727
	Mar.	3.601	93.069	2	53	522	3.044	492	38	1.553
Japanese banks	1988 Feb.	1.646	234.392	—	49	393	4.044	88	54	5.009
	Mar.	1.591	227.335	—	49	421	4.375	164	24	5.012
Other overseas banks	1988 Feb.	9.858	252.630	23	151	1.013	15.384	3.392	327	6.668
	Mar.	9.413	249.273	22	152	1.047	16.530	3.481	333	7.012
Total	1988 Feb.	71.682	941.544	2.324	1.150	7.540	58.869	11.302	1.712	20.010
	Mar.	73.921	933.073	2.399	898	8.913	61.468	12.814	1.726	20.529

[a] Some smaller institutions report at end-quarters only: the coverage of some of the groups in these tables will therefore not be complete. The groups affected are Merchant Banks. Other British. American and Other overseas. but in no case is the coverage of total liabilities/assets less than 97%. For an analysis of end-quarter reporting institutions see Table N.

[b] Comprises those monetary sector institutions which are members of The British Merchant Banking and Securities Houses Association (formerly The Accepting Houses Committee).

[c] Including unsecured money with LDMA.

[d] Including holdings of sterling time deposits placed with. and sterling certificates of deposit issued by. building societies.

M Discount market: balance sheet

£ millions

Liabilities: borrowed funds

	Sterling: Total	of which Call and overnight	of which Other	Bank of England	Other UK monetary sector	Other United Kingdom	Overseas	Other currencies: Total	UK monetary sector	Other United Kingdom	Overseas
Amount outstanding											
1987 Sept.	10.035	*9.338*	*697*	194	7.144	2.653	45	197	68	111	18
Oct.	11.066	*10.262*	*804*	135	8.103	2.786	41	146	43	93	11
Nov.	10.908	*10.119*	*788*	375	7.767	2.725	40	259	162	93	6
Dec.	11.128	*9.950*	*1.178*	45	8.064	2.953	66	184	59	116	9
1988 Jan.	10.726	*9.899*	*827*	266	7.784	2.636	40	248	58	171	19
Feb.	10.459	*8.340*	*2.119*	163	7.604	2.647	45	233	74	142	17
Mar.	11.960	*10.809*	*1.150*	46	8.973	2.909	31	237	72	148	17

Sterling assets

	Total	Cash ratio deposits with the Bank of England	Bills: Treasury bills	Local authority bills	Other public sector bills	Other bills	Funds lent: UK monetary sector	UK monetary sector CDs	Building society CDs and time deposits	UK local authorities	Other United Kingdom	Overseas
Amount outstanding												
1987 Sept.	10.370	8	132	32	—	4.652	429	3.714	400	55	300	69
Oct.	11.344	10	127	27	—	4.492	190	4.967	565	50	227	44
Nov.	11.224	10	426	47	—	4.876	370	3.791	647	45	343	42
Dec.	11.427	10	261	132	—	5.219	525	3.705	747	43	260	32
1988 Jan.	11.050	10	85	66	—	4.945	491	3.743	644	41	488	53
Feb.	10.785	10	82	—		4.788	668	3.477	693	39	369	76
Mar.	12.295	10	126	20	—	6.253	531	3.530	684	38	385	79

Amount outstanding		Bills: Treasury bills	Eligible local authority bills	Eligible bank bills	Other	Advances: UK public sector	UK private sector	Overseas	Banking Department lending to central government (net)	British government stocks	Other
British banks:											
Retail banks	1988 Feb.	136	419	4.610	424	485	114.387	3.484	684	5.830	4.180
	Mar.	196	494	5.390	601	791	119.133	4.495	477	6.329	4.152
Merchant banks [b]	1988 Feb.	1	—	191	257	48	5.514	1.142	—	533	1.015
	Mar.	1	—	226	216	73	5.694	1.144	—	563	1.228
Other British banks	1988 Feb.	6	—	158	70	48	24.785	1.612	—	503	1.869
	Mar.	13	—	93	86	50	24.805	1.555	—	428	2.022
Overseas banks:											
American banks	1988 Feb.	1	—	84	19	14	9.554	1.290	—	288	806
	Mar.	—	—	35	22	12	9.711	1.408	—	349	782
Japanese banks	1988 Feb.	2	—	—	18	457	5.527	859	—	83	2.654
	Mar.	2	—	—	11	504	5.927	912	—	96	2.635
Other overseas banks	1988 Feb.	65	10	83	212	433	26.581	3.604	—	631	3.004
	Mar.	92	10	107	202	523	27.248	3.680	—	539	3.165
Total	1988 Feb.	211	429	5.126	999	1.485	186.347	11.991	684	7.867	13.528
	Mar.	304	504	5.848	1.138	1.953	192.518	13.194	477	8.304	13.984

Amount outstanding		Other currency assets: Market loans and advances: Total	*of which advances*	UK monetary sector	UK monetary sector CDs	UK public sector	UK private sector	Overseas	Bills	Investments	Sterling and other currencies: Miscellaneous assets[d]	*Acceptances*	*Eligible liabilities*
British banks:													
Retail banks	1988 Feb.	49.640	*14.139*	10.667	223	46	5.943	32.760	210	6.297	19.586	*7.877*	*128.536*
	Mar.	47.762	*13.964*	10.840	206	18	6.189	30.510	218	5.911	22.685	*7.809*	*134.910*
Merchant banks [b]	1988 Feb.	13.020	*3.552*	3.914	588	15	1.276	7.227	114	1.115	2.400	*4.187*	*9.266*
	Mar.	11.688	*3.217*	3.561	515	12	1.144	6.457	100	921	2.488	*4.248*	*9.440*
Other British banks	1988 Feb.	26.534	*7.612*	6.419	229	264	2.195	17.426	94	970	1.415	*654*	*22.639*
	Mar.	24.261	*6.904*	5.707	256	105	2.183	16.009	112	893	1.461	*674*	*22.241*
Overseas banks:													
American banks	1988 Feb.	75.142	*24.755*	7.164	637	—	14.022	53.320	150	1.980	5.095	*2.100*	*12.661*
	Mar.	69.042	*23.952*	7.016	932	2	13.583	47.509	95	2.133	3.714	*2.235*	*12.443*
Japanese banks	1988 Feb.	197.627	*31.368*	17.884	531	98	11.215	167.900	71	16.234	1.223	*2.035*	*14.205*
	Mar.	191.234	*31.333*	20.652	579	28	11.818	158.156	50	15.069	1.069	*2.136*	*14.864*
Other overseas banks	1988 Feb.	174.804	*40.732*	32.593	6.673	38	12.009	123.492	1.871	10.442	3.929	*7.751*	*38.567*
	Mar.	169.169	*38.608*	32.440	6.111	27	11.445	119.146	1.986	10.466	3.509	*7.759*	*39.181*
Total	1988 Feb.	536.767	*122.158*	78.641	8.881	461	46.660	402.125	2.510	37.038	33.648	*24.604*	*225.874*
	Mar.	513.156	*117.978*	80.216	8.599	192	46.362	377.787	2.561	35.395	34.986	*24.861*	*233.079*

[**Table 4** in the *Quarterly Bulletin*]

Sterling assets *continued*: Investments: British government stocks	Local authorities	Other	Other sterling assets	**Other currency assets**: Total	Certificates of deposit	Bills	Other	**Total assets/ liabilities**		
154	5	361	59	202	33	42	127	10.572	1987	Sept.
138	3	442	63	143	36	27	80	11.487		Oct.
84	3	476	62	258	112	23	123	11.482		Nov.
33	2	400	58	182	38	25	119	11.609		Dec.
35	2	384	63	247	48	28	171	11.297	1988	Jan.
163	2	339	79	242	18	32	192	11.027		Feb.
204	2	354	79	235	47	28	160	12.530		Mar.

Liabilities

	Sterling deposits				CDs etc and other short-term paper issued	Other currency deposits				CDs etc and other short-term paper issued	Sterling and other currency non-deposit liabilities	Total liabilities/assets
	Total	UK monetary sector	Other UK residents	Overseas residents		Total	UK monetary sector	Other UK residents	Overseas residents			
1987 1st qtr	1.807	282	1.102	411	13	1.647	488	130	1.007	21	657	4.112
2nd ..	1.820	260	1.091	457	12	1.453	432	131	868	22	618	3.891
3rd ..	1.815	233	1.174	398	9	1.437	472	154	781	30	661	3.913
4th ..	1.697	201	1.043	440	14	1.248	410	143	662	33	719	3.664
1988 1st qtr	1.691	160	1.035	485	11	1.155	330	118	678	29	636	3.482

Sterling assets

	Cash and balances with the Bank of England	Balances with and loans to		Bills		Advances			Investments		
		UK monetary sector	Overseas	Treasury bills	Other	UK public sector	UK private sector	Overseas	British government stocks	UK local authorities and other public sector	Other
1987 1st qtr	2	1.405	55	–	19	6	600	44	30	2	130
2nd ..	3	1.472	72	–	17	3	530	57	32	2	96
3rd ..	3	1.521	38	–	8	4	543	49	38	2	104
4th ..	2	1.409	38	–	12	7	558	52	33	2	102
1988 1st qtr	2	1.385	56	–	9	4	572	58	29	2	93

Currency assets

	Market loans and advances				Bills	Investments	Sterling and other currencies miscellaneous assets
	UK monetary sector	UK public sector	Other UK residents	Overseas residents			
1987 1st qtr	695	–	95	688	117	59	164
2nd ..	660	–	74	620	86	10	159
3rd ..	607	–	86	691	81	17	121
4th ..	500	–	82	560	104	35	169
1988 1st qtr	448	–	63	526	22	58	155

Symbols and conventions
– nil or less than £ million.
- - - figures above and below are not strictly comparable.
. . not available.
Owing to rounding of figures, the sum of the separate items will sometimes differ from the total shown.

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Any comments plse by 11.30 am
Thursday 28 April JWG 27.4.88

ANALYSIS OF BANK LENDING FOR HOUSE PURCHASE
NEW PRESS RELEASE, FRIDAY 29 APRIL AT 11.30 am

1 I attach a draft of this new press release, containing the March quarter figures. It is very close to the draft which you saw last week. The earlier draft has been seen by all the recipients of this note (except GM, DHAI and JAM) as well as by HMT, CSO, DoE and the CLSB.

2 The CLSB will publish their own version of the figures on Thursday 28 April. They have been publishing their figures for several years, and they account for a very large proportion of the figures that we are publishing. The DoE have also been presenting our figures in their own publications for several years, though many months in arrears. Our release is not therefore a new source of information; it is simply meant as a vehicle for making existing sources of information available in a more timely fashion.

3 We hope to avoid attracting too much attention with this release. It will be part of a package comprising the full March money figures press release (1 page of text and 8 pages of tables), the March bill turnover statistics (2 pages of tables), and the March London sterling CDs statistics (2 pages of tables); it will not have the "blue stripe" at the top of the page (only the text of the full money figures release has this). Also released at the same time is the March Sterling commercial paper release.

4 Nevertheless, given the recent surge in building society lending, there may be more than usual interest in the banks' lending for house purchase. The figures show that banks' house purchase lending fell back a little in the March quarter; but total bank and building society lending has increased .

5 Any comments about this press release should reach me no later than mid-day on Thursday 28 April.

Financial Statistics Division
26 April 1988

C R Mann (4427) BB-1

CRM

Provisional analysis of bank lending for house purchase

First quarter 1988

1 The attached tables provide an analysis of lending for house purchase for the three months to 31 March 1988 undertaken by a sample of banks which account for 85%-90% of total monetary sector lending for house purchase. The figures are at this stage provisional and may differ from equivalent data published elsewhere at a later date. Except where otherwise stated, the reported figures have not been grossed up to allow for banks excluded from the sample. The figures have not been seasonally adjusted and no adjustments have been made for changes in the sample of reporting banks.

2 During the first quarter of 1988 the banks undertook £2,894 of gross lending for house purchase (excluding repayments), compared with £3,225 million during the previous quarter. The amount of lending approved for house purchase (which includes undrawn amounts but excludes topping-up and improvement loans) was £2,220 million.

3 The number of new mortgages approved during the quarter was 59,000, nearly half of which were for first time purchasers. The average amount approved for new dwellings rose from last quarter's level to £42,700. The average amount approved for all dwellings was £37,700.

Notes for Editors

1 This is the first of a new series of releases, which will normally be available about 4 weeks after the end of the quarter to which they relate. This release subsumes information made available for their member banks by the Committee of London & Scottish Bankers in their press release published on 28 April, and by the Department of the Environment in their quarterly and annual 'Housing and Construction Statistics' publication.

2 Some of the information contained in the attached tables will continue to be published by the Department of the Environment in 'Housing and Construction Statistics GB'.

House purchase finance undertaken by banks

Table 1 : Advances for house purchase by value

£ millions

Date		Amount outstanding[a]		Gross loans[c]	Amount approved[d]		
		Bridging	Other[b]		Total	New dwellings	First time purchasers
1985	Q1	792	16,614	994	850	103	207
	Q2	822	17,373	1,149	1,377	139	242
	Q3	851	19,068	1,739	1,534	146	291
	Q4	841	20,270	1,524	1,008	124	211
1986	Q1	831	20,880	1,134	1,056	104	238
	Q2	941	21,953	1,925	1,854	156	315
	Q3	928	23,682	2,520	2,142	197	343
	Q4	927	24,854	2,331	1,875	199	444
1987	Q1	959	26,235	2,130	1,646	205	506
	Q2	1,112	28,501	2,727	2,384	292	555
	Q3	1,270	31,546	3,413	2,718	328	843
	Q4	1,328	34,495	3,225	2,405	320	757
1988	Q1	1,378	36,657	2,894	2,220	303	756

[a] these figures comprise lending by all monetary sector institutions

[b] including topping-up and improvement loans

[c] excluding bridging finance

[d] excluding bridging finance, topping-up and improvement loans

Table 2 : Advances for house purchase by number of loans approved and average amount approved

Date		Number of loans (thousands)[a]			Average amount approved (£s)		
		All dwellings	New dwellings	First time purchasers	All dwellings	New dwellings	First time purchasers
1985	Q1	29	3	8	29,300	31,500	24,400
	Q2	45	4	10	30,900	31,500	25,300
	Q3	49	5	11	31,400	31,500	26,400
	Q4	32	4	8	31,500	32,200	27,200
1986	Q1	33	3	9	32,200	34,100	27,400
	Q2	57	5	11	32,600	34,700	28,500
	Q3	63	6	11	33,900	35,000	31,000
	Q4	57	6	15	32,900	35,600	29,800
1987	Q1	47	6	16	34,800	36,900	30,800
	Q2	65	8	18	36,600	38,800	31,300
	Q3	73	8	24	37,400	39,500	35,000
	Q4	65	8	23	37,300	39,200	33,000
1988	Q1	59	7	25	37,700	42,700	30,600

[a] the figures have not been grossed up. The equivalent data in the Department of the Environment's 'Housing and Construction Statistics' are grossed up to represent the whole of the monetary sector.

Table 3 : Distribution of loans by size of approval
percentage

Date	under £10,000		£10,000 to £19,999		£20,000 to £29,999		£30,000 to £39,999		£40,000 to £49,999		£50,000 +	
	value	number	value	number	value	number	value	number	value	number	value	number
1985 Q1	1	5	13	24	23	28	28	25	14	9	22	9
Q2	1	4	10	19	21	27	30	28	15	11	23	11
Q3	1	4	9	19	22	28	29	28	15	11	24	11
Q4	1	5	10	20	20	26	28	26	14	10	27	12
1986 Q1	1	5	10	21	20	26	25	24	15	11	30	14
Q2	1	5	9	20	19	25	26	26	14	11	30	13
Q3	1	5	9	19	18	25	24	25	13	10	35	16
Q4	1	4	9	19	19	26	24	25	14	11	32	15
1987 Q1	1	3	8	19	18	25	23	24	15	12	36	17
Q2	-	3	7	16	16	23	23	25	16	13	39	20
Q3	-	3	7	16	16	24	21	24	15	13	42	21
Q4	1	3	7	17	17	26	19	22	15	12	42	21
1988 Q1	1	3	7	17	15	24	19	21	14	12	44	23

Table 4 : Distribution of the number of loans by purchase price
percentage

Date	under £15,000	£15,001 to £19,999	£20,000 to £29,999	£30,000 to £39,999	£40,000 to £49,999	£50,000 to £59,999	£60,000 to £69,999	£70,000 to £79,999	£80,000 and over
1985 Q1	8	6	17	20	14	7	5	5	13
Q2	7	4	14	18	16	11	9	6	15
Q3	7	4	14	19	15	11	8	6	15
Q4	7	5	15	18	15	11	8	6	15
1986 Q1	8	5	14	17	15	10	8	6	17
Q2	9	4	13	17	15	11	8	6	17
Q3	7	3	12	16	15	9	7	7	20
Q4	7	5	15	14	15	8	6	6	18
1987 Q1	8	6	15	14	13	11	9	6	18
Q2	9	5	14	14	13	10	9	7	20
Q3	6	6	14	14	12	11	9	6	22
Q4	4	7	16	14	11	10	9	7	22
1988 Q1	5	7	17	13	10	9	9	7	23

Bank of England
29 April 1988

MONEY SUPPLY IN MARCH: PRESS BRIEFING

A. FACTUAL

(i) **Funding outturn 1987-88**

Main Point

Almost exact full fund of Government's activities in 1987-88 (in fact very small overfund of £0.1bn). All of last year's intervention fully funded. So effect on broad money/liquidity sterilised.

Other Points

Small carry over of 1986-87 underfund of £0.3bn. Taking account of this gives small underfund of £0.2bn, but more than covered by gilt sales already tied up in April. Underfund in March of £5.6bn. Overfund of £1.4bn in 1987-88 on M4 definition.

(ii) **Changes in main monetary aggregates**

figures revised

	per cent			
	M0	M3	**M4**	M5
12 month growth rate	**+6.4** **(+5.8)**	+20.9	**16.8**	16.7
Annualised six-month growth	**(+4.6)**	(+19.7)	**(+15.6)**	(15.5)
one month change	**+1.8** **(+0.8)**	+ 4.9 (+ 3.2)	**+3.3** **(+2.3)**	+3.5 (+2.4)

(Figures in brackets seasonally adjusted s.a.)

(iii) **MO**

Seasonally adjusted figure (5.8%) within 1987-88 target range. Unadjusted figures (6.4%) outside range, but due to different timing of Easter in 1987 and 1988.

(iv) **Broad money**

(a) 12 month growth rates. M4 slightly up on February and is a record.

(b) But 3 and 6 month growth rates lower than mid 1987-88.

(c) One month growth rates. M4 above recent growth rates (but see defensive (ii)).

(d) M4 gives less erratic signals than M3. Hence MTFS' emphasis on measures including liabilities of building societies as well as banks.

(v) **Lending**

(a) Should not read too much into individual counterparts, which are hard to interpret.

(b) Trends in bank lending also distorted by increase in banks' share of mortgage lending in 1987:

- Banks' market share up from 18 per cent of new advances 1986 to 37 per cent end 1987.

- Banks' mortgage lending a quarter of total increase in bank lending in 1987, compared with 15 per cent in 1986.

Bank plus building society lending therefore a better measure than bank lending alone. See EPR article.

(c) One month changes: percentage growth in bank and building society lending lower than bank lending alone. (Unadjusted £bn increases in bank and bank and building society lending are records.)

	Bank and building society lending		Bank lending	
	£ billion	%	£ billion	%
January	6.4 (+7.1)	+1.9 (+2.1)	15.1 (+5.6)	+2.4 (+2.7)
February	+3.9 (+4.2)	+1.2 (+1.2)	+2.5 (+2.6)	+1.2 (+1.2)
March	7.8 (+6.7)	+2.3 (+1.9)	+5.9 (+4.8)	+2.7 (+2.2)

(Figures in brackets seasonally adjusted)

figures revised

(d) 12 month growth rates (unadjusted): bank and bank and building society lending figure are records.

	Bank and building society %	Bank
September	20.0	23.6
October	19.3	22.9
November	19.0	22.5
March	18.8	22.8
January	20.0	24.7
February	19.9	24.3
December	20.8	25.2

figures revised

SECRET AND PERSONAL
UNTIL 11.30 AM ON FRIDAY 29 APRIL 1988

(vi) **Monetary Policy - Recent Statements**

(a) **Chancellor in Mansion House speech 4 Nov 1987**

"To prevent there being excessive liquidity in the economy, our policy is to ensure that, over time, any net intervention is sterilized - in other words, fully funded."

(b) **Chancellor in Autumn Statement debate (14 January)**

"Keeping the economy on track involves keeping a constant watch on all the indicators of how the economy is developing and then taking action as necessary. I have never hesitated to act in the past when I have judged that there was a risk to our inflation objectives. I can assure the House that I shall not hesitate to do so in future. It is precisely by acting promptly that we have been able to avoid the need for drastic and destabilising lurches in policy. Our track record speaks for itself."

(c) **Chancellor on interest rates (Budget speech, 15 March)**

"Short term interest rates remain the essential instrument of monetary policy. Within a continuous and comprehensive assessment of monetary conditions, I will continue to set interest rates at the level necessary to ensure downward pressure on inflation."

(d) **Chancellor on exchange rates (Budget speech, 15 March)**

"Exchange rates play a central role in domestic monetary decisions as well as in international policy co-operation. I believe that most businessmen have welcomed the greater exchange rate stability over the past year. It is important that they also accept the financial discipline inherent in this policy."
(Also see MTFS, 2.11)

(e) **Chancellor on inflation and exchange rates (This Week Next Week interview, 24 April)**.

added

"Our ultimate aim is certainly the total eradication of inflation."

"We are certainly interested in the maximum possible exchange rate stability, within the context of sound anti-inflationary policy."

B. POSITIVE

(i) Achieved full fund for 1987-88 and all intervention fully funded. Intervention has not been allowed to lead to inflationary pressures.

(ii) **Commitment**: Government remains committed to maintaining sound monetary conditions as key to keeping firm downward pressure on inflation.

(iii) **<u>Increases in domestic costs</u>:** Will not be accommodated either by monetary expansion or by exchange rate depreciation. See factual (vi) (d).

C. DEFENSIVE

(i) **<u>MO growth likely to breach target range</u>?** MO within 2-6 per cent range set in 1987 Budget for 1987-88, of which March is last month (but see factual (iii)). 1988-89 FSBR chapter 3 recognised that 12-month growth may move to top of or outside 1-5 per cent target range in early part of 1988-89 but should be within range later in year. Six-month growth rates (annualised) currently below 12-month rates.

(ii) **<u>Why one month M4 (and M3) growth so high</u>?** Profile of PSBR means large underfund in March (£5.6bn this month). Only small increase in 12 month growth rate. Large index linked gilt redemption very close to end of month, may have had an expansionary effect on money supply growth.

(iii) **<u>How to interpret bank lending figures</u>?**

Unadjusted 1 month £bn increase and 12 month growth rate in <u>bank lending</u> are records, but figures inflated because March is an interest charging month. Seasonally adjusted, the £bn increase is below the figures for December and January. Possible that some companies switching from equity financing to bank borrowing. Also, lending for house purchase thought to have been buoyant.

added

SECRET AND PERSONAL
UNTIL 11.30 AM ON 29 APRIL 1988

Unadjusted £bn increase and 12 month growth rates in bank and building society lending are records, but like bank lending, figures inflated because March is an interest charging month. Seasonally adjusted, the £bn increase is below the figures for January.

Too much should not be read into one months figures (but note that 12 month growth rates are very high).

(iv) **Growth of credit/liquidity inflationary?**

- Experience of number of years shown that high rate of growth of lending and liquidity consistent with lower inflation because increase liquidity willingly held ie held as savings rather than for spending. See EPR article.

- No sign of resurgence of inflation.

- Not right to restrict growth by quantitative controls: lenders and borrowers should be free to make own decisions. Nor would such controls be effective.

(v) **Consumer credit boom?**

- No evidence that rate of lending to consumers accelerating in recent months: 12 month growth rate close to its average since 1982 of 18 per cent. (Some credit simply displacing cash and cheque payments - over 40 per cent of credit card users pay no interest.)

- Vast bulk of personal borrowing takes form of mortgages, which represented 2/3 of outstanding personal debt at end of 1987. Mortgage lending accounts for almost half of all of bank and building society lending. Increase overall as percentage of GDP in 1980s mainly attributable to growth in mortgage borrowing, as result of 2½ million increase in households buying own home.

- Consumer credit only some 15 per cent of total personal debt. Less than 5 per cent of personal debt takes form of credit card lending (including interest-free component). (See Chancellor's speech to FHA, 17 June 1987).

(vi) **Significance of broad money**. No explicit broad money target in 1988-89. But growth of broad money still taken into account. See MTFS 2.09 and 3.11.

(vii) **Intervention inflationary?** Only poses inflationary threat if not funded. 1987-88 intervention has been fully funded.

(viii) **Government no longer committed to exchange rate stability?** At recent international meetings, commitment to currency stability re-affirmed. Stability never implied complete immobility in all circumstances as Chancellor made clear repeatedly.

(ix) **Conflict between maintaining stable exchange rate and message from domestic indicators?** As Chancellor told interim committee:

> "Clearly, if a conflict between objectives for inflation and exchange rates emerges priority must be given to inflation - but, in practice, this dilemma occurs only infrequently."

(x) <u>**Future changes in interest rates**</u>? Never speculate. (Also see factual (v) (a)).

(xi) <u>**Counter latest exchange rate rise with interest rate cut or intervention**</u>? Never discuss market tactics.

(xii) <u>**UK's real interest rates out of line with competitors**</u>? Deflating current three month money rates by recent pricc indices suggests UK real interest rates above international average for major countries, but <u>no evidence that this is inhibiting growth or investment</u>. FSBR forecasts 9 per cent growth in business investment for 1988.

(xiii) <u>**Change to funding rule**</u>. From start of 1988-9 Building societies will be treated same as banks so gilt sales to building societies will no longer count towards full fund. No relaxation of monetary policy. Including building societies with banks recognises their evolving status.

(x) **Future changes in interest rates?** Never speculate. (Also see factual (v) (a)).

(xi) **Counter latest exchange rate rise with interest rate cut or intervention?** Never discuss market tactics.

(xii) **UK's real interest rates out of line with competitors?** Deflating current three month money rates by recent price indices suggests UK real interest rates above international average for major countries, but no evidence that this is inhibiting growth or investment. FSBR forecasts 9 per cent growth in business investment for 1988.

(xiii) **Change to funding rule.** From start of 1988-9 Building societies will be treated same as banks so gilt sales to building societies will no longer count towards full fund. No relaxation of monetary policy. Including building societies with banks recognises their evolving status.

FROM: T PIKE
DATE: 28 April 1988

1. MR GRICE
2. ECONOMIC SECRETARY

cc PS/Chancellor
Sir P Middleton
Sir T Burns
Sir G Littler
Mr Scholar
Mr Sedgwick
Mr Culpin
Mr Peretz
Mrs Lomax
Miss O'Mara o/r
Ms Ryding
Mr Hurst
Ms Bronk

File: MAMC C9

Despite the small increase in the 12 month rate, the six month annualised growth in notes and coin has been dropping steadily since December.

JWG
28.4.88

M0 FIGURES

The latest weekly figures for M0, covering the final week of April, are attached. They show that the 12 month growth rate of M0 in April is 6.2 per cent (5.9 per cent not seasonally adjusted). The sa and nsa 12 month growth rates of notes and coin in April are 6.1 and 5.8 per cent respectively.

2. Six month annualised growth of notes and coin is 4.8 per cent in April.

T. Pike

T PIKE

CONFIDENTIAL

M0 : THE WIDE MONETARY BASE

thly data	Level £ million (Change in brackets)							Percentage change on previous month		6 month % growth annualised		Percentage change on previous year			
	Notes and Coin (nsa)	Notes and Coin (sa)		Bankers' Deposits	M0 (nsa)	M0 (sa)		Notes(sa) and Coin	M0 (sa)	Notes & Coin (sa)	M0 (sa)	Notes and Coin (nsa)	Notes and Coin (sa)	M0 (nsa)	M0 (sa)
August	15337	15258	(92)	182	15519	15440	(39)	0.6	0.3	6.0	6.2	4.3	4.6	4.5	4.7
September	15349	15376	(118)	185	15534	15561	(121)	0.8	0.8	7.8	7.0	5.3	5.0	5.2	4.9
October	15299	15456	(80)	203	15501	15659	(98)	0.5	0.6	7.4	7.3	5.1	5.2	5.5	5.6
November	15365	15525	(69)	183	15548	15707	(48)	0.4	0.3	7.4	7.0	4.8	4.8	4.9	4.9
December	16447	15651	(136)	186	16633	15846	(139)	0.9	0.9	7.9	8.5	4.7	4.8	4.2	4.3
January	15458	15620	(-41)	181	15638	15801	(-45)	-0.3	-0.3	6.1	5.3	4.7	4.5	4.8	4.6
February	15353	15659	(39)	124	15477	15783	(-18)	0.2	-0.1	5.3	4.5	5.7	5.7	5.3	5.3
March	15588	15753	(94)	162	15750	15916	(133)	0.6	0.8	5.0	4.6	6.9	6.4	6.4	5.8
April	15796	15825	(72)	229	16025	16054	(138)	0.5	0.9	4.8	5.1	5.8	6.1	5.9	6.2

	Level £ million (Change in brackets)					Percentage change on previous week
	Notes(sa) and Coin		Bankers' Deposits	M0 (sa)		M0 (sa)
h						
	15682	(14)	98	15780	(-16)	-0.1
	15731	(49)	239	15970	(190)	1.2
	15738	(7)	133	15871	(-99)	-0.6
	15788	(50)	161	15949	(78)	0.5
	15827	(39)	181	16008	(59)	0.4
l						
	15832	(5)	263	16095	(87)	0.5
	15775	(-57)	97	15872	(-223)	-1.4
	15833	(58)	259	16092	(220)	1.4
	15861	(28)	297	16158	(66)	0.4

SECRET

CHANCELLOR OF THE EXCHEQUER

PMP

"First guess" money figures:

M3

1% (seasonally adjusted)

0·2% (unadjusted)

18·2 – 19·2% over 12 months.

I thought we were now on M4!

Lending

£4·6 – 6·6 bn (adjusted)

£4 bn (unadjusted)

90/G.jfw.45/024

CONFIDENTIAL

FROM: MS V F BRONK
DATE: 5 May 1988

1. MR GRICE JWG 5.5.88
2. ECONOMIC SECRETARY

cc PS/Chancellor
Sir P Middleton
Sir T Burns
Sir G Littler
Mr Scholar
Mr Sedgwick
Mr Culpin
Mr Peretz
Mrs Lomax
Miss O'Mara
Ms Ryding
Mr Hurst
Mr Pike

File: MAMC C9

M0 FIGURES

The latest weekly figures for M0, covering the first week of May, are attached. They show that the 12 month growth rate of M0 to the latest four week period was 5.7 per cent (4.5 per cent not seasonally adjusted). Annual growth of notes and coin to the latest four week period was 5.9 per cent (4.7 per cent not seasonally adjusted).

2. The latest four week period annual comparison may still be affected by imperfect seasonal adjustments around Easter last year. The level of M0 in the first week of May was 6.1 per cent higher than the May average last year, and growth of notes and coin over the same period was 6.4 per cent (6.5 per cent not seasonally adjusted).

3. The six month annualised growth rate of notes and coin to the latest four week period was 5.0 per cent, compared with 4.8 per cent in April.

Vivien Bronk

MS V F BRONK

CONFIDENTIAL

M0 : THE WIDE MONETARY BASE

Monthly data — Level £ million (Change in brackets)

Monthly data	Notes and Coin (nsa)	Notes and Coin (sa)	(Change)	Bankers' Deposits	M0 (nsa)	M0 (sa)	(Change)	Percentage change on previous month: Notes(sa) and Coin	Percentage change on previous month: M0 (sa)	6 month % growth annualised: Notes & Coin (sa)	6 month % growth annualised: M0 (sa)	Percentage change on previous year: Notes and Coin (nsa)	Percentage change on previous year: Notes and Coin (sa)	Percentage change on previous year: M0 (nsa)	Percentage change on previous year: M0 (sa)
1987 September	15349	15376	(118)	185	15534	15561	(121)	0.8	0.8	7.8	7.0	5.3	5.0	5.2	4.9
October	15299	15456	(80)	203	15501	15659	(98)	0.5	0.6	7.4	7.3	5.1	5.2	5.5	5.6
November	15365	15525	(69)	183	15548	15707	(48)	0.4	0.3	7.4	7.0	4.8	4.8	4.9	4.9
December	16447	15661	(136)	186	16633	15846	(139)	0.9	0.9	7.9	8.5	4.7	4.8	4.2	4.3
1988 January	15458	15620	(-41)	181	15638	15801	(-45)	-0.3	-0.3	6.1	5.3	4.7	4.5	4.8	4.6
February	15353	15659	(39)	124	15477	15783	(-18)	0.2	-0.1	5.3	4.5	5.7	5.7	5.3	5.3
March	15588	15753	(94)	162	15750	15916	(133)	0.6	0.8	5.0	4.6	6.9	6.4	6.4	5.8
April	15797	15826	(73)	229	16026	16055	(139)	0.5	0.9	4.8	5.1	5.8	6.1	5.9	6.2
May (1/4) @	15947	15948	(122)	160	16107	16108	(53)	0.8	0.3	5.5	5.2	6.5	6.4	6.1	6.1
Latest 4 weeks @	15756	15855	(59)	203	15959	16058	(77)	0.4	0.5	5.0	5.1	4.7	5.9	4.5	5.7

Weekly data — Level £ million (Change in brackets)

Weekly data	Notes(sa) and Coin	(Change)	Bankers' Deposits	M0 (sa)	(Change)	Percentage change on previous week: M0 (sa)
April						
6th	15832	(5)	263	16095	(87)	0.5
13th	15775	(-57)	97	15872	(-223)	-1.4
20th	15834	(59)	259	16093	(221)	1.4
27th	15862	(28)	297	16159	(66)	0.4
May						
4th	15948	(86)	160	16108	(-51)	-0.3

@ Weekly data for the current month so far include estimates for the unbacked note issue. The latest week also includes an estimate for coin. The changes for the current month so far use as a base the previous full month and the full month a year ago.

Ch
I have asked for updates on the various statistics
AA

From : D L C Peretz
Date : 11 May 1988

MR A ALLAN

cc Miss Noble
Miss O'Mara
Mrs Ryding

USE OF PRUDENTIAL CONTROLS TO RESTRAIN MORTGAGE LENDING

The Chancellor asked to be reminded of the (somewhat limited) thinking done in this area at the time of abolition of mortgage lending guidance.

2. I am attaching :-

a) a note by Mrs Lomax (17 November 1986);

b) a subsequent letter from the Bank of England, dated 24 November 1986.

c) a minute from Mr Bridgeman, dated 25 November 1986, with a subsequent exchange of minutes between you and the Economic Secretary's Office.

d) the minutes of the Chancellor's meeting of 4 December 1986. Paragraphs 5-12 deal with this issue.

e) the speaking note the Chancellor used in explaining the change to the Prime Minister in December 1986. Paragraph 7 describes the prudential action taken.

f) the "prudential" letter the Bank of England sent to all banks and deposit takers.

3. The Building Societies Commission capital adequacy rules, circulated in February 1987, set a 4% capital requirement for mortgages of 95% or more, compared to the requirement of 1 or 2% for ordinary mortgages.

4. The letter mentioned in (b) above from Mr Barnes is quite a good exposition of the supervisory angle, as seen by the Bank of England.

pp D L C PERETZ

90/G/jfw/4561/024

COPY NO..1...OF 15 COPIES

SECRET AND PERSONAL

FROM: MS V F BRONK

DATE: 11 May 1988

1. MISS O'MARA

The growth of broad money looks moderate, as we expected, but the lending figures remain high

Moss

2. CHANCELLOR

(X and Y)

cc Economic Secretary
Sir P Middleton
Sir T Burns
Mr Scholar
Mr Peretz
Mr Grice o/r
Mr Pike
Mrs Ryding
Mr Holgate
Mr Gray No 10

n/s

Ch/ This partly explains why MG seem to forget about M4 in the 1st guess & provisionals - Bank don't have all the figs they need at this time of the month to do a full 1st guess. Would be interesting to know historic error between the data we do have on M4 at this stage of cycle and final figs. MPW 11/5

MONEY SUPPLY IN APRIL: "FIRST GUESS" FOR M3 AND OUTTURN FOR M0

(All figures are unadjusted unless specified otherwise)

Table 1 summarises the Bank's "first guess" at the M3 figures for April, which are still subject to significant revision, and shows the confirmed outturn figures for M0 that were circulated on 28 April.

Table 1: Growth of Monetary Aggregates in April

per cent

	M0	M3**
Annual growth rate*	5.9 (6.2)	18.2 to 19.2
Change in month*	0.5 (0.9)	-0.2 to 0.6 (0.6 to 1.4)
Target range	1-5	-

* Figures in brackets are seasonally adjusted

** The actual outturn has been within the range forecast on this basis in 15 of the last 18 months.

X 2. M4 figures are not yet available. But figures for the largest building societies show fairly strong retail inflows of around £1.3 billion (including interest crediting). This suggests that the percentage rise in M4 may be about the same as that in M3 and that annual growth of M4 may also have dropped back by over 1 per cent.

3. Sterling bank lending is likely to have remained high in April, with an increase in the range £2.9-£4.9 billion (£4.6 billion-£6.6 billion seasonally adjusted). The figure may have been boosted by increased lending for home improvements, as commitments made ahead of the April tax change were translated into actual borrowing. The British Gas call on 19 April may also have caused an increase in borrowing. There is no evidence of unwinding of January's bill arbitrage (which would have depressed lending), although some unwinding may have been masked by further arbitrage in April, as bill rates were depressed in the middle of the month.

4. Lending by the largest building societies continued buoyant in April.

M3 components and counterparts

5. Table 2 (attached) compares the changes in M3 components underlying the "first guess" with the average monthly change over the previous 12 months. Table 3 (attached) provides a similar comparison for M3 counterparts.

Timetable

6. We expect to receive provisional April M3 figures on Friday 13 May and provisional M4 figures on Tuesday 17 May. They will be published on Thursday 19 May. Full money and banking figures for March will appear on Tuesday 31 May.

Vyvien Bronk

V F BRONK

SECRET AND PERSONAL

TABLE 2: M3 COMPONENTS - APRIL 1988

"First Guess" compared with average monthly change in the previous year.

£ millions

	First Guess	Average monthly change in previous 12 months
Notes and coins in circulation	- 213	150
Non-interest bearing sight	283	350
Interest bearing sight	959	870
Time deposits (including (CDs)	- 775	1410
Grossing up to full population	33	-
	-----	-----
Change in M3	287	2780
	-----	-----

SECRET AND PERSONAL

TABLE 3 : M3 COUNTERPARTS - APRIL 1988

"First guess compared with average monthly change in the previous year

£ millions

		First Guess		Average change in previous 12 month
CGBR (O) (ex bank deposits)		-1537		-290
Other public sector: LABR) PCBR) OPS debt sales)		912		80
		------		------
Modified PSBR*		-625		-210
CG debt: Gilts	-861		-200	
Treasury bills	72		-10	
National Savings	-180		-170	
CTD's etc.	35		10	
		------		------
Total CG debt sales (-)		-934		-370
External and fc finance of public sector (-)		-92		570
		------		------
Wide over(-)/under(+)funding		-1651		-10
		------		------
Sterling lending to nbps (incl Issue Dept commercial bills)		3927 #		3730
Net private externals **) Residual (includes NNDLS **) and reporting differences))		-1989		-940
		------		------
Change in M3		287		2780
		------		------
(Monthly percentage change)		(0.2%)		(1.6%)
(12 month percentage change)		(18.7%)		(21.0%)

---

* Modified PSBR equals PSBR less OPS debt sales

** For the "first guess", Private Externals and NNDLs cannot be separately identified

\# £5636 million after seasonal adjustment.

SECRET AND PERSONAL

TABLE 3 : M3 COUNTERPARTS - APRIL 1988

"First guess compared with average monthly change in the previous year

£ millions

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CG debt: Gilts	-861		-200	
Treasury bills	72		-10	
National Savings	-180		-170	
CTD's etc.	35		10	
Total CG debt sales (-)		-934		-370
External and fc finance of public sector (-)		-92		570
Wide over(-)/under(+)funding		-1651		-10
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(12 month percentage change)		(18.7%)		(21.0%)

---

* Modified PSBR equals PSBR less OPS debt sales

** For the "first guess", Private Externals and NNDLs cannot be separately identified

£5636 million after seasonal adjustment.

NH6/28M

UNCLASSIFIED

MP

FROM: MISS M P WALLACE
DATE: 12 May 1988

MS V BRONK

cc Miss O'Mara

FIRST GUESS

The Chancellor was most grateful for your minute of 11 May.

MPW

MOIRA WALLACE

90/G.jfw.45/024

CONFIDENTIAL

FROM: T PIKE
DATE: 12 May 1988

1. MISS ~~O'MARA~~ MOM 12/5

2. ECONOMIC SECRETARY

cc PS/Chancellor
Sir P Middleton
Sir T Burns
Sir G Littler
Mr Scholar
Mr Sedgwick
Mr Culpin
Mr Peretz
Mrs Lomax
Mr Grice o/r
Ms Ryding
Mr Hurst
Ms Bronk

File: MAMC C9

M0 FIGURES

The latest weekly figures for M0, covering the second week of May, are attached. They show that the 12 month growth rate of M0 to the latest four week period was 6.1 per cent (5.2 per cent not seasonally adjusted). Annual growth of notes and coin to the latest four week period was also 6.1 per cent (5.3 per cent not seasonally adjusted). The nsa growth rates are still distorted by the timing of Easter last year.

2. The six month annualised growth rate of notes and coin to the latest four week period was 5.1 per cent, compared with 4.8 per cent in April.

T. Pike

T PIKE

TABLE 16

CONFIDENTIAL

M0 : THE WIDE MONETARY BASE

Monthly data	Level £ million (Change in brackets)							Percentage change on previous month		6 month % growth annualised		Percentage change on previous year			
	Notes and Coin (nsa)	Notes and Coin (sa)		Bankers' Deposits	M0 (nsa)	M0 (sa)		Notes(sa) and Coin	M0 (sa)	Notes & Coin (sa)	M0 (sa)	Notes and Coin (nsa)	Notes and Coin (sa)	M0 (nsa)	M0 (sa)
1987 September	15349	15376	(118)	185	15534	15561	(121)	0.8	0.8	7.8	7.0	5.3	5.0	5.2	4.9
October	15299	15456	(80)	203	15501	15659	(98)	0.5	0.6	7.4	7.3	5.1	5.2	5.5	5.6
November	15365	15525	(69)	183	15548	15707	(48)	0.4	0.3	7.4	7.0	4.8	4.8	4.9	4.9
December	16447	15661	(136)	186	16633	15846	(139)	0.9	0.9	7.9	8.5	4.7	4.8	4.2	4.3
1988 January	15458	15620	(-41)	181	15638	15801	(-45)	-0.3	-0.3	6.1	5.3	4.7	4.5	4.8	4.6
February	15353	15659	(39)	124	15477	15783	(-18)	0.2	-0.1	5.3	4.5	5.7	5.7	5.3	5.3
March	15588	15753	(94)	162	15750	15916	(133)	0.6	0.8	5.0	4.6	6.9	6.4	6.4	5.8
April	15797	15826	(73)	229	16026	16055	(139)	0.5	0.9	4.8	5.1	5.8	6.1	5.9	6.2
May (2/4) a	15845	15930	(104)	163	16008	16093	(38)	0.7	0.2	5.3	5.0	5.8	6.3	5.5	6.0
Latest 4 we[illegible] a	15764	15889	(83)	221	15984	16110	(129)	0.5	0.8	5.1	5.4	5.3	6.1	5.2	6.1

Weekly data	Level £ million (Change in brackets)					Percentage change on previous week
	Notes(sa) and Coin		Bankers' Deposits	M0 (sa)		M0 (sa)
April						
6th	15832	(5)	263	16095	(87)	0.5
13th	15775	(-57)	97	15872	(-223)	-1.4
20th	15834	(59)	259	16093	(221)	1.4
27th	15862	(28)	297	16159	(66)	0.4
May						
4th	15948	(86)	160	16108	(-51)	-0.3
11th	15912	(-36)	166	16078	(-30)	-0.2

a Weekly data for the current month so far include estimates for the unbacked note issue. The latest week also includes an estimate for coin.
The changes for the current month so far use as a base the previous full month and the full month a year ago.
The latest four week changes use as a base the four week averaged level four weeks ago and a year ago.

psl/55A

CONFIDENTIAL

BF w meeting - 18/5

FROM: A C S ALLAN

DATE: 13 May 1988

mp

MR PERETZ

cc Sir P Middleton
Sir T Burns
Sir G Littler
Mr Scholar
Miss Noble
Miss O'Mara
Mrs Ryding

USE OF PRUDENTIAL CONTROLS TO RESTRAIN MORTGAGE LENDING

The Chancellor was grateful to you for showing him the work done in this area at the time of abolition of mortgage lending guidance. He wishes to hold a meeting next week to discuss this (without involving the Bank or the Building Societies' Commission at this stage).

2. Before then, he would be grateful if you could let him have the latest available figures for mortgage advances as a percentage of purchase prices, and for the ratio of advances to income.

ACSA

A C S ALLAN

CONFIDENTIAL

Papers please.

From : D L C Peretz
Date : 16 May 1988

CHANCELLOR

cc Economic Secretary
Sir P Middleton
Sir T Burns
Sir G Littler
Mr Scholar
Miss Noble
Miss O'Mara
Mr Ilett
Mr Grice
Mrs Ryding
Mr Pike
Mr Cropper

[PEM thinks meeting worthwhile]

USE OF PRUDENTIAL CONTROLS TO RESTRAIN MORTGAGE LENDING

Sir Peter Middleton had a meeting on Friday to consider what if any ways were available to restrain the growth of lending without using fiscal policy, or interest rates - or putting upward pressure on the exchange rate.

2. He asked me to put together a list categorising possible ideas, to act as background for the meeting that your office has now arranged for Thursday. This is attached. I fear there is nothing that is either new or at all promising.

(not now)

3. I also attach as a percentage of purchase prices, and for the ratio of advances to incomes. Neither ratio seems to have shifted dramatically in recent quarters.

DLCP

D L C PERETZ

Ideas for resolving the interest rate/domestic credit/exchange rate dilemma

1. Use of **prudential** controls. For example, capital ratios for mortgage lending might be increased. There are no prudential grounds for this (mortgage lending is less risky than most other forms of bank/building society lending). The effect would be to divert lending through new mortgage intermediaries, and possibly offshore.

2. **Direct controls** on lending or intermediation. For example banks and building societies might be asked to maintain a ratio of non-interest bearing special deposits against new lending or new deposits (ie reintroduce the corset). The effect, like that of the corset, would be to lead to disintermediation, and to drive business offshore. **Monetary base control**, without a mandatory ratio, does not suffer from this difficulty : but there are other well known problems.

3. **Lending guidance.** Could not be made to work in today's competitive markets. And contrary to Government's philosophy.

4. **Consumer credit tax.** Examined carefully 18 months ago. Would have little effect unless applied to mortgage lending. And problem of interface between individuals and small companies.

5. **Property taxes.** Much of current problem relates to speculative bubble in the property market. Ending of the rates has not helped. The announcement of a new property tax (eg reintroduction of Schedule A) could act to break inflationary expectations in the housing and property market.

[illegible]

6. **Inflow controls,** to hold down exchange rate, or to create two tier interest rates. Looked at all the possibilities exhaustively in 1980/1981. Could not open up an interest rate differential between Euro-sterling and domestic sterling market without exchange controls. Now have no powers.

7. **Interest rate manipulation.** Are currently delaying cuts in national savings rates, in an attempt to hold building society and retail rates up, against fall in wholesale market rates. May be some limited scope here to create, temporarily, a form of "two tier" interest rate. Similarly, might be possible through Bank's money market operations to depress say one week and one month interest rates, without triggering a fall in base rates. Unlikely to be able to sustain this for very long, but might have some temporary effect.

8. **Foreign borrowing in sterling market.** A minor point, but the Bank of England still use COBO to limit the amount of sterling issues by foreign borrowers in the sterling bond market. Such issues are helpful in current circumstances, to the extent that the proceeds are switched out of sterling by the borrowers reducing presusre on the exchange rate; or that they syphon money away from domestic lending.

TABLE 1 : AVERAGE ADVANCE AS A PERCENTAGE OF AVERAGE HOUSE PRICES AND AVERAGE ADVANCE/INCOME RATIOS

		Average advance as a % of average house prices		Advance/income ratio (exc. first time buyers)	
		Building Societies	Banks	Building Societies	
1970		n/a		1.78	
1971		n/a		1.79	
1972		n/a		2.02	- 2
1973		n/a		2.01	
1974		n/a		1.82	
1975		62.6		1.72	
1976		65.8		1.70	
1977		65.1		1.64	
1978		65.5		1.72	
1979		58.6		1.67	
1980		56.7		1.54	— 1½
1981		61.9		1.63	
1982		67.9		1.70	
1983		67.5	n/a	1.79	
1984		68.6	62	1.84	
1985		69.2	63	1.83	
1986		69.5	63	1.92	
1987		67.4	67	1.96	
1987	Q1	68.9	67	1.94	
	Q2	68.3	68	1.95	
	Q3	65.8	67	1.96	
	Q4	66.5	66	1.98	
1988	Q1	67.7	67	n/a	— 2

Sources : col 1 BSA. Figures refer to mortgage completions.

col 2 Bank of England, analysis of bank lending for house purchase. Note the percentages are only approximate, based on estimates of average house prices.

col 3 BSA. Figures for bank mortgage advance/income ratios are not available.

PMP

Passed on to Mr.

FROM: MR M WHEATLEY/MS V F BRONK

DATE: 18 May 1988

AF 19/5

1. ~~MISS~~ O'MARA
2. CHANCELLOR

cc: EST
Sir P Middleton
Sir T Burns
Sir G Littler
Mr Scholar
Mr Peretz o/r
Mr R I G Allen
Mr Grice o/r
Mr Cropper
Mr Gray (No 10 Personal)

We shall want to focus attention on the growth in the money supply where unadjusted measures of both narrow and broad money show a reduction on last month. Unfortunately, this is unlikely to deflect media attention from the seasonally adjusted lending figures which are a new record and well above market expectations.

MOM 18/5

PROVISIONAL MONEY FIGURES - APRIL
(All figures are unadjusted unless specified otherwise)

The provisional money supply figures for April will be published by the Bank at 11.30 am on Thursday 19 May. As usual M3, M4 and M5 broad money figures are subject to revision.

Summary

Monetary aggregates for March (per cent)

	Annual Growth Rate	Previous Month		Six month Growth (annualised)	Monthly Growth Rate	Previous Month
M0	5.9	6.4			1.7	1.8
	6.2	5.8	s.a.	5.1	0.9	0.8
M3	19.3	20.9			0.6	4.9
			s.a.	14.6	1.5	3.2
M4	15.9	16.8			0.6	3.3
			s.a.	12.8	1.0	2.3
M5	15.6	16.6			0.4	3.4
			s.a.	12.3	0.8	2.3

One or 2 pts on briefing. More importantly, I do not agree with X: these [illegible] have underlying (via [illegible]) effects [illegible] figs adversely, & will continue to do so until both prices [illegible] of growth in [illegible] will we see the benefits. This needs to be incorporated in briefing.

Lending

		£ billion			Per cent Growth Rates	
		This Month	Last Month	Average Of Last 6 Months	Annual (Monthly) (unadjusted)	Previous Month Annual (Monthly) (unadjusted)
Banks		4.1	6.0	4.4	26.8 (1.9)	25.2 (2.8)
	s.a.	5.8	4.9	4.5		
Banks and building societies		6.5	7.9	5.9	21.8 (1.8)	20.8 (2.3)
	s.a.	8.2	6.7	6.1		
Building Societies		2.2	2.1	1.6	14.3) (1.5)	13.9 (1.6)

Notes

1. Unadjusted bank and bank and building society lending for April is the largest ever in absolute and annual percentage terms.

Table 2 attached gives the historical growth rates for **M0, M3, M4, M5, NIBM1, M1** and the **wider sterling aggregate.** Tables 3 and 4 (attached) show respectively the components and counterparts, for broad money, together with the average changes over the previous twelve months.

1 Growth of M4 was moderate in April. Its annual rate fell by nearly 1 per cent, bringing it - marginally - under 16 per cent for the first time in five months. The relatively modest growth may, however, reflect the unwinding of earlier special factors which are thought to have boosted growth in January and March. In January there was widespread anecdotal evidence of hard arbitrage inflating bank lending and broad money, consistent with a differential between bill and interbank rates which persisted throughout January. It is not possible to quantify arbitrage from available statistics. The boost to broad money and bank lending will almost certainly have unwound by the end of April although it is more difficult to collect anecdotal evidence of this having happened than it was for the original transactions. There were some reports of

limited further arbitrage in April, working in the opposite direction, so April annual growth rates of broad money and lending may still be inflated marginally by arbitrage effects - but less so than in March.

3 The second factor tending to reduce broad money growth in April was the unwinding of the temporary boost from small investors receiving redemption monies of the 2% Treasury Index-Linked Stock at the end of March. The boost to retail bank deposits in March was thought to be some £½ billion. Growth of retail bank deposits in April at £½ billion (£¼ billion seasonally adjusted) was £½-¾ billion lower than average during the previous 12 months, and this would be consistent with such unwinding.

4 An additional factor which might have reduced broad money growth in April was the £1.5 billion British Gas call in mid-month. Any depressing effect would be expected to be seen mainly in wholesale bank deposits, since the personal sector held less than 1/3 of the shares. Growth in wholesale bank deposits was, however, about average for the previous year after allowing for seasonal factors, so that the effect on broad money was probably small.

5 Retail building society inflows remained strong at £1.7 billion compared with an average of £1.3 billion during the previous year. Societies also raised very substantial wholesale funds, although they repaid £0.1 billion to the private sector (included in M4).

6 M3 growth was comparable to M4 growth in spite of the relatively low bank retail inflows, because building societies held £1.1 billion of the proceeds of their strong retail and wholesale inflows as bank deposits.

7 Moderate growth in broad money occurred despite further record growth in bank and building society sterling lending. No comfort can be drawn from the lower bank lending figure in not seasonally adjusted terms since seasonal influences reducing bank lending in April are well established. They include (i) absence of interest changing (which boosts lending by over £1 billion at end quarters)

and (ii) day of week effects of the particular reporting dates, caused by companies borrowing on Thursdays to make up Friday wage packets. Building society mortgage lending increased by over £2 billion for the second month running, bringing its annual growth rate to 14¼ per cent. Bank and building society sources have suggested that the Budget measures had little impact on lending in April: they consider that changes in home improvement loans relief will have small effects overall, and that the change to single residence relief will not yet have resulted in increased advances. This is consistent with the very high pre-Budget mortgage commitment figures and a further acceleration in commitments in April. Bank lending for house purchase by the clearing banks remained high at £0.7 billion, but no higher than average over the past year.

8 Clearing banks' lending to persons other than for house purchase increased moderately by £0.4 billion - similar to the rise in April last year. But this figure may be depressed to the extent that the personal sector borrowed to pay the British Gas call.

9 Clearing banks' figures give fairly good coverage of the remaining rise in bank lending in April. They suggest that company borrowing, and in particular borrowing by manufacturing industry, was the main contributor to April's acceleration in bank lending. Within this, bank lending to property companies grew less than in recent months. Financial companies also borrowed very strongly in April, in contrast to flat borrowing over the last year. It is known that this was concentrated in lending to securities' dealers, although the reasons for this are not clear.

10 Bank lending to companies and the financial sector may have been understated in April because of the effects of unwinding arbitrage (see paragraph 2). Annual growth should be less distorted than last month, although it may remain a little inflated because of further modest amounts of hard arbitrage which are reported to have occurred in April.

11 High sterling bank borrowing by the private sector was accompanied by large repayments of £2.3 billion of foreign currency bank

borrowing. There is no breakdown of the repayments by sector, but it is known that they were concentrated in several large repayments to Japanese and American banks, suggesting that they were connected with offshore activity unrelated to sterling borrowing. Industrial lending figures in the past have not suggested direct substitution between sterling and foreign currency bank borrowing.

12. Other negative counterparts to the moderate growth of broad money were

(i) overfunding of £1.7 billion reflecting the PSBR surplus and substantial purchases of gilts by the private sector from banks (intervention and the public sector externals were extremely small);

(ii) an increase of £2.2 billion in overseas banks' net sterling deposits; and

(iii) an increase of £1.8 billion in building societies' net non-deposit liabilities reflecting their heavy wholesale issues.

<u>Presentation</u>

The lending figures, particularly in their adjusted form, are likely to be the main focus of attention. It would be unwise to attempt to divert attention to the unadjusted figures, which are only lower because of genuine seasonal factors. Nor have the Budget measures as home improvement loans or multiple mortgage tax relief yet begun to affect the figures. The best course presentationally would be to stress that the increase in lending to the personal sector is relatively modest. The bulk of it is lending to companies. Taken with these lending figures the increase in the ceiling for building society lending, to be announced by a PQ tomorrow, may attract notice. A defensive line is included in the press briefing.

X

MW Vyvien Bronk

MR M WHEATLEY/MS V F BRONK

TABLE 2

SECRET

£ million

GROWTH RATES OF MONETARY AGGREGATES

			1987 JUNE	JULY	AUG	SEP	OCT	NOV	DEC	1988 JAN	FEB	MAR
M0 -	Monthly change	sa	24	189	39	120	99	49	139	-46	-18	133
	Monthly % change	nsa	-0.6	2.8	0.1	0.1	-0.2	0.3	7.0	-6.0	-1.0	1.8
	Monthly % change	sa	0.2	1.2	0.3	0.8	0.6	0.3	0.9	-0.3	-0.1	0.8
	6-month annualised % change	sa	0.2	4.0	6.2	7.0	7.3	7.0	8.5	5.3	4.5	4.6
	Annual % change	sa	4.2	5.4	4.7	4.9	5.6	4.9	4.3	4.6	5.3	5.8
M3 -	Monthly change	nsa	1907	4262	2220	1670	5690	1256	2580	-2159	546	8967
	Monthly % change	nsa	1.1	2.5	1.3	1.0	3.2	0.7	1.4	-1.2	0.3	4.9
	Monthly % change	sa	1.4	2.2	1.4	1.4	3.6	0.0	1.4	0.5	0.4	3.2
	6-month annualised % change	sa	24.2	26.5	25.2	21.9	25.5	21.8	21.7	17.7	15.6	19.5
	Annual % change	nsa	19.2	21.0	22.2	19.6	22.4	21.5	22.8	22.3	20.4	20.9
M4 -	Monthly change	nsa	4042	5347	2679	2992	5367	1577	4899	295	1253	9971
	Monthly % change	nsa	1.5	1.9	0.9	1.0	1.8	0.5	1.6	0.1	0.4	3.3
	Monthly % change	sa	1.5	1.6	1.3	1.2	2.2	0.3	1.3	0.3	1.0	2.3
	6-month annualised % change	sa	15.8	18.9	18.4	17.2	18.8	17.3	16.8	13.9	13.1	15.5
	Annual % change	nsa	13.9	15.0	15.6	15.0	15.8	15.2	16.3	16.5	16.0	16.8
M5 -	Monthly change	nsa	4126	5481	2793	3055	5500	1531	5209	-25	978	10904
	Monthly % change	nsa	1.4	1.8	0.9	1.0	1.8	0.5	1.7	0.0	0.3	3.4
	Monthly % change	sa	1.5	1.5	1.3	1.2	2.1	0.3	1.3	0.3	0.8	2.3
	6-month annualised % change	sa	15.2	18.5	17.9	17.0	18.9	16.7	16.3	13.7	12.7	15.3
	Annual % change	nsa	13.5	14.4	15.0	14.4	15.2	14.7	15.8	16.3	15.5	16.6
NIBM1 -	Monthly change	nsa	1444	82	-93	384	184	493	391	-1523	874	2254
	Monthly % change	nsa	3.4	0.2	-0.2	0.9	0.4	1.1	0.9	-3.3	2.0	5.0
	Monthly % change	sa	4.2	0.2	0.3	0.7	3.4	-2.2	-0.2	3.3	1.5	1.4
	6-month annualised % change	sa	15.3	9.9	9.7	13.3	24.1	13.8	4.3	10.8	13.3	14.9
	Annual % change	nsa	13.1	11.9	11.8	5.6	11.4	10.1	9.9	11.4	12.2	14.8
M1 -	Monthly change	nsa	2102	1083	1104	1579	2864	508	-258	-1106	-416	5427
	Monthly % change	nsa	2.5	1.3	1.3	1.8	3.2	0.6	-0.3	-1.2	-0.5	6.0
	Monthly % change	sa	2.8	1.3	1.6	1.6	4.8	-1.0	-1.0	2.2	-0.6	3.9
	6-month annualised % change	sa	30.4	24.4	28.2	23.0	36.0	24.7	15.6	17.5	12.5	17.6
	Annual % change	nsa	23.6	22.6	23.7	20.4	24.7	21.7	22.7	21.7	20.5	20.7
WIDER £	Monthly change	nsa	531	5243	1412	1828	7689	4	3505	516	188	8595
AGGREGATE	Monthly % change	nsa	0.3	2.7	0.7	0.9	3.8	0.0	1.7	0.2	0.1	4.0
	Monthly % change	sa	0.5	2.4	0.8	1.3	4.1	-0.6	1.6	1.7	0.2	2.5
	6-month annualised % change	sa	22.4	23.5	21.9	20.2	24.9	18.2	20.9	19.2	17.8	20.7
	Annual % change	nsa				18.6	22.3	20.4	21.5	21.6	19.9	20.6

SECRET AND PERSONAL

TABLE 3:PROVISIONAL BROAD MONEY COMPONENTS

£ million

	APRIL	Average growth in 12 months to March
Notes and coins in circulation (nbps)	-251	145
Bank deposits (nbps)		
Retail		
non-interest bearing	156	362
interest bearing	654	455
Wholesale	653	1821
Change in M3	1212	2783
Building society holdings of M3	-1098	-370
Buildings society deposits (nbnbsps)		
Retail	1761	1300
Wholesale	-123	72
Change in M4	1752	3785
Money market instruments (nbnbsp	-369	54
National Savings Bank (nbnbsps)	71	94
Change in M5	1454	3933

nbnbsps = non-bank,non-building-society private sector

TABLE 4: PROVISIONAL BROAD MONEY COUNTERPARTS

April 1988 (£ million)

	M3	M4	M5
1. PSBR	-1001	-1001	-1001
2. Debt sales to private sector (-)			
Gilts	-760	-643	-643
Treasury bills	49	49	
National Savings	-157	-157	-86
CTD's	37	37	
Other CG debt	-6	-6	-6
LA and PC debt	177	116	65
3. External finance of public sector (-)	-53	-53	-53
4. Public sector contribution (1+2+3)	-1714	-1658	-1724
5. Sterling lending to private sector	4128	6453	6221
6. Externals	-1384	-1427	-1427
7. £NNDLs	182	-1616	-1616
8. Total change (4+5+6+7)	1212	1752	1454
(Percentage change)	(+0.6)	(+0.6)	(+0.4)

Average growth in previous 12 months (£ million)

	M3	M4	M5
1. PSBR	-290	-290	-290
2. Debt sales to private sector (-)			
Gilts	-204	-238	-238
Other public debt	-80	-154	-13
3. External finance of public sector (-)	573	573	573
4. Public sector contribution (1+2+3)	-1	-109	32
5. Sterling lending to private sector	3725	5046	5053
6. Externals	-565	-641	-641
7. £NNDLs	-375	-511	-511
8. Total change (4+5+6+7)	2784	3785	3933
(Percentage change)	(+1.6)	(+1.3)	(+1.3)

MONEY SUPPLY IN APRIL: PRESS BRIEFING

A. FACTUAL

(i) **Changes in main monetary aggregates**

per cent

	M0	M3	**M4**	M5
12 month growth rate	**+5.9** **(+6.2)**	+19.3 (+19.9)	**+15.9** **(+15.8)**	+15.6 (+15.5)
Annualised six-month growth	**(+5.1)**	(+14.6)	**(+12.8)**	(+12.3)
one month change	**+0.6** **(+0.9)**	+ 0.6 (+ 1.5)	**+0.6** **(+1.0)**	+ 0.4 (+0.8)

(Figures in brackets seasonally adjusted s.a.)

(ii) MO

Figures (+5.9 and +6.2 s.a.) above target range, but FSBR recognised this was likely.

(iii) **Broad money**

(a) 1, 6 and 12 month growth rates. M3 and M4 below levels of March.

(b) But 3 month growth rates returning to levels of mid 1987-88.

(c) M4 gives less erratic signals than M3. Hence MTFS' emphasis on measures including liabilities of building societies as well as banks.

(iv) Lending

(a) Should not read too much into individual counterparts, which are hard to interpret.

(b) One month changes: unadjusted bank lending lower than March, adjusted higher and at record levels.

	Bank and building society lending		Bank lending	
	£ billion	%	£ billion	%
February	+3.9 (+4.2)	+1.1 (+1.2)	+2.5 (+2.6)	+1.2 (+1.2)
March	+7.9 (+6.7)	+2.3 (+2.0)	+6.0 (+4.9)	+2.8 (+2.6)
April	+6.5 (+8.2)	+1.8 (+2.3)	+4.1 (+5.8)	+1.9 (+2.6)

(Figures in brackets seasonally adjusted)

(d) 12 month growth rates (unadjusted). Bank and building society lending and bank lending both show record growth rates.

	Bank and building society %	Bank
November	+19.0	+22.5
December	+18.8	+22.8
January	+20.0	+24.7
February	+19.9	+24.3
March	+20.8	+25.2
April	+21.8	+26.8

(e) Approximate breakdown of increase in clearing banks advances in April. Bulk of increase is for companies, not for personal sector:

	£ billion	
Manufacturing	+0.8	
Business and other services	+0.5	
Financial companies	+1.0	
Personal sector	+1.0	
of which house purchase		+0.6
consumption		+0.4
Other bank lending	+0.8	

(v) **Funding.** Overfund (on new, M4 definition) in April of £1.4 billion. PSBR April 1988 a surplus of about £1.7 billion

(vi) **Monetary Policy - Recent Statements**

(a) **Chancellor in Mansion House speech 4 Nov 1987**

"To prevent there being excessive liquidity in the economy, our policy is to ensure that, over time, any net intervention is sterilized - in other words, fully funded."

(b) **Chancellor in Autumn Statement debate (14 January)**

"Keeping the economy on track involves keeping a constant watch on all the indicators of how the economy is developing and then taking action as necessary. I have never hesitated to act in the past when I have judged that there was a risk to our inflation objectives. I can assure the House that I shall not hesitate to do so in future. It is precisely by acting promptly that we have been able to avoid the need for drastic and destabilising lurches in policy. Our track record speaks for itself."

(c) **Chancellor on interest rates (Budget speech, 15 March)**

"Short term interest rates remain the essential instrument of monetary policy. Within a continuous and comprehensive assessment of monetary conditions, I will continue to set interest rates at the level necessary to ensure downward pressure on inflation."

(d) **Chancellor on exchange rates (Budget speech, 15 March)**

"Exchange rates play a central role in domestic monetary decisions as well as in international policy co-operation. I believe that most businessmen have welcomed the greater exchange rate stability over the past year. It is important that they also accept the financial discipline inherent in this policy."
(Also see MTFS, 2.11)

(e) **Chancellor on inflation and exchange rates (This Week Next Week interview, 24 April).**

"Our ultimate aim is certainly the total eradication of inflation."

"We are certainly interested in the maximum possible exchange rate stability, within the context of sound anti-inflationary policy."

(f) **Prime Minister on anti-inflation strategy, exchange rates and interest rates, House of Commons 17 May**

"My rhf [Chancellor] and I entirely agree that we must maintain a firm monetary policy and a downward pull on inflation. I totally agree with my rhf's Budget speech, every bit of it ..... Exchange rate policy ..... is a part of total economic policy .... we have taken interest rates down three times in the last two months. That was clearly designed to affect the exchange rate. We use the available levels, both interest rates and intervention, as seems right in the circumstances .... It would be a great mistake for any speculator to think at any time that sterling was a one-way bet"

r

"As the value of sterling has risen, that is the exchange rate has risen, that has tightened money supply, which enables us to reduce the interest rate without having any adverse effect on inflation."

This is not strictly correct: tighter XR tightens monetary conditions, not money supply

B. POSITIVE

?

~~(i) **Monetary policy**: Prime Minister and Chancellor entirely agree (Prime Minister in House 17 May) "must maintain firm monetary policy and downward pressure on inflation."~~

~~(ii) **Increases in domestic costs**: Will not be accommodated either by monetary expansion or by exchange rate depreciation.~~

No positive briefing req'd on this occasion

C. DEFENSIVE

(i) Lending

(a) **Why bank and building society lending so high?** Bulk of increase to companies which are switching from equity financing to bank borrowing; within increase in lending to personal sector, bulk for house purchase, not consumption.

(b) **Lending figures show overheating? Why cut interest rates on 17 May?**

- If anything, latest figures from real economy [index of production and figures on capital investment] show some slight slowing in growth (though indicators are mixed). CBI quarterly survey shows "few signs of overheating".

- Judgement of monetary conditions and inflationary pressures must take account of whole range of factors, including downward pressure on inflation from exchange rate.

- Experience of number of years shown that high rate of growth of lending and liquidity consistent with lower inflation because increased liquidity willingly held ie held as savings rather than for spending.

- No sign of resurgence of inflation.

(c) **Lending figures inconsistent with indicators from real economy? [Index of production and capital investment].** Real economy figures show mixed picture. In any case, would not expect historical figures to be affected by April lending. CBI April Quarterly Survey said investment intentions strengthened considerably.

(d) Consumer credit boom?

- No evidence that rate of lending to consumers accelerating in recent months: 12 month growth rate close to its average since 1982 of 18 per cent. (Some credit simply displacing cash and cheque payments - over 40 per cent of credit card users pay no interest.)

- Vast bulk of personal borrowing takes form of mortgages, which represented 2/3 of outstanding personal debt at end of 1987. Mortgage lending accounts for almost half of all of bank and building society lending. Increase overall as percentage of GDP in 1980s mainly attributable to growth in mortgage borrowing, as result of 2½ million increase in households buying own home.

- Consumer credit only some 15 per cent of total personal debt. Less than 5 per cent of personal debt takes form of credit card lending (including interest-free component). (See Chancellor's speech to FHA, 17 June 1987).

(e) **Why not impose controls on lending?** Not right to restrict growth by quantitive controls: lenders and borrowers should be free to make own decisions. Nor would such controls be effective.

(f) **Should not effects of unwinding of arbitrage from January have depressed bank lending figures?** Possibly, but do not know precisely how much to expect. Easier to detect arbitrage when it is happening than when unwinding.

(g) **Why increase ceiling for building society unsecured lending [from £5,000 to £10,000] when lending already so high?**

[Orders laid today (Thursday) to extend range of building society activities. PQ foreshadowed future order which will raise ceiling for unsecured lending from £5-10,000].

Not a new announcement. EST announced in February. No reason to expect increased limit to lead to any significant growth in overall consumer credit. Societies will replace other credit sources, and right they should be given greater scope to compete for retail customers. Building Societies Commission will ensure that societies continue to have adequate credit assessment and control procedures in place. Societies also subject to overall limit on new assets: includes unsecured lending. Mortgage lending for house purchase will continue to be bulk of business.

[See also separate FIM briefing].

(ii) **Money Supply**

(a) **M0 growth outside target range? Won't Tuesday's interest rate cut make this worse?** 1988-89 FSBR chapter 3 recognised that 12-month growth may move to top of or outside 1-5 per cent target range in early part of 1988-89 but should be within range later in year. Six-month growth rates (annualised) currently below 12-month rates.

(b) **M4 (and M3) still rising fast?** After large rises in March, slower rise in April.

(c) **Significance of broad money.** No explicit broad money target in 1988-89. But growth of broad money still taken into account. See MTFS 2.09 and 3.11.

(iii) Prime Minister's statement 17 May

(a) **Prime Minister's statement 17 May "papering over the cracks"?** No. Prime Minister indicated absolute support for Chancellor. Said she agreed with all of Budget speech, which included clear statement of policy on monetary policy, exchange rate etc.

(b) **After interest rate cut on 17 May, Government running out of ammunition to hold down exchange rate?** ~~Not at all.~~ Prime Minister ~~referred to both interest rates and intervention and, as~~ reminded House, that sterling not a one-way bet. and made clear that "we use available levers, both interest rates and intervention, as seems appropriate".

(c) **Interest rate cut to bring down sterling or because level of sterling made it safe to do so without loosening monetary conditions?** False dichotomy. Decision taken in light of all relevant factors.

(d) **Intervention inflationary?** Only poses inflationary threat if not funded. 1987-88 intervention was fully funded. Within financial year.

(e) **BEQB said current combination of high exchange rates and low interest rates not ideal and different balance would be desirable. Hasn't interest rate cut made this worse?** BEQB referred to an ideal policy mix. But Government has to act in light of market conditions at the time. Overall ~~tightness?~~ ~~stance~~ (tightness) of policy remains appropriate. ~~and monetary conditions continue to bear down on inflation.~~

(f) Why cut interest rates rather than intervene? As Prime Minister said, use available levers - interest rates and intervention - as seems right in circumstances.

(iv) Further movements in interest rates? Intervention? Never discuss market tactics. As Prime Minister said, anyone asking to know what will happen is aiding and abetting speculator.

(v) UK's real interest rates out of line with competitors? Deflating current three month money rates by recent price indices suggest UK only just above G7 average.

(vi) Change to funding rule. From start of 1988-89 building societies treated same as banks, so gilt sales to building societies will no longer count towards full fund. No relaxation of monetary policy. Including building societies with banks recognises their evolving status.

2510B SECRET 18. 5.88

THE GOVERNOR'S PRIVATE SECRETARY	HO-P
THE DEPUTY GOVERNOR	HO-P
MR GEORGE	HO-P
MR LOEHNIS	HO-P
MR COLEBY	HO-P
MR FLEMMING	HO-P

Economics Division

MR TAYLOR	HO-4
MR MIDGLEY	HO-4
MR SHEPPARD	HO-4

From: C R Mann

Financial Statistics Division

MR BULL	BB-1
MR PENNINGTON	BB-1
MR THORP	BB-1
MR M ST J WRIGHT	BB-4

Foreign Exchange Division

MR FOOT	HO-1

Money Markets Operations Division

MR ALLEN	HO-G
MR BRIAULT	HO-G
MR JONES	HO-G

Gilt-Edged Division

MR PLENDERLEITH	HO-G
MR MORTIMER-LEE	HO-G
MR HOPTON	HO-G

Wholesale Markets Supervision Division

MR TOWNEND	HO-G

Information Division

MR WARLAND	HO-1
MR INGRAM	HO-1
MR MATHESON	HO-1

HMT

MISS O'MARA
MS RYDING
MR PERETZ

PRESS STATEMENT: APRIL BANKING AND MONEY FIGURES
£ million

1 The preliminary monetary aggregates press release for April will be published by the Bank at 11.30 am on Thursday. A copy of the press release is attached. Figures for member bank groups will be published by the CLSB at the same time. The full banking and money supply figures will be published on Tuesday, 31 May.

2 The growth in bank and building society lending in April sets new records, and credit growth will again be the main focus of attention.

3 This note begins with the usual one-page summary, in the form of an aide-memoire, with references to the more detailed discussion which follows.

Financial Statistics Division
18 May 1988

C R Mann (4427) BB-1 CRM

APRIL MONEY PRESS RELEASE: AIDE MEMOIRE

(References are to the detailed discussion attached)

1 M3 + 1.5% s/a, M4 +1.0% sa in April, fairly buoyant despite the call on British Gas shareholders (paras 1, 2).

2 M0 +0.9% s/a (+1.7% u/a) in April, partly reflecting a large increase in bankers' balances. 12-month growth rate +5.9% (u/a), down from +6.4% in March, but distorted downwards by timing of Easter. Seasonally adjusted 12-month growth rate +6.2%. Both outside the 1988/89 target range. (Para 2a).

3 Overfunding, including:

(i) PSBR -£0.9 bn nsa
A large surplus, reflecting the call on British Gas shareholders and repayment of British Gas debentures (£1.8 bn in total) (para 4).

(ii) Nbps gilts purchases of £0.8 bn and overseas gilts purchases £0.3 bn, mainly from the banks. (para 5).

4 Bank lending +£5.8 bn sa (+2.6%), comparable with January's record +£5.6 bn (+2.7%). Bank and building society lending +£8.2 bn sa (+2.3%), even higher than the previous record in January (£7.1 bn, +2.1%) (para 9).

(i) Little sign of arbitrage undertaken in January unwinding in April (para 10).

(ii) Building societies may still be capturing market share from banks in the mortgage market (para 12). Total bank and building society lending for house purchase is still buoyant (causing M4 lending to grow).

(iii) Company sector continues to be the main borrower from banks (industry detail para 13).

(iv) GEMMs borrow £0.5 bn - partly temporary; partly working capital (para 13).

5 Other Issues

The Budget and monetary policy - para 15 (Greater emphasis placed on M4 in 1988/89 including the use of the M4-funding rule, but we continue to monitor and publish M3, M4 and M5)

Overfunding in the last 12 months depresses the 12-month growth rates of M3, M4 and M5 (para 2e).

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* Much of this information remains SECRET indefinitely (eg where it refers to individual banks or their customers).

APRIL MONEY PRESS RELEASE: DETAILED DISCUSSION

£ million, not seasonally adjusted (unless otherwise stated)

The aggregates

1 The growth rates of the main aggregates are summarised below.

% changes		M0 (1)	M1	M2	M3	M4	M5
Apr	(nsa)	+1.7	+ 1.0	+ 0.7	+ 0.6	+ 0.6	+ 0.4
	(sa)	+0.9	+ 1.0	+ 0.7	+ 1.5	+ 1.0	+ 0.8
12 months to							
Apr	(nsa)	+5.9	+20.9	+13.1	+19.3	+15.9	+15.6
	(sa)	+6.2	+21.9	+12.9	+19.9	+15.8	+15.5
12 months to							
Mar	(nsa)	+6.4	+20.7	+13.5	+20.9	+16.8	+16.6
	(sa)	+5.8	+20.3	+12.7	+20.7	+16.3	+16.2

(1) Calculated as an average of Wednesdays in the month.

The target for M0 in 1988/89 set in the Budget is 1%-5%. There is no explicit target for broad money.

2 There are several points to note about these figures.

(a) As expected, M0 starts the year outside its target range. Because of the different timing of Easter in 1987 and 1988, the 12-month unadjusted growth rate in April is understated. The seasonally adjusted 12-month growth rate in April (which removes this timing distortion) is +6.2%. Bankers' balances increased strongly in April, accounting for almost half of the growth in M0. But over the last 12 months bankers' balances have grown very little, so that the underlying 12-month growth rate of M0 (as measured by the seasonally adjusted growth in the note circulation alone) is +6.1%, down a little from last month's figure of +6.4%.

(b) The final call of £1.5 bn on British Gas shareholders ought to have had a depressing effect on bank and/or building society deposits, at least as far as "small" shareholders are concerned. However, small shareholders only accounted for about 20% (£0.3 bn) of the payment, so it may not be surprising that none of the categories of retail bank and building society deposits is significantly below trend. The share premium provided an incentive for illiquid shareholders to finance the payment by bank borrowing, but since the increase in personal borrowing from CLSB banks was not unusually high, this effect is likely to be small. It is not known how the "large" shareholders financed their payment, but the presumption must be that bank deposits were affected, since we do know that deposits fell unusually strongly in the middle of April at the time of the payment.

(c) Within M4, there was a large rise of 1,990 (s/a) in retail deposits. This included 50 (s/a) of non-interest-bearing bank deposits, some 360 (s/a) of inflows to banks' interest-bearing retail accounts in M2, and 1,580 (s/a) of inflows to share and deposit accounts with building societies. For the banks, the inflow is £0.4 bn lower than the average of the previous 6 months; but for the societies the inflow is £0.2 bn higher.

(d) Wholesale deposits within M4 rose by 1,440 (s/a), almost entirely concentrated in M3. This is close to the average of £1.4 bn per month over the preceding six months. There is no evidence here to support the theory that arbitrage undertaken in earlier months is now unwinding (see para 10 below), particularly if one bears in mind that this is the category of deposits most likely to be depressed by the British Gas call. Building societies' own bank deposits (included in M3 but not in M4) rose by 1,130 (s/a).

(e) The 12-month growth rates of M3, M4 and M5 are probably distorted by the erratic path of overfunding last year and this. Over the last 12-months cumulative overfunding has been 4,960 and 5,550 on the M3 and M4 bases respectively. This will have had a depressing effect on the 12-month growth rates of M3 and M4, though not necessarily one-for-one as there will have been effects on other counterparts too. If the effect were one-for-one, the "underlying" 12-month seasonally adjusted growth rates of M3 and M4 would be 22.8% and 17.7% respectively.

Counterparts to the aggregates

		Counterparts to:		
April	£ million nsa	M3	M4	M5
A	PSBR	-1,003*	-1,003*	- 1,003*
B	CG debt sales (-)	- 838	- 721	- 736
C	LA & PC debt sales (-)	+ 177	+ 116	+ 65
D	External & FC finance of public sector	- 55	- 55	- 55
E = A+B+C+D	Overfunding (-)	-1,719	-1,663	- 1,729
	(memorandum item: s/a)	(-1456)	(-1420)	(-1,803)
F	Sterling lending	+4,131	+6,456	+ 6,227
G	Banking/B Soc externals	-1,396	-1,439	- 1,439
H	£ net non-deposit liabilities	+ 197	-1,601	- 1,601
I = E+F+G=H	(the aggregate)	+1,213	+1,753	+ 1,458

*our press release shows -£0.9 bn so as to agree with yesterday's PSBR press release. The figure shown here is more up to date.

3 Amongst the counterparts to money in the press release, only sterling lending is shown in seasonally adjusted form; the split of the "other counterparts" between the externals and £NNDLs (G and H above) is not shown, nor is the split of public sector debt sales between CG, PCs and LAs (B and C above).

4 The PSBR was in surplus, reflecting the final payment for British Gas shares and the repayment of some British Gas debentures which together brought in £1.8 bn. In seasonally adjusted terms (not published) the PSBR was in surplus by 1,660.

5 Nbps gilts holdings rose by 760 (within which building society holdings rose by 120) and overseas holdings rose by 340. These increases in holdings were largely due to sales of gilts by the banks, as net official sales by the authorities were only 200. National Savings receipts were 160. CTD surrenders were 40 (in seasonally adjusted terms there were net surrenders of 170); the rates offered on new issues were uncompetitive, at least in comparison with the expiring rates on year-old CTDs.

6 The banking external counterparts were strongly contractionary; the overseas sector were net depositors in sterling by £2.2 bn, offset in its effect on M3 and M4 by a fall of £1 bn in banks' net foreign currency deposit liabilities (ie banks were switching out of sterling).

7 Banks' £NNDLs were little changed, but building societies built up non-deposit liabilities, partly through the normal seasonal tax accruals and build-up of interest accrued but not yet paid out to depositors, and also through the issue of long-term bonds excluded from M4.

8 The M4-funding definition is now in operation (see para 15). Building societies' gilts holdings rose by only 120, so the M3- and M4-funding figures are not much different in April.

Bank and building society lending

9 The seasonally adjusted sterling bank lending increase of 5,840 (s/a) or 2.6% is yet another new record in nominal terms, though just below January's record 2.7% in percentage terms. The 3, 6 and 12-month growth rates continue to be well above 25%. Bank and building society sterling lending (ie the M4 lending counterpart) increased by 8,190 (s/a) or 2.3%. This is a record, exceeding the previous record increase of 2.1% in January. Within this, building society lending was very strong at 2,240 (s/a), also a record increase though mortgages alone were higher in March. Banks' foreign currency lending to the nbps fell strongly by 2,410 in transactions terms and the "bill leak" also fell by 140, but the M5 lending counterpart (which includes the non-building society part of the bill leak) also showed a record increase.

The M4 lending counterpart in the first quarter of 1988 shows an acceleration over 1987 growth:

	Sterling lending		Sterling and currency lending
£ billion, seasonally adjusted	M3 counterpart (banks) (1)	M4 counterpart (banks + societies) (2)	(M4 counterpart + banks FC lending to the nbps) (3)
1987 Q1	+ 6.9 (+4.0%)	+10.6 (+3.8%)	+17.7 (+5.4%)
Q2	+ 8.8 (+5.0%)	+13.4 (+4.6%)	+18.1 (+5.3%)
Q3	+11.4 (+6.2%)	+14.8 (+4.9%)	+13.6 (+3.8%)
Q4	+11.2 (+5.7%)	+14.1 (+4.4%)	+14.0 (+3.8%)
1988 Q1	+13.0 (+6.3%)	+18.1 (+5.4%)	+19.9 (+5.2%)
12 months to:			
Dec 87	+38.3 (+22.5%)	+52.8 (+18.8%)	+63.3 (+19.5%)
Mar 88	+44.4 (+25.1%)	+60.3 (+20.7%)	+65.5 (+19.3%)
Apr 88	+48.1 (+26.9%)	+64.6 (+22.0%)	+66.2 (+19.3%)
month changes:			
Jan 88	+ 5.6 (+ 2.7%)	+ 7.1 (+ 2.1%)	+ 7.9 (+ 2.1%)
Feb 88	+ 2.6 (+ 1.2%)	+ 4.2 (+ 1.2%)	+ 3.2 (+ 0.8%)
Mar 88	+ 4.9 (+ 2.3%)	+ 6.8 (+ 2.0%)	+ 8.9 (+ 2.3%)
Apr 88	+ 5.8 (+ 2.6%)	+ 8.2 (+ 2.3%)	+ 5.8 (+ 1.4%)

10 Within the total of bank lending, bill finance fell by 460, but this is more than accounted for by switching by customers of one bank from bill finance to loan facilities. There is no firm evidence to suggest that unwinding of arbitrage activity in earlier months has had a depressing effect on bank lending in April. Such unwinding would have been of 3-month bills drawn in January. Any unwinding that did occur may have been masked by some new arbitrage, particularly when bill rates were depressed in the middle of April; but the opportunities in April were much less in January, so we would still expect a net unwinding in April.

11 As explained in para 2(b) above, it is possible that some British Gas shareholders financed the payment of the final call by borrowing. However, personal borrowing from the CLSB banks was not unusual, so this effect is likely to be small.

12 Lending for house purchase by both banks and building societies was once again strong. Other lenders report only quarterly, in arrears:

£ million, s/a	Banks	Societies	Others	Total
Quarterly Flows:				
1987 Q1	1,718	3,716	756	6,190
Q2	2,406	3,697	887	6,990
Q3	2,959	3,682	1,282	7,923
Q4	2,958	3,977	1,508	8,443
1988 Q1	2,576	5,370	1,200*	9,146
Amounts Outstanding				
1988 Q1	38,034	137,518	17,150*	192,702
Monthly Flows:				
1988 Jan	495ø	1,652	n/a	
Feb	487ø	1,481	n/a	
Mar	987ø	2,237	n/a	
Apr	651ø	2,146	n/a	

* partly estimated ø CLSB banks only, not seasonally adjusted

In the first quarter of 1988 societies clearly regained market share at the expense of the banks and other lenders, and this trend seems likely to have continued in April. Total mortgage lending remains very buoyant although it is not year clear whether Budget effects have begun to come through (ie home improvement borrowing arranged before 5 April, double-tax-relief mortgages being arranged before August, as well as general effects of increased personal income).

13 In the composition of bank lending by instrument, the main increase in April was in loans and advances (£5.0 bn), partly offset by a fall in bill finance (-£0.5 bn). The CLSB coverage is reasonably good (75% of total advances, and 65% of bill finance -in total they account for 80% of lending). There has been some switching of corporate lending from non-CLSB banks to CLSB banks, so not all the inflows to CLSB will explain the increase in total bank lending. The detailed CLSB analysis shows personal borrowing

of 650 for house purchase and 390 for consumption. The latter compares with 360 last April and seems to be in line with past seasonal patterns (we do not have a long enough run of figures to construct proper seasonal adjustments); the underlying rate of CLSB consumer lending does not seem to have changed in the past year. Total borrowing by financial companies (advances plus acceptances) was 1,010, largely accounted for by securities dealers who borrowed 830. Within the latter, we know that GEMMs borrowed some 500 (about £0.2 bn of this is temporary and should unwind in May; another £0.2 bn is working capital to buy gilts). Lending to the company sector was buoyant at 1,240. The largest movement (advances plus acceptances) was an increase of 790 in manufacturing industry (of which "food, drink and tobacco" +240, the remainder being widely spread amongst other categories of manufacturers). This is the largest single monthly increase in CLSB lending to manufacturing industry for many years, but there does not seem to be any particular explanation for it (except, perhaps, switching from non-CLSB banks). Property companies borrowed "only" 190 this month (a 2% increase). Taken together with the analysis of lending for the three months to end February and the March outturns, these figures continue to suggest that it is the non-financial company sector which has caused the acceleration in bank borrowing in recent quarters.

14 Almost all of the fall of 2,410 in foreign currency borrowing took place outside the CLSB groups. We have identified a fall of £1.1 bn in lending to Japanese companies operating in the UK by two Japanese banks, which seems to be the unwinding of temporary lending last month. We have also noted falls in lending of some £0.5 bn to non-bank Channel Islands subsidiaries of American banks, and some £0.3 bn to securities dealers.

The Budget and monetary policy

15 Amongst the broad money aggregates, greater emphasis is now given to M4 (the only broad aggregate to be mentioned by name in the "Red Book"). It is stated that it is sensible to concentrate on measures of broad money that include both bank and building society deposits because of the increasing overlap between the two sectors' activities. Although the M4-funding definition is not

mentioned by name, the MTFS states that "The authorities will seek to fund the net total of maturing debt, the PSBR, and any underlying change in foreign exchange reserves, by sales of debt outside the banking and building society sectors". M4 and M5 were introduced in the May 1987 Bulletin; in that Bulletin article it was pointed out that there can at present be no unique definition of broad money, because of developments in the financial system and substitutability between assets included in and excluded from the various aggregates. For these reasons we shall continue to monitor and publish M3, M4 and M5.

Secret until 1130 a.m. 19/5/88

Provisional estimates of monetary aggregates: April 1988

1 Provisional information suggests the following:

% changes		M0	M3	M4	M5
12 months to April (not seasonally adjusted)		+5.9	+19.3	+15.9	+15.6
April	- not seasonally adjusted	+1.7	+ 0.6	+ 0.6	+ 0.4
	- seasonally adjusted	+0.9	+ 1.5	+ 1.0	+ 0.8

2 Provisional counterparts to the changes in M3, M4 and M5 are:

£ billions, not seasonally adjusted	M3		M4		M5	
	April	latest 12 months	April	latest 12 months	April	latest 12 months
A PSBR	–0.9	- 6.4	–0.9	- 6.4	- 0.9	- 6.4
B debt sales to private sector (–) (1)	–0.7	- 4.1	–0.6	- 4.7	–0.7	- 3.0
C external flows to public sector (–)	0.1	+ 5.6	0.1	+ 5.6	–0.1	+ 5.6
D public sector contribution (A+B+C)	–1.7	- 4.9	–1.6	- 5.5	–1.7	- 3.8
E sterling lending (2)	+4.1	+47.7	+6.5	+64.2	+6.2	+63.9
F other counterparts (3)	–1.2	–11.3	–3.1	–15.0	–3.1	–15.0
Total (D+E+F)	+1.2	+31.5	+1.8	+43.7	+1.4	+45.1
Sterling lending (seasonally adjusted)	+5.8		+8.2		+8.0	
(average of previous 6 months)	+4.0		+5.4		+5.4	

(1) Sales of public sector debt to the private sector other than banks (and, for M4 and M5, building societies), with an adjustment in the case of M5 for private holdings of certain liquid government debt.

(2) Lending by the monetary sector (and, for M4 and M5, by building societies) to the rest of the private sector. For M5, an adjustment is necessary for private holdings of certain money-market instruments etc.

(3) External and foreign currency transactions and net non-deposit liabilities of banks (and, for M4 and M5, of building societies).

3 The PSBR was reduced in April by privatisation proceeds totalling some £1.8 billion, reflecting receipt of the final payment for British Gas shares and repayment of some British Gas debentures.

4 Full money and banking figures for April, including revised estimates of the figures given above, will be published on 31 May.

Bank of England
19 May 1988

91G.SCB.14.20

SECRET AND PERSONAL
UNTIL 11.30 AM THURSDAY 19 MAY 1988

FROM: M H WHEATLEY
DATE: 19 May 1988

MR R I G ALLEN

cc:
PPS
PS/Chief Secretary
PS/Economic Secretary
Sir P Middleton
Sir G Littler
Sir T Burns
Mr Scholar
Mr Peretz
Mr Grice
Miss O'Mara
Mr Pickford
Mrs Ryding
Mr Pike/Ms Bronk
Mr Cropper
Mr Bush

APRIL: PROVISIONAL MONEY FIGURES

I attach the press briefing for today's provisionals. I have sidelined the amendments.

2. There have been only slight changes to the main figures circulated in my minute yesterday.

3. I also attach the Bank's Press Notice and the regular monthly statement of the London and Scottish Banks. Questions on this should be directed to the CLSB press office (01-626-8486).

MW

M H WHEATLEY

SECRET AND PERSONAL
UNTIL 11.30 AM THURSDAY 19 MAY 1988

MONEY SUPPLY IN APRIL: PRESS BRIEFING

A. FACTUAL

(i) **Changes in main monetary aggregates**

slight revisions

	M0	M3	**M4**	M5
				per cent
12 month growth rate	**+5.9 (+6.2)**	+19.3 (+19.9)	**+15.9 (+15.8)**	+15.6 (+15.5)
Annualised six-month growth	**(+5.1)**	(+14.6)	**(+12.8)**	(+12.3)
one month change	**+1.7 (+0.9)**	+ 0.6 (+ 1.5)	**+ 0.6 (+ 1.0)**	+ 0.4 (+ 0.8)

(Figures in brackets seasonally adjusted s.a.)

(ii) **MO**

Figures (+5.9 and +6.2 s.a.) above target range, but FSBR recognised this was likely.

(iii) **Broad money**

(a) <u>1, 6 and 12 month growth rates</u>. M3 and M4 below levels of March.

(b) <u>But 3 month growth</u> rates returning to levels of mid 1987-88.

(c) M4 gives less erratic signals than M3. Hence MTFS' emphasis on measures including liabilities of building societies as well as banks.

(iv) Lending

(a) Should not read too much into individual counterparts, which are hard to interpret.

(b) One month changes: unadjusted bank lending lower than March, adjusted higher and at record levels.

Slight revisions

	Bank and building society lending		Bank lending	
	£ billion	%	£ billion	%
February	+3.9 (+4.2)	+1.1 (+1.2)	+2.5 (+2.6)	+1.2 (+1.2)
March	+7.9 (+6.8)	+2.3 (+2.0)	+6.0 (+4.9)	+2.8 (+2.3)
April	+6.5 (+8.2)	+1.8 (+2.3)	+4.1 (+5.8)	+1.9 (+2.6)

(Figures in brackets seasonally adjusted)

(d) 12 month growth rates (unadjusted). Bank and building society lending and bank lending both show record growth rates.

Slight revisions

	Bank and building society %	Bank
November	+19.0	+22.5
December	+18.8	+22.8
January	+20.0	+24.7
February	+19.9	+24.2
March	+20.8	+25.2
April	+21.8	+26.8

(e) Approximate breakdown of increase in clearing banks advances in April. Bulk of increase is for companies, not for personal sector:

	£ billion	
Manufacturing	+0.8	
Business and other services	+0.5	
Financial companies	+1.0	
Personal sector	+1.0	
of which house purchase		+0.6
consumption		+0.4
Other bank lending	+0.8	

(v) **Funding**. Overfund (on new, M4 definition) in April of £1.4 billion. PSBR April 1988 a surplus of about £1.7 billion

(vi) **Monetary Policy - Recent Statements**

(a) **Chancellor in Mansion House speech 4 Nov 1987**

"To prevent there being excessive liquidity in the economy, our policy is to ensure that, over time, any net intervention is sterilized - in other words, fully funded."

(b) **Chancellor in Autumn Statement debate (14 January)**

"Keeping the economy on track involves keeping a constant watch on all the indicators of how the economy is developing and then taking action as necessary. I have never hesitated to act in the past when I have judged that there was a risk to our inflation objectives. I can assure the House that I shall not hesitate to do so in future. It is precisely by acting promptly that we have been able to avoid the need for drastic and destabilising lurches in policy. Our track record speaks for itself."

(c) **Chancellor on interest rates (Budget speech, 15 March)**

"Short term interest rates remain the essential instrument of monetary policy. Within a continuous and comprehensive assessment of monetary conditions, I will continue to set interest rates at the level necessary to ensure downward pressure on inflation."

(d) **Chancellor on exchange rates (Budget speech, 15 March)**

"Exchange rates play a central role in domestic monetary decisions as well as in international policy co-operation. I believe that most businessmen have welcomed the greater exchange rate stability over the past year. It is important that they also accept the financial discipline inherent in this policy."
(Also see MTFS, 2.11)

(e) **Chancellor on inflation and exchange rates (This Week Next Week interview, 24 April).**

"Our ultimate aim is certainly the total eradication of inflation."

"We are certainly interested in the maximum possible exchange rate stability, within the context of sound anti-inflationary policy."

(f) **Prime Minister on anti-inflation strategy, exchange rates and interest rates, House of Commons 17 May**

"My rhf [Chancellor] and I entirely agree that we must maintain a firm monetary policy and a downward pull on inflation. I totally agree with my rhf's Budget speech, every bit of it ..... Exchange rate policy ..... is a part of total economic policy .... we have taken interest rates down three times in the last two months. That was clearly designed to affect the exchange rate. We use the available levers, both interest rates and intervention, as seems right in the circumstances .... It would be a great mistake for any speculator to think at any time that sterling was a one-way bet"

She also said that as the value of sterling had risen it had tightened monetary conditions allowing a reduction in interest rates without any adverse effect on inflation.

No positives

B. DEFENSIVE

(i) **Lending**

(a) **Why bank and building society lending so high?** Bulk of increase to companies which are switching from equity financing to bank borrowing; within increase in lending to personal sector, bulk for house purchase, not consumption. Impact of Budget measures on home improvement loans and multiple mortgage tax relief beginning to show.

(b) **Lending figures show overheating? Why cut interest rates on 17 May?**

- If anything, latest figures from real economy [index of production and figures on capital investment] show some slight slowing in growth (though indicators are mixed). CBI quarterly survey shows "few signs of overheating".

- Judgement of monetary conditions and inflationary pressures must take account of whole range of factors, including downward pressure on inflation from exchange rate.

- Experience of number of years shown that high rate of growth of lending and liquidity consistent with lower inflation because increased liquidity willingly held ie held as savings rather than for spending.

- No sign of resurgence of inflation.

(c) **Lending figures inconsistent with indicators from real economy? [Index of production and capital investment].** Real economy figures show mixed picture. In any case, would not expect historical figures to be affected by April lending. CBI April Quarterly Survey said investment intentions strengthened considerably.

(d) **Consumer credit boom?**

- No evidence that rate of lending to consumers accelerating in recent months: 12 month growth rate close to its average since 1982 of 18 per cent. (Some credit simply displacing cash and cheque payments - over 40 per cent of credit card users pay no interest.)

- Vast bulk of personal borrowing takes form of mortgages, which represented 2/3 of outstanding personal debt at end of 1987. Mortgage lending accounts for almost half of all of bank and building society lending. Increase overall as percentage of GDP in 1980s mainly attributable to growth in mortgage borrowing, as result of 2½ million increase in households buying own home.

- Consumer credit only some 15 per cent of total personal debt. Less than 5 per cent of personal debt takes form of credit card lending (including interest-free component). (See Chancellor's speech to FHA, 17 June 1987).

(e) **Why not impose controls on lending**? Not right to restrict growth by quantitive controls: lenders and borrowers should be free to make own decisions. Nor would such controls be effective.

(f) **Should not effects of unwinding of arbitrage from January have depressed bank lending figures?** Possibly, but do not know precisely how much to expect. Easier to detect arbitrage when it is happening than when unwinding.

(g) **Why increase ceiling for building society unsecured lending [from £5,000 to £10,000] when lending already so high**?

[Orders laid today (Thursday) to extend range of building society activities. PQ foreshadowed future order which will raise ceiling for unsecured lending from £5-10,000].

Not a new announcement. No reason to expect increased limit to lead to any significant growth in overall consumer credit. Societies will replace other credit sources, and right they should be given greater scope to compete for retail customers. Building Societies Commission will ensure that societies continue to have adequate credit assessment and control procedures in place. Societies also subject to overall limit on new assets: includes unsecured lending. Mortgage lending for house purchase will continue to be bulk of business.

[See also separate FIM briefing].

(ii) **Money Supply**

(a) **M0 growth outside target range? Won't Tuesday's interest rate cut make this worse?** 1988-89 FSBR chapter 3 recognised that 12-month growth may move to top of or outside 1-5 per cent target range in early part of 1988-89 but should be within range later in year. Six-month growth rates (annualised) currently below 12-month rates.

(b) **M4 (and M3) still rising fast?** After large rises in March, slower rise in April.

(c) **Significance of broad money.** No explicit broad money target in 1988-89. But growth of broad money still taken into account. See MTFS 2.09 and 3.11.

(iii) Prime Minister's statement 17 May

(a) Prime Minister's statement 17 May "papering over the cracks"? No. Prime Minister indicated absolute support for Chancellor. Said she agreed with all of Budget speech, which included clear statement of policy on monetary policy, exchange rate etc.

(b) After interest rate cut on 17 May, Government running out of ammunition to hold down exchange rate? Prime Minister reminded House that sterling not a one-way bet and made clear that "we use available levers, both interest rates and intervention as seems appropriate."

(c) Interest rate cut to bring down sterling or because level of sterling made it safe to do so without loosening monetary conditions? False dichotomy. Decision taken in light of all relevant factors.

(d) Intervention inflationary? Only poses inflationary threat if not funded. 1987-88 intervention was fully funded within financial year.

(e) BEQB said current combination of high exchange rates and low interest rates not ideal and different balance would be desirable. Hasn't interest rate cut made this worse? BEQB referred to an ideal policy mix. But Government has to act in light of market conditions at the time. Overall tightness of policy remains appropriate.

(f) Why cut interest rates rather than intervene? As Prime Minister said, use available levers - interest rates and intervention - as seems right in circumstances.

(iv) **Further movements in interest rates? Intervention?** Never discuss market tactics. As Prime Minister said, anyone asking to know what will happen is aiding and abetting speculator.

(v) **UK's real interest rates out of line with competitors?** Deflating current three month money rates by recent price indices suggest UK only just above G7 average.

(vi) **Change to funding rule**. From start of 1988-89 building societies treated same as banks, so gilt sales to building societies will no longer count towards full fund. No relaxation of monetary policy. Including building societies with banks recognises their evolving status.

Provisional estimates of monetary aggregates: April 1988

1 Provisional information suggests the following:

% changes		M0	M3	M4	M5
12 months to April (not seasonally adjusted)		+5.9	+19.3	+15.9	+15.6
April	- not seasonally adjusted	+1.7	+ 0.6	+ 0.6	+ 0.4
	- seasonally adjusted	+0.9	+ 1.5	+ 1.0	+ 0.8

2 Provisional counterparts to the changes in M3, M4 and M5 are:

£ billions, not seasonally adjusted	M3		M4		M5	
	April	latest 12 months	April	latest 12 months	April	latest 12 months
A PSBR	−0.9	- 6.4	−0.9	- 6.4	- 0.9	- 6.4
B debt sales to private sector (−) (1)	−0.7	- 4.1	−0.6	- 4.7	−0.7	- 3.0
C external flows to public sector (−)	−0.1	+ 5.6	−0.1	+ 5.6	−0.1	+ 5.6
D public sector contribution (A+B+C)	−1.7	- 4.9	−1.6	- 5.5	−1.7	- 3.8
E sterling lending (2)	+4.1	+47.7	+6.5	+64.2	+6.2	+63.9
F other counterparts (3)	−1.2	−11.3	−3.1	−15.0	−3.1	−15.0
Total (D+E+F)	+1.2	+31.5	+1.8	+43.7	+1.4	+45.1
Sterling lending (seasonally adjusted)	+5.8		+8.2		+8.0	
(average of previous 6 months)	+4.0		+5.4		+5.4	

(1) Sales of public sector debt to the private sector other than banks (and, for M4 and M5, building societies), with an adjustment in the case of M5 for private holdings of certain liquid government debt.

(2) Lending by the monetary sector (and, for M4 and M5, by building societies) to the rest of the private sector. For M5, an adjustment is necessary for private holdings of certain money-market instruments etc.

(3) External and foreign currency transactions and net non-deposit liabilities of banks (and, for M4 and M5, of building societies).

3 The PSBR was reduced in April by privatisation proceeds totalling some £1.8 billion, reflecting receipt of the final payment for British Gas shares and repayment of some British Gas debentures.

4 Full money and banking figures for April, including revised estimates of the figures given above, will be published on 31 May.

Bank of England
19 May 1988

PRESS INFORMATION from Banking Information Service

10 Lombard Street, London EC3V 9AR
Telephone 01-626 8486

NOT FOR PUBLICATION BEFORE 11.30 am
Thursday, 19th May 1988

THE COMMITTEE OF LONDON & SCOTTISH BANKERS
MONTHLY STATEMENT: APRIL 1988

Sterling advances to the U.K. private sector again rose very strongly, by £3,759 million in April. After allowing for an estimated seasonal fall and for transit items, the underlying increase was over £5,300 million, compared with £3,200 million in March and the monthly average of around £2,000 million over the last six months. However, the pattern of interest rates suggests that corporate lending this month may have switched to the C.L.S.B. groups away from market-related borrowing; i particular there is some evidence of switching from acceptances into advances, and bill finance probably contracted over the month (both C.L.S.B. acceptances and bill holdings fell).

The analysis of advances, which is not seasonally adjusted, shows that personal lending, though still the dominant influence, accounted for a smaller proportion of the rise than usual (28% instead of the more usual 40%), because of the increase in company borrowing. Personal lending increased by £1,041 million, less than the £1,620 million in March (a quarterly interest-charging month), but well up on the average of some £500 million in January and February. Lending for house purchase showed its usual spring-time increase rising by £651 million (including £54 million of bridging finance), 38% more than in April 1987, and lending "for consumption" rose by £390 million, much stronger than recent non-interest-charging months, but only 8% more than in the same month last year (credit card credit rose by £125 million against £161 million in April 1987). Within the corporate borrowing, advances to 'other services' (+£295 million), property companies (+£190 million) and construction (+£183 million) all continued their recent strong growth, but the most notable increases were for manufacturers (+£656 million, quite well spread, and the largest rise since the formation of the C.L.S.B.) and to securities dealers (+£831 million, largely of a short-term nature).

Among the banks' other assets, lending to the L.D.M.A. and holdings of gilt-edged stock fell by £235 million and £548 million respectively, while operational balances at the Bank of England recovered by £232 million and cash ratio deposits increased by £51 million following the half-yearly adjustment.

On the liabilities side of the balance sheet, deposits from the U.K. private sector rose by £1,057 million. After allowing for seasonal factors and for transit items, the underlying increase was nearly £2,900 million, rather less than the £3,200 million in March, but roughly twice the average monthly increase in the last six months. Much of the increase was in time deposits, largely of a wholesale nature, but high interest personal accounts also rose quite strongly. There was a very large rise in deposits from overseas residents (+£1,593 million) reflecting the attractiveness of sterling, but public sector deposits were little changed. Both borrowing and lending in the CD and interbank market were reduced, with the banks withdrawing net some £900 million. Two of the banks received the proceeds of foreign currency bond issues totalling some £250 million.

Eligible liabilities rose by £3,818 million to £149,895 million.

For further information, please contact:

John Ecklin, Head of C.L.S.B. Statistical Unit (01-283 8866)

Edwin Lawton, Press and Information Manager (01-626 8486)

CONFIDENTIAL UNTIL 11.30 A.M. ON THURSDAY, 19TH MAY, 1988

BALANCES OF C.L.S.B. GROUPS AS AT END-APRIL, 1988

These tables cover the business of the offices of members of the Committee of London and Scottish Bankers and their subsidiaries in the United Kingdom (including the Channel Islands and the Isle of Man) which are listed by the Bank of England as falling within the monetary sector. The items are defined as in Table 3 of the Bank of England's Quarterly Bulletin.

£ millions

TABLE 1. AGGREGATE BALANCES

	Total Outstanding		Change on Month	
LIABILITIES				
STERLING DEPOSITS :				
U.K. monetary sector	29,534		+ 89	
U.K. private sector	126,299		+ 1,057	
U.K. public sector	4,087		+ 47	
Overseas residents	18,956		+ 1,593	
Certificates of deposit	14,110	192,986	- 652	+ 2,134
of which : Sight		81,642		- 246
Time (inc. C.D.'s)		111,344		+ 2,380
FOREIGN CURRENCY DEPOSITS :				
U.K. monetary sector	15,457		+ 154	
Other U.K. residents	8,028		- 117	
Overseas residents	36,224		- 2,311	
Certificates of deposit	4,352	64,060	+ 44	- 2,229
TOTAL DEPOSITS		257,046		- 95
NOTES IN CIRCULATION		817		+ 8
OTHER LIABILITIES (a)		47,769		- 2,197
TOTAL LIABILITIES		305,632		- 2,284
ASSETS				
STERLING				
Cash & balances with Bank of England:				
Cash ratio deposits	631		+ 51	
Other balances	2,120	2,751	+ 191	+ 243
Market loans :				
Discount houses	5,819		- 235	
Other U.K. monetary sector	26,982		- 740	
U.K. monetary sector C.D.'s	5,568		- 743	
Local authorities	1,035		0	
Other	6,738	46,142	- 36	- 1,754
Bills :				
Treasury bills	130		- 73	
Other bills	5,247	5,378	- 210	- 283
Investments :				
British Government stocks	5,524		- 548	
Other	5,354	10,878	- 85	- 633
Advances :				
U.K. private sector	136,239		+ 3,759	
U.K. public sector	505		- 114	
Overseas residents	6,251	142,996	+ 141	+ 3,786
Other sterling assets (a)		18,899		- 1,890
FOREIGN CURRENCIES				
Market loans :				
U.K. monetary sector	15,452		- 604	
Certificates of deposit	461		- 72	
Other	33,981	49,894	- 592	- 1,267
Bills		306		- 26
Advances :				
U.K. private sector	8,207		- 22	
U.K. public sector	118		- 6	
Overseas residents	12,307	20,632	- 296	- 324
Other foreign currency assets (a)		7,755		- 137
TOTAL ASSETS		305,632		- 2,284
ACCEPTANCES		8,333		- 342
ELIGIBLE LIABILITIES		149,895		+ 3,818

(a) includes items in suspense and in transit

FOR TABLE 2 SEE OVER

TABLE 2. INDIVIDUAL GROUP BALANCES

£ millions	C.L.S.B. GROUPS	BANK OF SCOTLAND	BARCLAYS	LLOYDS	MIDLAND	NATIONAL WESTMINSTER	ROYAL BANK OF SCOTLAND	STANDARD CHARTERED	TSB
LIABILITIES									
Sterling deposits									
outstanding	192,986	7,946	46,967	26,825	27,794	50,949	11,567	3,907	17,028
change on month	+ 2,134	- 241	+ 941	+ 303	+ 617	+ 1,058	- 384	- 4	- 157
Foreign currency deposits									
outstanding	64,060	1,242	13,881	7,433	11,742	18,268	3,881	6,634	979
change on month	- 2,229	- 79	- 153	- 114	+ 317	- 1,745	- 35	- 458	+ 38
Total deposits									
outstanding	257,046	9,188	60,849	34,258	39,536	69,217	15,448	10,541	18,008
change on month	- 95	- 320	+ 788	+ 189	+ 934	- 687	- 419	- 462	- 119
STERLING ASSETS									
Cash and Balances with the Bank of England									
outstanding	2,751	335	498	246	260	583	643	19	168
change on month	+ 243	+ 9	+ 151	0	- 14	+ 67	+ 14	+ 3	+ 12
Market loans :									
U.K. monetary sector									
outstanding	32,801	1,054	5,700	3,277	4,676	10,948	1,789	885	4,471
change on month	- 974	- 207	- 333	- 260	+ 364	- 6	- 380	- 272	+ 119
Other									
outstanding	13,341	201	3,221	1,254	1,831	3,492	524	486	2,332
change on month	- 779	- 38	- 469	+ 120	- 155	- 24	- 184	- 18	- 12
Bills									
outstanding	5,378	228	1,847	1,179	137	1,485	309	46	146
change on month	- 283	- 5	+ 257	+ 21	- 252	- 122	- 17	- 22	- 142
British government stocks									
outstanding	5,524	128	1,574	555	874	193	224	269	1,707
change on month	- 548	- 44	+ 151	+ 12	- 9	- 344	- 10	- 3	- 302
Advances									
outstanding	142,996	6,847	36,419	20,859	20,972	35,621	9,429	3,647	9,202
change on month	+ 3,786	+ 59	+ 1,170	+ 364	+ 508	+ 1,034	+ 266	+ 139	+ 247
FOREIGN CURRENCY ASSETS									
Market loans and bills									
outstanding	50,200	508	10,448	6,270	8,646	15,460	3,093	4,993	781
change on month	- 1,293	- 83	- 417	+ 2	+ 117	- 855	+ 33	- 126	+ 37
Advances									
outstanding	20,632	834	3,621	2,953	4,671	4,438	1,255	2,589	271
change on month	- 324	- 2	- 50	+ 14	- 78	- 200	+ 58	- 67	+ 1
ACCEPTANCES									
outstanding	8,333	326	2,186	395	1,732	2,121	791	270	513
change on month	- 342	+ 30	- 510	+ 110	- 138	+ 31	+ 45	+ 4	+ 86
ELIGIBLE LIABILITIES									
outstanding	149,895	6,856	38,840	22,306	21,563	36,687	9,231	2,733	11,680
change on month	+ 3,818	+ 19	+ 1,786	+ 440	+ 492	+ 904	+ 192	+ 280	- 296

COMPOSITION OF GROUPS (U.K. offices only)

The Bank of Scotland Group comprises Bank of Scotland, Bank of Wales plc, North West Securities Ltd. and The British Linen Bank Ltd.

The Barclays Group comprises Barclays Bank PLC, Barclays Bank Finance Company (Jersey) Ltd., Barclays Bank Trust Company Ltd., Barclays de Zoete Wedd Ltd., Barclays Finance Company (Guernsey) Ltd., Barclays Finance Company (Isle of Man) Ltd. and Mercantile Credit Company Ltd.

The Lloyds Group comprises Lloyds Bank PLC, Lloyds Bank Finance (Jersey) Ltd., Lloyds Bowmaker Ltd., Lloyds Merchant Bank Ltd. and The National Bank of New Zealand Ltd.

The Midland Group comprises Midland Bank PLC, Forward Trust Ltd., Midland Bank Finance Corporation Ltd., Midland Bank Trust Company Ltd., Midland Bank Trust Corporation (Guernsey) Ltd., Midland Bank Trust Corporation (Isle of Man) Ltd., Midland Bank Trust Corporation (Jersey) Ltd. and Samuel Montagu & Co., Ltd.

The National Westminster Group comprises National Westminster Bank PLC, Coutts & Co., Coutts Finance Co., International Westminster Bank PLC, Lombard Bank Ltd., Lombard & Ulster Ltd., Lombard Bank (Isle of Man) Ltd., Lombard Banking (Jersey) Ltd., Lombard North Central PLC, National Westminster Bank Finance (C.I.) Ltd., NatWest Investment Bank Ltd., Ulster Bank Ltd., Ulster Bank Trust Company and Ulster Investment Bank Ltd.

The Royal Bank of Scotland Group comprises The Royal Bank of Scotland PLC, Charterhouse Bank Ltd. and RoyScot Trust plc.

The Standard Chartered Group comprises Standard Chartered Bank, Chartered Trust plc and Standard Chartered Merchant Bank Ltd.

The TSB Group comprises TSB England & Wales plc, TSB Northern Ireland plc, TSB Scotland plc, Hill Samuel & Co Ltd., Hill Samuel & Co (Jersey) Ltd., Hill Samuel Personal Finance Ltd. and United Dominions Trust Ltd.

THE COMMITTEE of LONDON and SCOTTISH BANKERS'
STATISTICAL UNIT
10 Lombard Street, London EC3V 9AP
Telephone : 01-283-8866

90/G.jfw.45/024

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FROM: T PIKE
DATE: 19 May 1988

1. MR GRICE

2. ECONOMIC SECRETARY

No great comfort in these figures. The key point about the timing of the Bank Holiday is that last year there was a Wednesday in May both before and afterwards but not this year. This apparently upsets the nsa 12 month comparison.

JWG 19.5.88

cc PS/Chancellor
Sir P Middleton
Sir T Burns
Sir G Littler
Mr Scholar
Mr Sedgwick
Mr Culpin
Mr Peretz
Mrs Lomax
Miss O'Mara
Ms Ryding
Mr Hurst
Ms Bronk

File: MAMC C9

M0 FIGURES

The latest weekly figures for M0, covering the third week of May, are attached. They show that the 12 month growth rate of M0 to the latest four week period was 6.4 per cent (5.9 per cent not seasonally adjusted). Annual growth of notes and coin to the latest four week period was also 6.4 per cent (5.9 per cent not seasonally adjusted).

2. The six month annualised growth rate of notes and coin to the latest four week period was 5.3 per cent, compared with 4.8 per cent in April.

3. The difference between the sa and nsa 12 month growth rates reflects differences in the timing of the end of May Bank Holiday, which last year came just after the third Wednesday of May, and therefore boosted the nsa level of M0 in the current four week period a year ago. Because M0 was also boosted in the final week of May last year - which was just after the Bank Holiday - this difference between the sa and nsa 12 month growth rates should persist for May as a whole.

T. Pike

T PIKE

TABLE 16

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M0 : THE WIDE MONETARY BASE

Monthly data	Notes and Coin (nsa)	Notes and Coin (sa)	(Change in brackets)	Bankers' Deposits	M0 (nsa)	M0 (sa)	(Change in brackets)	% change on previous month: Notes(sa) and Coin	% change on previous month: M0 (sa)	6 month % growth annualised: Notes & Coin (sa)	6 month % growth annualised: M0 (sa)	% change on previous year: Notes and Coin (nsa)	% change on previous year: Notes and Coin (sa)	% change on previous year: M0 (nsa)	% change on previous year: M0 (sa)
1987 September	15349	15376	(118)	185	15534	15561	(121)	0.8	0.8	7.8	7.0	5.3	5.0	5.2	4.9
October	15299	15456	(80)	203	15501	15659	(98)	0.5	0.6	7.4	7.3	5.1	5.2	5.5	5.6
November	15365	15525	(69)	183	15548	15707	(48)	0.4	0.3	7.4	7.0	4.8	4.8	4.9	4.9
December	16447	15661	(136)	186	16633	15846	(139)	0.9	0.9	7.9	8.5	4.7	4.8	4.2	4.3
1988 January	15458	15620	(-41)	181	15638	15801	(-45)	-0.3	-0.3	6.1	5.3	4.7	4.5	4.8	4.6
February	15353	15659	(39)	124	15477	15783	(-18)	0.2	-0.1	5.3	4.5	5.7	5.7	5.3	5.3
March	15588	15753	(94)	162	15750	15916	(133)	0.6	0.8	5.0	4.6	6.9	6.4	6.4	5.8
April	15797	15826	(73)	229	16026	16055	(139)	0.5	0.9	4.8	5.1	5.8	6.1	5.9	6.2
May (3/4) @	15811	15937	(111)	193	16003	16130	(75)	0.7	0.5	5.4	5.5	5.6	6.4	5.4	6.2
Latest 4 weeks @	15791	15919	(102)	219	16010	16137	(120)	0.6	0.7	5.3	5.7	5.9	6.4	5.9	6.4

Level £ million (Change in brackets)

Weekly data	Notes(sa) and Coin	(Change in brackets)	Bankers' Deposits	M0 (sa)	(Change in brackets)	Percentage change on previous week: M0 (sa)
April						
6th	15832	(5)	263	16095	(87)	0.5
13th	15775	(-57)	97	15872	(-223)	-1.4
20th	15834	(59)	259	16093	(221)	1.4
27th	15862	(28)	297	16159	(66)	0.4
May						
4th	15948	(86)	160	16108	(-51)	-0.3
11th	15912	(-36)	166	16078	(-30)	-0.2
18th	15952	(40)	252	16204	(126)	0.8

@ Weekly data for the current month so far include estimates for the unbacked note issue. The latest week also includes an estimate for coin.
The changes for the current month so far use as a base the previous full month and the full month a year ago.
The latest four week changes use as a base the four week averaged level four weeks ago and a year ago.

91G/SCB/4322/11

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FROM: IAN RICH

DATE: 23 May 1988

1. MISS ~~O'~~MARA

2. ECONOMIC SECRETARY

We strongly recommend announcing a reduction as soon as possible, slightly larger than the one we envisaged a couple of weeks ago, given the base rate cut meanwhile.

23/5

cc: Chancellor
Sir P Middleton
Sir T Burns
Mr Scholar
Mr Peretz
Mr Grice
Miss Anderson
Mr Cropper

Mr Patterson (DNS)
Mr Ward (DNS)

NATIONAL SAVINGS INTEREST RATES

Introduction

1. My submission of 6 May recommended reductions in the interest rates payable on three National Savings products - by ¾% (to 8¼%) on Income and Deposit Bonds and by 1% (to 7½%) on the Investment Account - to bring them into line with competing bank and building society rates, and so avoid attracting substantial inflows into these relatively liquid products. In the event Ministers preferred not to make any reductions immediately because of concern about triggering a change in building society rates, but agreed to take stock in about 2 weeks' time (Mr Barnes' minute of 11 May refers).

Background

2. A number of building societies had reduced their deposit rates by ½% net to reflect the 8% base rate at the time of my original submission, and many more have done so since. In the interim, bank base rates have been cut by a further ½%. No building society has yet reduced its mortgage or deposit rates to reflect this latest reduction, but they are expected to make a further ½% cut if it appears that the latest base rate reduction will be sustained. A table giving more detailed comparisons between National Savings and competing interest rates is at Annex A.

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Options

3. Following last week's base rate cut, the case for a reduction in these three National Savings rates now seems to us to be very strong indeed. DNS agree. We do not believe that this in itself would precipitate a cut in building society rates; any move there would reflect the base rate change rather than a reduction in National Savings rates.

4. However, in the light of last week's developments we now recommend making slightly larger reductions of 1% (to 8%) in the Income and Deposit Bond rates, and 1¼% (to 7¼%) in the Investment Account rate. This would give the building societies a modest additional competitive edge, and so avoid the presentational awkwardness of another reduction in National Savings rates in the near future if the societies were to make further cuts.

5. If Ministers decide that the Income and Deposit Bond rate should be reduced by 1%, DNS would prefer to limit the Investment Account reduction to 1%, forgoing on this occasion the extra ¼% we hitherto had in mind for this product. They feel that a 1¼% reduction would be too severe, and would be badly received by investors. Treasury officials continue to see a strong case on quality of funding grounds for the full 1¼%.

Timing

6. We see advantage in announcing reductions in the three rates as soon as possible, so that they are fully associated in the public's mind with last week's reduction in base rates. We do not think the change in National Savings rates should have any impact on building societies' decisions on whether to reduce their own rates further. The reductions would also save us £2½-3 million a week in interest costs. You will recall that we have to give 6 weeks' notice of changes in Income and Deposit Bond rates, so they would become effective in mid-July. It is customary to give 2 weeks' notice of changes in the Investment Account rate, which would thus come into force in mid-June.

7. However, if you wished, you could defer decisions until Wednesday's funding meeting with announcement as soon as possible thereafter.

Recommendation

8. Treasury officials recommend a reduction of 1% in the interest rates on Income and Deposit Bonds, and 1¼% in the interest rate on the Investment Account. The changes recommended are:

	Present Rate %	Recommended Rate %
Income and Deposit Bonds	9	8
Investment Account	8½	7¼

Ian Rich

IAN RICH

ANNEX A

TABLE 3 : NATIONAL SAVINGS INSTRUMENTS : VARIABLE RATE PRODUCTS.

Compound Return	Per cent Tax Rate (%) 0	25	40	Administrative costs
Income Bond (1)	9.5	7.1	5.7	0.2
Deposit Bond	9.0	6.8	5.4	0.3
Investment Account	8.5	6.4	5.1	0.4
Premium Bond	6.5	6.5	6.5	1.1
Savings Certificate on GER terms	5.0	5.0	5.0	0.2
12 Month Cost of Government Borrowing (2)	8.8	6.6	5.3	-
CTDs	7.5	5.6	4.5	-
Bank Retail Deposit Rate (3)	5.6	5.6	4.5	N/A
Building Society Retail Deposit Rate (3)	6.7	6.7	5.4	N/A

(1) Assuming interest reinvested in Investment Account.

(2) Yield on a basket of gilts with maturities clustered around one year.

(3) Average of rates applying to the top bands of selected high interest accounts at 4 May 1988.

(4) The Premium Bond rate will be lowered on 1 July 1988.

Pmp

MINUTES OF A MEETING HELD IN CHANCELLOR'S ROOM
HM TREASURY AT 3.45PM ON TUESDAY, 24 MAY 1988

Those present

Chancellor
Economic Secretary
Sir P Middleton
Sir T Burns
Mr Scholar
Mrs Lomax
Mr Peretz
Mr Grice
Miss O'Mara
Mr Culpin
Mr Tyrie

USE OF PRUDENTIAL CONTROLS TO RESTRAIN MORTGAGE LENDING

The Chancellor said he was grateful for Mr Peretz's note of 16 May, which set out various possible ways of restraining the growth of mortgage lending, though he had to agree that none of these were very promising. Clearly, from a prudential point of view, mortgage lending was less risky than various other forms of unsecured lending, but there was cause for worry in the increasing ratio of advances to individuals' earnings, which must increase the risk of a rash of defaults. So in the circumstances, we had to consider options that could have an effect, even psychological, on the growth of lending.

2. Sir P Middleton said that he had held a meeting to consider the options available, short of using fiscal policy, or interest rates, and he too thought that none of them looked very promising. If Ministers decided to attack the problem via prudential controls, we would want to approach first the BSC, and then the Bank. He had informally sounded out the Bank, who were clearly unenthusiastic about doing anything via prudential controls. Of the other possibilities in Mr Peretz's note, the only one that he thought practicable was some relaxation of limits on foreign borrowers' sterling issues, under COBO.

3. Sir T Burns said that he agreed with the Chancellor that it was desirable to do something to cool off this sector of the economy. The mood of the market resembled that in the equity markets before 19 October, and clearly, if the bubble was going to burst, then the sooner it did so the less painful it would be. But he too thought it would be difficult to run the prudential argument. What was really worrying was the high income multiples which lenders were now prepared to advance.

4. The Chancellor agreed: he asked if it would be possible to re-do the tables attached to Mr Peretz's minute so that they included first-time buyers. He noted that the average advance:income ratio now seemed to be approaching 2 again, the level it had been at in 1972-73, although it had dropped to 1½ in the intervening years. It would be interesting to know if there were significant regional variations underlying the average figures. He would also like an analysis of how the position now compared with that in 1972-73, taking into account the various relevant factors - real interest rates (and any differential between building society rates and others), the tax position, real earnings etc. Sir T Burns agreed to provide a note.

5. The meeting then considered whether there were any other options which might be considered as ways of tackling the problem. One possibility would be the various supply side measures being considered in the housing field - freeing-up the supply of land, or obliging councils to sell empty council houses. Alternatively, Ministers could try and "talk the market down": the Building Societies' Commission had tried this in the past, but now were not convinced there was a case for doing this on prudential grounds. It did not seem very attractive for Ministers to make warning noises about personal indebtedness.

6. The Chancellor asked what the state of play was on the National Credit Register. Mr Scholar reported that the Data Protection Registrar had questioned whether confidentiality was

adequately protected by the waiver provision now to be included on loan applications.

7. Finally, Sir P Middleton raised one further possibility. We had been holding off cutting National Savings rates lest this should prompt further reductions in building society rates. It would be possible to keep National Savings rates where they were, and offset this by buying-in long gilts. This might attract funds from building societies. It was agreed that the Economic Secretary should consider this further.

MPW.

MOIRA WALLACE

26 May 1988

Distribution

Those present

Miss Noble

90/G.jfw.45/024

CONFIDENTIAL

FROM: T PIKE
DATE: 26 May 1988

1. MR GRICE JWG 26.5.88
2. ECONOMIC SECRETARY o/r

cc PS/Chancellor
Sir P Middleton
Sir T Burns
Sir G Littler
Mr Scholar
Mr Sedgwick
Mr Culpin
Mr Peretz
Mrs Lomax
Miss O'Mara
Ms Ryding
Mr Hurst
Ms Bronk o/r

File: MAMC C9

M0 FIGURES

The latest weekly figures for M0, covering the final week of May, are attached. They show that the 12 month growth rate of M0 in May was 6.2 per cent (5.7 per cent not seasonally adjusted). Annual growth of notes and coin in May was 6.4 per cent (5.9 per cent not seasonally adjusted).

2. The six month annualised growth rate of notes and coin in May was 5.5 per cent, compared with 4.8 per cent in April.

T Pike

T PIKE

TABLE 16

CONFIDENTIAL (Until Publication)

M0 : THE WIDE MONETARY BASE

Monthly data	Level £ million (Change in brackets) Notes and Coin (nsa)	Notes and Coin (sa)		Bankers' Deposits	M0 (nsa)	M0 (sa)		Percentage change on previous month Notes(sa) and Coin	M0 (sa)	6 month % growth annualised Notes & Coin (sa)	M0 (sa)	Percentage change on previous year Notes and Coin (nsa)	Notes and Coin (sa)	M0 (nsa)	M0 (sa)
1987 September	15349	15376	(118)	185	15534	15561	(121)	0.8	0.8	7.8	7.0	5.3	5.0	5.2	4.9
October	15299	15456	(80)	203	15501	15659	(98)	0.5	0.6	7.4	7.3	5.1	5.2	5.5	5.6
November	15365	15525	(69)	183	15548	15707	(48)	0.4	0.3	7.4	7.0	4.8	4.8	4.9	4.9
December	16447	15661	(136)	186	16633	15846	(139)	0.9	0.9	7.9	8.5	4.7	4.8	4.2	4.3
1988 January	15458	15620	(-41)	181	15638	15801	(-45)	-0.3	-0.3	6.1	5.3	4.7	4.5	4.8	4.6
February	15353	15659	(39)	124	15477	15783	(-18)	0.2	-0.1	5.3	4.5	5.7	5.7	5.3	5.3
March	15588	15753	(94)	162	15750	15916	(133)	0.6	0.8	5.0	4.6	6.9	6.4	6.4	5.8
April	15797	15826	(73)	229	16026	16055	(139)	0.5	0.9	4.8	5.1	5.8	6.1	5.9	6.2
May (4/4)	15860	15943	(117)	183	16042	16126	(71)	0.7	0.4	5.5	5.4	5.9	6.4	5.7	6.2

Weekly data	Level £ million (Change in brackets) Notes(sa) and Coin		Bankers' Deposits	M0 (sa)		Percentage change on previous week M0 (sa)
April						
6th	15832	(5)	263	16095	(87)	0.5
13th	15775	(-57)	97	15872	(-223)	-1.4
20th	15834	(59)	259	16093	(221)	1.4
27th	15862	(28)	297	16159	(66)	0.4
May						
4th	15948	(86)	160	16108	(-51)	-0.3
11th	15912	(-36)	166	16078	(-30)	-0.2
18th	15952	(40)	252	16204	(126)	0.8
25th	15960	(8)	153	16113	(-91)	-0.6

PS can I have briefing on provisionals

91G.SCB.3433.8

SECRET AND PERSONAL
UNTIL 11.30 AM ON TUESDAY 31 MAY 1988

FROM: M H WHEATLEY
DATE: 26 May 1988

~~BF 11/6~~ PUP.

MR SCHOLAR

Ok — two corrections — passim

cc PPS
PS/Chief Secretary
PS/Economic Secretary
Sir P Middleton
Sir G Littler
Sir T Burns
Mr R I G Allen
Mr Peretz
Mr Grice
Miss O'Mara
Mr Bush
Mr Pike
Mrs Ryding
Ms Bronk
Mr Cropper

<u>FULL MONEY FIGURES: APRIL</u>

I attach the Bank's press release on the full money figures which will be published at 11.30am on Tuesday 31 May.

2. The only change to note from the provisional figures is :

- the PSBR for April now rounds to a surplus of £1.1 billion (rather than £0.9 billion in the provisional figures).

3. The only change to the provisional press briefing apart from one or two (sidelined) small adjustments to the figures is the addition of the Chancellor's remarks on inflation at the Conservative Women's Conference on 24 May.

4. IDT advise that there is normally very little interest in the full money figures. Their appearance on the privilege day should therefore cause no problems.

SECRET AND PERSONAL
UNTIL 11.30 AM ON TUESDAY 31 MAY 1988

5. I would be grateful if you could let me have any comments on the revised press briefing by midday on Friday 27 May.

Cathy Ryding

PP M H WHEATLEY
MG1

91G.SCB.10.3433

MONEY SUPPLY IN APRIL: PRESS BRIEFING

A. FACTUAL

(i) **Changes in main monetary aggregates**

per cent

	M0	M3	**M4**	M5
12 month growth rate	**+5.9** **(+6.2)**	+19.3 (+19.9)	**+15.9** **(+15.8)**	+15.6 (+15.5)
Annualised six-month growth	**(+5.1)**	(+14.6)	**(+12.8)**	(+12.3)
one month change	**+1.7** **(+0.9)**	+ 0.6 (+ 1.5)	**+ 0.6** **(+ 1.0)**	+ 0.4 (+ 0.8)

(Figures in brackets seasonally adjusted s.a.)

(ii) **MO**

Figures (+5.9 and +6.2 s.a.) above target range, but FSBR recognised this was likely.

(iii) **Broad money**

(a) 1, 6 and 12 month growth rates. M3 and M4 below levels of March.

(b) But 3 month growth rates returning to levels of mid 1987-88.

(c) M4 gives less erratic signals than M3. Hence MTFS' emphasis on measures including liabilities of building societies as well as banks.

(iv) Lending

(a) Should not read too much into individual counterparts, which are hard to interpret.

(b) One month changes: unadjusted bank lending lower than March, adjusted higher and at record levels.

	Bank and building society lending		Bank lending	
	£ billion	%	£ billion	%
February	+3.9 (+4.2)	+1.1 (+1.2)	+2.5 (+2.6)	+1.2 (+1.2)
March	+7.9 (+6.8)	+2.3 (+2.0)	+6.0 (+4.9)	+2.8 (+2.3)
April	+6.4 (+8.2)	+1.8 (+2.3)	+4.1 (+5.8)	+1.9 (+2.6)

(Figures in brackets seasonally adjusted)

(d) 12 month growth rates (unadjusted). Bank and building society lending and bank lending both show record growth rates.

	Bank and building society %	Bank
November	+19.0	+22.5
December	+18.8	+22.8
January	+20.0	+24.7
February	+19.9	+24.2
March	+20.8	+25.2
April	+21.8	+26.8

(e) Approximate breakdown of increase in clearing banks advances in April. Bulk of increase is for companies, not for personal sector:

	£ billion	
Manufacturing	+0.8	
Business and other services	+0.5	
Financial companies	+1.0	
Personal sector	+1.0	
of which house purchase		+0.6
consumption		+0.4
Other bank lending	+0.8	

(v) **Funding.** Overfund (on new, M4 definition) in April of £1.7 billion. PSBR April 1988 a surplus of about £1.1 billion

(vi) **Monetary Policy - Recent Statements**

(a) **Chancellor in Mansion House speech 4 Nov 1987**

"To prevent there being excessive liquidity in the economy, our policy is to ensure that, over time, any net intervention is sterilized - in other words, fully funded."

(b) **Chancellor in Autumn Statement debate (14 January)**

"Keeping the economy on track involves keeping a constant watch on all the indicators of how the economy is developing and then taking action as necessary. I have never hesitated to act in the past when I have judged that there was a risk to our inflation objectives. I can assure the House that I shall not hesitate to do so in future. It is precisely by acting promptly that we have been able to avoid the need for drastic and destabilising lurches in policy. Our track record speaks for itself."

(c) **<u>Chancellor on interest rates (Budget speech, 15 March)</u>**

"Short term interest rates remain the essential instrument of monetary policy. Within a continuous and comprehensive assessment of monetary conditions, I will continue to set interest rates at the level necessary to ensure downward pressure on inflation."

(d) **<u>Chancellor on exchange rates (Budget speech, 15 March)</u>**

"Exchange rates play a central role in domestic monetary decisions as well as in international policy co-operation. I believe that most businessmen have welcomed the greater exchange rate stability over the past year. It is important that they also accept the financial discipline inherent in this policy."
(Also see MTFS, 2.11)

(e) **<u>Chancellor on inflation and exchange rates (This Week Next Week interview, 24 April)</u>.**

"Our ultimate aim is certainly the total eradication of inflation."

"We are certainly interested in the maximum possible exchange rate stability, within the context of sound anti-inflationary policy."

(f) **Prime Minister on anti-inflation strategy, exchange rates and interest rates, House of Commons 17 May**

"My rhf [Chancellor] and I entirely agree that we must maintain a firm monetary policy and a downward pull on inflation. I totally agree with my rhf's Budget speech, every bit of it ..... Exchange rate policy ..... is a part of total economic policy .... we have taken interest rates down three times in the last two months. That was clearly designed to affect the exchange rate. We use the available levers, both interest rates and intervention, as seems right in the circumstances .... It would be a great mistake for any speculator to think at any time that sterling was a one-way bet"

She also said that as the value of sterling had risen it had tightened monetary conditions allowing a reduction in interest rates without any adverse effect on inflation.

(g) **Chancellor on anti-inflationary policy, Conservative Women's Conference, 24 May**

Chancellor said no risks would be taken with inflation. Battle against inflation remained "at the very core and centre" of policies "as it has done throughout my time as Chancellor, and Geoffrey Howe's before me."

B. DEFENSIVE

(i) Lending

(a) **Why bank and building society lending so high?** Bulk of increase to companies which are switching from equity financing to bank borrowing; within increase in lending to personal sector, bulk for house purchase, not consumption. Impact of ~~Budget measures on~~ bringing forward home improvement loans and multiple mortgages ~~tax relief~~ to bear Budget measures beginning to show.

(b) **Lending figures show overheating? Why cut interest rates on 17 May?**

- If anything, latest figures from real economy [index of production and figures on capital investment] show some slight slowing in growth (though indicators are mixed). CBI quarterly survey shows "few signs of overheating".

- Judgement of monetary conditions and inflationary pressures must take account of whole range of factors, including downward pressure on inflation from exchange rate.

- Experience of number of years shown that high rate of growth of lending and liquidity consistent with lower inflation because increased liquidity willingly held ie held as savings rather than for spending.

- No sign of resurgence of inflation.

(c) **Lending figures inconsistent with indicators from real economy? [Index of production and capital investment]**. Real economy figures show mixed picture. In any case, would not expect historical figures to be affected by April lending. CBI April Quarterly Survey said investment intentions strengthened considerably.

(d) **Consumer credit boom?**

- No evidence that rate of lending to consumers accelerating in recent months: 12 month growth rate close to its average since 1982 of 18 per cent. (Some credit simply displacing cash and cheque payments - over 40 per cent of credit card users pay no interest.)

- Vast bulk of personal borrowing takes form of mortgages, which represented 2/3 of outstanding personal debt at end of 1987. Mortgage lending accounts for almost half of all of bank and building society lending. Increase overall as percentage of GDP in 1980s mainly attributable to growth in mortgage borrowing, as result of 2½ million increase in households buying own home.

- Consumer credit only some 15 per cent of total personal debt. Less than 5 per cent of personal debt takes form of credit card lending (including interest-free component). (See Chancellor's speech to FHA, 17 June 1987).

(e) **Why not impose controls on lending?** Not ~~right~~ Sensible to restrict growth by quantitative controls: lenders and borrowers should be free to make own decisions. Nor would such controls be effective.

(f) **Should not effects of unwinding of arbitrage from January have depressed bank lending figures?** Possibly, but do not know precisely how much to expect. Easier to detect arbitrage when it is happening than when unwinding.

(g) **Why increase ceiling for building society unsecured lending [from £5,000 to £10,000] when lending already so high?**

[Orders laid 19 May to extend range of building society activities. PQ foreshadowed future order which will raise ceiling for unsecured lending from £5-10,000].

Not a new announcement. No reason to expect increased limit to lead to any significant growth in overall consumer credit. Societies will replace other credit sources, and right they should be given greater scope to compete for retail customers. Building Societies Commission will ensure that societies continue to have adequate credit assessment and control procedures in place. Societies also subject to overall limit on new assets: includes unsecured lending. Mortgage lending for house purchase will continue to be bulk of business.

[See also separate FIM briefing].

(ii) **Money Supply**

(a) **M0 growth outside target range? Won't interest rate cut on 17 May make this worse?** 1988-89 FSBR chapter 3 recognised that 12-month growth may move to top of or outside 1-5 per cent target range in early part of 1988-89 but should be within range later in year. Six-month growth rates (annualised) currently below 12-month rates.

(b) **M4 (and M3) still rising fast?** After large rises in March, slower rise in April.

(c) **Significance of broad money.** No explicit broad money target in 1988-89. But growth of broad money still taken into account. See MTFS 2.09 and 3.11.

(iii) **Prime Minister's statement 17 May**

(a) **Prime Minister's statement 17 May "papering over the cracks"?** No. Prime Minister indicated absolute support for Chancellor. Said she agreed with all of Budget speech, which included clear statement of policy on monetary policy, exchange rate etc.

(b) **After interest rate cut on 17 May, Government running out of ammunition to hold down exchange rate?** Prime Minister reminded House that sterling not a one-way bet and made clear that "we use available levers, both interest rates and intervention as seems appropriate."

Slight misquote: use correct version (see relevant statements)

(c) **Interest rate cut to bring down sterling or because level of sterling made it safe to do so without loosening monetary conditions?** False dichotomy. Decision taken in light of all relevant factors.

(d) **Intervention inflationary?** Only poses inflationary threat if not funded. 1987-88 intervention was fully funded within financial year.

(e) **BEQB said current combination of high exchange rates and low interest rates not ideal and different balance would be desirable. Hasn't interest rate cut made this worse?** BEQB referred to an ideal policy mix. But Government has to act in light of market conditions at the time. Overall tightness of policy remains appropriate.

(f) **Why cut interest rates rather than intervene?** As Prime Minister said, use available levers - interest rates and intervention - as seems right in circumstances.

(iv) **Further movements in interest rates? Intervention?** Never discuss market tactics. As Prime Minister said, anyone asking to know what will happen is aiding and abetting speculator.

(v) **UK's real interest rates out of line with competitors?** Deflating current three month money rates by recent price indices suggest UK only just above G7 average.

(vi) **Change to funding rule.** From start of 1988-89 building societies treated same as banks, so gilt sales to building societies will no longer count towards full fund. No relaxation of monetary policy. Including building societies with banks recognises their evolving status.

0007F COVERING SECRET 25.5.88

MR GEORGE Copies to Mr Coleby
Mr Flemming
Mr Plenderleith
Mr Foot
Mr W A Allen
Mr Warland
Mr Mann
Mr Midgley
Mr Pennington

Mr M St J Wright
Groups 2/2
2/3
2/4

Miss O'Mara)
Ms Ryding) HMT
Mr C Mowl)

FINAL MONEY PRESS RELEASE FOR APRIL 1988

I attach a draft of the covering text for the full press release for publication at 11.30 am on Tuesday, 31 May (including a brief mention of the building society balance sheet table which appears for the first time in this release). Please may I have any comments by 10.30 am on Friday, 27 May.

The only change of any note from the provisional press release is an upwards revision to the PSBR surplus in April, from "£0.9 bn" in the provisional release (£933 mn in the PSBR release) to £1058 mn now.

Financial Statistics Division BB-1
25 May 1988

J W Thorp (4764)

J

DRAFT Secret until 11.30am 31/05/88

Monetary statistics: April 1988

1 The changes in the monetary aggregates are summarised below:

% changes	12 months to April 1988	April 1988	
	not seasonally adjusted	not seasonally adjusted	seasonally adjusted
M0	+ 5.9	+1.7	+0.9
M1	+20.9	+1.0	+1.0
of which, non-interest-bearing M1	+13.3	−0.2	−0.3
M2	+13.1	+0.7	+0.7
M3	+19.3	+0.6	+1.5
M3c	+15.9	+0.3	+1.0
M4	+15.9	+0.6	+1.0
M5	+15.6	+0.4	+0.8

2 Tables A-G and I show the components and counterparts of the monetary aggregates. Tables K-N show details of the banks' and discount market's balance sheets; transactions of the consolidated UK monetary sector, excluding interbank items and valuation changes on foreign currency items, are shown in Table H. Details of the building societies' balance sheet are shown in Table O, which appears for the first time in this release. An article in the May 1987 *Quarterly Bulletin* discussed the construction of the broad monetary aggregates.

3 The PSBR was reduced in April by privatisation proceeds totalling some £1.8 billion, reflecting receipt of the final payment for British Gas shares and repayment of some British Gas debentures.

4 Estimated seasonal movements in May 1988

The provisional seasonal movements are shown below. Because of the difficulties referred to in the December 1986 *Quarterly Bulletin* (page 519), the figures should be regarded as more uncertain than were the figures formerly given for banking months. They remain subject to revision.

£ millions	
M0	− 50
M3	+1360
M4	+1200
M5	+ 960
M3 counterpart: banks' sterling lending to UK private sector	+ 20
M4 and M5 counterpart: bank and building society sterling lending to the rest of the UK private sector (see footnotes to Table G)	+ 50

The seasonally-adjusted changes are obtained by subtracting (with due regard to sign) the seasonal movement from the unadjusted changes.

Bank of England
31 May 1988

PMP

HAMBROS

41 Bishopsgate, London EC2P 2AA. Telephone: 01-588 2851 S.W.I.F.T.: HAMB GB 2L Telex: 883851

HAMBROS PLC

CHS/RBS

26th May 1988

Ch/ Interesting. Suggests that average income multiple in D Peretz[']s note may conceal big variations - regional & between 1st-time buyers & others. Worth circulating?

Yes. MPW 27/5

The Rt Hon Nigel Lawson, M.P.
Chancellor of the Exchequer,
The Treasury,
Parliament Street,
London, SW1P 3AJ

Dear Chancellor,

It was very nice to see you at lunch here last Friday. During our discussions on the somewhat overheated state of the private home market you asked me what sort of salary multiples our customers were spending on their mortgages. We have a subsidiary called Taylors which operates from High Wycombe in the south to Rugby in the north and from Banbury in the west to Kettering in the east. It is probably our fastest-growing subsidiary and its customers are more predominantly first-time home buyers than in other parts of our business.

Taylors' overall average mortgage arranged is £39,000 and the multiple for single home buyers is 2.93 times their salary and, in the case of couples, the multiple is 2.46 times their combined salaries. The latter category will obviously disappear after the end of July this year. The average price of houses sold by the Group in 1987 was £56,000 and the average mortgage arranged by Taylors of £39,000 is some 70% of the total house cost.

Where has this suddenly come from?

I am not sure what these figures prove, except to demonstrate the position we hold in the marketplace and that these multiples, which are fixed by the lending institutions, are likely to reach levels where the individual borrowers could begin to experience difficulties.

Naturally, if you want any other facts or figures I would be delighted to supply you with them.

Yours sincerely

Christopher Sporborg

C.H. Sporborg
Vice Chairman

pl clean up & circulate for info to those attending meeting behind

M.

regulations between mortgage interest repayments (which the State will sometimes help with) and capital repayments (which it will not help with).

● Step 3 [illegible] the tenant take out a [illegible]start, "index-linked" mortgage on his home, to the full amount of the sale price as calculated in Step 1, less any discount entitlement under the existing Right-to-Buy legislation.

The advantage of an index-linked mortgage is that unlike ordinary mortgages, it starts with low repayments that rise more or less in line with inflation. As a result, many tenants would find that, throughout the period of the mortgage, their loan repayments would actually be cheaper—about £5 a week less—than what they would have paid in rent.

● Step 4: Oblige the homebuyer to invest the £5 a week in a with-profits insurance fund, run by the private sector but approved by the Government, so that the profits would be used for minor repairs and the insurance element would take care of major repairs.

The remarkable thing about this scheme is that it benefits everybody.

The former tenant benefits because, by paying no more each week than he formerly paid in rent, he ends up owning his home. And once he has paid off the mortgage, his weekly bill for housing will drop dramatically.

Insurance

The local authority benefits because it gets an upfront lump sum for its council house, and it can then use that sum for renovating its existing stock or reducing the outstanding debt on it. Also, it no longer has to pay for repairs or management.

The Treasury benefits because, although it goes on supporting the poorer homebuyer while the mortgage is still running, at the end of the loan period its contributions fall to just £5 a week, enough to continue the purchaser's insurance against future repairs.

The reason why there are no losers is simple. The council housing stock of Britain is an enormous capital asset, but it is an asset that is very badly managed and, therefore, financially unproductive.

The proposed scheme encourages the individual to borrow against the now-frozen capital asset in which he lives, thereby releasing enough extra wealth to make him, the local authority and the State better off.

Thus, what appears to be a Socialist redistribution of wealth in favour of the poor is also a sound, capitalistic exploitation of what is now the country's largest wasting asset—the stock of council houses.

From the misty fastnesses of Wales, Peter Walker may have started something. Which is a lot more than can be said for Richard Rich, who merely finished somebody.

Thursday, May 26, 1988

Pry

FINANCIAL TIMES

Mortgage defaults 'increasing'

BY STEPHEN FIDLER, EUROMARKETS CORRESPONDENT

49 =

A PICTURE of growing instability in British house prices and rising numbers of defaults on home mortgages is painted in a report published yesterday by Moody's Investors Service, the US credit rating agency.

The agency says growing owner occupation in Britain means that financially less able home buyers are entering the mortgage market at a time when home prices are rising at double-digit rates.

First-time buyers are stretching budgets to afford their rising mortgage payments and buyers require less and less of their own equity to purchase a home. This has resulted in a growth in mortgage arrears and default rates since the late 1970s, a trend which Moody's says it expects to continue and which will be intensified by the growing competition among mortgage lenders.

House mortgages in repossession or in arrears of more than six months rose from about 10,000 in 1979 to 75,000 last year, the agency says.

However, it says losses incurred by mortgage lenders have been low because of the rapid rise in house prices. "Moody's believes, however, that home prices are becoming increasingly unstable," the report says.

Increased mortgage demand and rising personal incomes have contributed to price rises but speculative purchases have added to house price instability.

"In a recessionary climate," says the report, "home prices may stagnate or even decline, exposing lenders to substantially higher levels of default rates and subsequent losses than have been experienced in the past."

Mohe
Worth getting if it
doesn't cost £££

Alex

~~Tarry P~~

Can you find out
how many £££ pl?

M

~~Alex~~
Not yet published (next wk)
but unpublished version believed

18a

CONFIDENTIAL x, and my note of Y pl. m

BF 1/6
KM

From : D L C Peretz
Date : 26 May 1988

CHANCELLOR

cc Economic Secretary
Sir P Middleton
Sir T Burns
Sir G Littler
Mr Scholar
Mrs Lomax
Miss O'Mara
Mr Grice
Mr Courtney
Mr Rich
Mr Cropper
Mr Tyrie

Mr Patterson - DNS
Mr C Ward - "

Ch/ wait for PEM's views? mpw.

yes please

NATIONAL SAVINGS INTEREST RATES

Y Following the discussion at your meeting on 24 May we considered this further with the Bank of England and DNS at the Economic Secretary's Funding Meeting, yesterday afternoon. The Economic Secretary asked me to let you have a note of our agreed conclusions and recommendations.

Issues

X 2. Mr Rich's minute of 23 May proposed a reduction in the main DNS variable interest rates (on income bonds, deposit bonds, and the investment account) for fairly straightforward reasons :

- other rates have fallen, and DNS now look over-competitive (see the table attached to Mr Rich's minute).

- we have wanted if anything to edge these rates down slightly in relation to other rates in the course of the year, to help to produce the lower national savings take we are looking for this year - on the grounds that these liquid instruments represent rather poor quality funding.

- keeping the rates higher than necessary costs money. Indeed the delay in reducing them is costing us something like £3 million a week. This is the "dead weight" cost : ie the cost of extra interest being paid on the £15 billion stock of these national savings products. There might be some small offset to this cost if the extra money being attracted turns out in the end to be cheaper than alternative forms of funding (eg if the proceeds are used to buy in long conventional gilts) - but the amount of extra money likely to be attracted is very small in relation to the stock (see para 6 below).

3. There are two arguments for delay, both connected with our concern about the rapid growth of mortgage lending and house prices.

a) at your meeting on 24 May we discussed the idea that attracting extra inflows into national savings might be a way of diverting funds away from building societies, and hence reducing the availability of finance for mortgage lending.

b) we were worried, particularly before the most recent cut in base rates, that a move might trigger the building societies to cut mortgage rates when otherwise they might have stayed put.

Retail deposit flows

4. We discussed these last points at the Funding Meeting yesterday.

5. The attached table shows the relationship between mortgage lending and national savings flows over a run of years. You will see that national savings flows are nowadays very modest in comparison to the flows of money into the mortgage market. It would take a very sharp rise in national savings inflows to have any marked effect on the availability of money for mortgage lending.

6. If we were to leave the rates on these national savings variable rate products where they are, rather than reduce them as proposed, we think the effect of DNS inflows would be of the order of £20-£40 million a month : a drop in the ocean compared to mortgage lending which is currently running at a rate of over £3 billion a month.

7. It would take a different kind of move on national savings to produce a more significant impact on flows : for example introducing a new national savings certificate, or raising the £1000 new purchase limit on the present certificate. We and DNS find that unattractive : we want to concentrate our efforts on developing and launching a successful taxable fixed rate product, but that will not be ready until later in the year.

8. The key point, however, is that even if we were successful in diverting a larger percentage of <u>retail</u> savings flows into national savings, that would be unlikely nowadays to have any effect on the availability of funds for mortgages. With banks competing in the market as well as building societies, and with building societies' access to wholesale funds, the result would merely be that more mortgage lending was financed in the wholesale market, and less from retail flows.

<u>Mortgage rates</u>

9. Mr George said yesterday he expected the Halifax Building Society to cut their mortgage rate soon, by around 1% from its present 9.8%. Since the Halifax is at the top of the present range of rates, others might move by less. Certainly the Halifax have scope to come down by 1% - and possibly more - though they may seek to limit themselves to, say, ½-$^3/_4$%. It seems certain that one way or another they will move soon. A cut of around 1% in national savings rates (which were set before the last ½% cut in building society rates) would not affect the outcome.

10. Nevertheless, we should present a reduction with care. We think on reflection this will be easiest if we move all three national savings rates down by 1% (Mr Rich's original recommendation was for a 1% cut for income bonds and deposit

bonds, and a $1\frac{1}{4}$% cut for the investment account). We can then present this very simply as following the 1% cut in base rates (from $8\frac{1}{2}$% to $7\frac{1}{2}$%) since we announced the last cut in national savings rates on 17 March.

11. When the building societies do move we might then want to announce a further adjustment to rates, certainly including a cut in the general extension rate from 1 July, and possibly some further edging down of the rate on the investment account.

Summary and recommendation

12. In short, on further consideration we doubt whether there is anything in the arguments for delaying the cut in national savings rates further.

13. If you agree, we should therefore like to implement the following reductions as quickly as they can be arranged :-

	Present Rate	Proposed New Rate
Income Bonds	9%	8%
Deposit Bonds	9%	8%
Investment Account	$8\frac{1}{2}$%	$7\frac{1}{2}$%

We would present the change as simply reflecting the 1% fall in base rates since the present national savings rates were announced on 17 March.

DLP

D L C PERETZ

cc Mr E George) Bank of
Mr I Plenderleith) England

MORTGAGE LENDING AND INFLOWS TO NATIONAL SAVINGS

£ million

	Mortgage Lending			National Savings Inflows	Col 4 / Col 3
	1 Building Societies	2 Other*	3 Total	4	%
1971	1600	97	1697	632	37.2
1972	2215	316	2531	857	33.9
1973	1999	473	2472	372	15.0
1974	1490	287	1777	- 11	-
1975	2768	76	2844	423	14.9
1976	3618	55	3673	588	16.0
1977	4100	127	4227	1290	30.5
1978	5115	321	5436	1525	28.1
1979	5271	822	6093	1062	17.4
1980	5722	850	6572	1377	21.0
1981	6331	2525	8856	4192	47.3
1982	8147	5302	13449	3645	27.1
1983	10928	3756	14684	2993	20.4
1984	14530	2488	17018	3391	19.9
1985	14627	4648	19275	2490	12.9
1986	19427	7077	26504	2605	9.8
1987	14452	13982	28434	2395	8.4
1986 Q1	3883	706	4589	287	6.3
Q2	5034	1481	6515	659	10.1
Q3	5749	2364	8113	863	10.6
Q4	4761	2526	7287	796	10.9
1987 Q1	3406	2189	5595	1046	18.7
Q2	3621	3232	6853	651	9.5
Q3	3701	4323	8024	532	6.6
Q4	3724	4249	7973	166	2.1
1988 Q1	4960	3212	8172	720	8.8
Jan	1466	884	2350	298	12.7
Feb	1385	880	2265	233	10.3
March	2097	1448	3545	189	5.3
April	2220	1235	3455	157	4.5

* Banks and other mortgage lenders (excluding the public sector)

Figures in 1988 are estimates

Source: Financial Statistics and Bank of England

CONFIDENTIAL PPS

From: SIR PETER MIDDLETON

Date: 1 June 1988

CHANCELLOR

Thanks. I shd be grateful for EST to look into the suggestion @ X. In the meantime, & in current mkt conditions, we want action of the sort to be taken on NS interest rates.

cc Economic Secretary
Sir T Burns
Sir G Littler
Mr Scholar
Mr Peretz

NATIONAL SAVINGS INTEREST RATES

I appreciate the points put forward in Mr Peretz's minute of 26 May. National Savings flows are now relatively small; holding the variable rates up will not itself make much difference; and there are alternative sources of funds in the wholesale markets. But national savings rates are about the only instrument we have to convey a signal to the mortgage market. And I should avoid anything which might look like official encouragement to reduce mortgage rates - especially, of course, if today's rise in market rates becomes established. The Building Societies folk memory will make them more cautious if they detect that we are going to use national savings rates more aggressively. I therefore think we should examine the scope for this. X It would be good funding to get in more national savings and buy in long gilts, so why not do a lot more? My own inclination would be to raise the present limits of the conventional certificate, despite the tax problems, and actively promote national savings instruments.

2. A series of warning shots would be better than welcoming gestures.

PEM

P E MIDDLETON

SECRET

10 DOWNING STREET

LONDON SW1A 2AA

From the Principal Private Secretary

CH/EXCHEQUER

REC. 02 JUN1988

ACTION

COPIES TO

2 June 1988

PUS
(no distribution)

Dear Alex,

INTEREST RATES

The Prime Minister and the Chancellor of the Exchequer had a short discussion this morning about interest rates.

The Chancellor explained that recent developments in the foreign exchange markets suggested that there was a strong case for an immediate increase of ½ per cent in interest rates. The Prime Minister said that she agreed with this judgement. The Chancellor said that it might be necessary to increase interest rates by a further ½ per cent before too long. The Prime Minister hoped that this would not be the case, because of the effect on mortgage rates. But she agreed that if higher interest rates were necessary, they should be increased.

Yours sincerely

Nigel Wicks

N. L. WICKS

Alex Allan, Esq.,
H.M. Treasury.

SECRET

pmp

SECRET UNTIL ANNOUNCED

INTEREST RATE INCREASE

cc PPS
PS/EST
Mr Peretz
Mr Bush
Miss O'Mara
Mrs Ryding

FACTUAL

1. In the noon dealing round, the Bank of England accepted offers of bills 1/2 per cent above previous dealing rates.

2. Interest rate moves since 7 August 1987

1987	7 August	10%
	26 October	9 1/2%
	5 November	9%
	4 December	8 1/2%
1988	2 February	9%
	18 March	8 1/2%
	11 April	8%
	18 May	7 1/2%

3. W. Germany, Austria, Spain and Portugal markets closed for Corpus Christi Holiday.

LINE TO TAKE

Circumstances which led to the last 1/2 point cut (17 May) have reversed, so now appropriate to unwind. In line with the series of 7 previous half point moves.

POSITIVE

1. Short term interest rates will continue to be held at the levels necessary to keep monetary conditions on track. Will not take risks with inflation.

DEFENSIVE

!!

2. Further increases on the way?
Wait and see. Anyone asking to know what will happen is aiding and abetting speculators.

3. Increase will damage industry?
Industry has more to fear from resurgeance of inflation. 1% increase in

and if sustained for

SECRET UNTIL ANNOUNCED

3. Increase will damage industry?

Industry has more to fear from resurgence of inflation. 1% ~~increase~~ rise in interest rates increases costs by quarter of amount by which 1% ~~increase~~ rise in pay settlements increases them.

4. Why defend present high level of sterling which is damaging industry?

If firms accept financial discipline inherent in Government strategy and contain their costs, no need for any loss of competitiveness. Greatest threat to output and employment would come if Government relaxed its anti-inflationary stance.

5. Government applies formula whereby interest rates moved by 1 per cent for each 4 per cent opposite change in exchange rate?

No. No mechanical formula applies. Interest rate decisions taken within continuous and comprehensive assessment of monetary conditions, taking all evidence into account. Exchange rate a key indicator of monetary conditions, but not the only factor.

6. Treasury model shows that interest rates should be raised by 1 per cent for each 4 per cent fall in the exchange rate?

Appropriate interest rate response depends on exact circumstances and factors causing exchange rate movement. Clearly response should be different if caused e.g. by oil price movements / changes in other commodity prices / supply side improvements / changes in demand / changes in world conditions / changes in domestic economy. No rule to cover all cases, even approximately.

Treasury model useful analytical tool, but only if all relevant factors are taken into account. Simulations no substitute for careful assessment of evidence at each point.

7. Is Government operating a floor at DM3.15 [or any other level]?

No. ~~Would be~~ Wrong to talk about any particular level. But Government has made it clear on numerous occasions that it will not accommodate inflationary pressures through excessive depreciation of sterling.

8. Monetary conditions too loose?

No. Interest rate decisions based on continuous and comprehensive assessment of monetary conditions so as to ensure downward pressure on inflation. Will not take risks with inflation.

9. Economy overheating?

No.

- Continued growth does not necessarily mean economy is overheating.
- Supply-side improvements since 1970s allow firms to operate more efficiently at higher levels of capacity utilisation.
- CBI's latest quarterly survey (April) found little evidence of widespread overheating. 86 per cent of firms reported capacity adequate or more than adequate to meet expected demand.
- Foundations for continued supply side flexibility reinforced by strong growth in fixed investment. 32% of respondents in CBI's April quarterly survey expect to authorise increased capital expenditure over next 12

SECRET UNTIL ANNOUNCED

months; highest since 1973.

10. Why raise interest rates rather than intervene?
Judgement of best course at time.

11. Have you intervened as well?
Never comment.

12. What does this mean for mortgage rates?
Matter for mortgage lenders - ask them.

MG1 Division
2 June 1988

90/G.jfw.45/024

CONFIDENTIAL

FROM: T PIKE
DATE: 2 June 1988

1. MISS O'~~MARA~~ MOM 2/6

2. CHANCELLOR

cc PS/EST
Sir P Middleton
Sir T Burns
Sir G Littler
Mr Scholar
Mr Sedgwick
Mr Culpin
Mr Peretz
Mrs Lomax
Mr Grice o/r
Ms Ryding
Mr Hurst
Ms Bronk o/r

File: MAMC C9

Tony pl thank

✓ N.L.

M0 FIGURES

The latest weekly figures for M0, covering the first week of June, are attached. They show that the 12 month growth rate of M0 to the latest four week period was 6.5 per cent (6.4 per cent not seasonally adjusted). Annual growth of notes and coin to the same period was 6.7 per cent (6.5 per cent not seasonally adjusted). The six month annualised growth rate of notes and coin to the latest 4 weeks was 6.0 per cent, compared with 5.8 per cent in May. The seasonally adjusted figures for the last week of May and first week of June are probably distorted by faulty seasonal factors either side of the end of May Bank Holiday.

2. We have today uncovered a slight error in the May outturn figures, the revised figures are shown in the table attached. They show that the 12 month growth rate of M0 in May was 6.3 per cent, <u>not</u> 6.2 per cent as reported last week. The 12 month growth rate of notes and coin in May was 6.6 per cent, <u>not</u> 6.4 per cent as reported last week.

T. Pike

T PIKE

CONFIDENTIAL (Until Publication)

M0 : THE WIDE MONETARY BASE

Monthly data	Level £ million (Change in brackets)					Percentage change on previous month		6 month % growth annualised		Percentage change on previous year			
	Notes and Coin (nsa)	Notes and Coin (sa)	Bankers' Deposits	M0 (nsa)	M0 (sa)	Notes(sa) and Coin	M0 (sa)	Notes & Coin (sa)	M0 (sa)	Notes and Coin (nsa)	Notes and Coin (sa)	M0 (nsa)	M0 (sa)
1987 October	15299	15456 (80)	203	15501	15659 (98)	0.5	0.6	7.4	7.3	5.1	5.2	5.5	5.6
November	15365	15525 (69)	183	15548	15707 (48)	0.4	0.3	7.4	7.0	4.8	4.8	4.9	4.9
December	16447	15661 (136)	186	16633	15846 (139)	0.9	0.9	7.9	8.5	4.7	4.8	4.2	4.3
1988 January	15458	15620 (-41)	181	15638	15801 (-45)	-0.3	-0.3	6.1	5.3	4.7	4.5	4.8	4.6
February	15353	15659 (39)	124	15477	15783 (-18)	0.2	-0.1	5.3	4.5	5.7	5.7	5.3	5.3
March	15588	15753 (94)	162	15750	15916 (133)	0.6	0.8	5.0	4.6	6.9	6.4	6.4	5.8
April	15797	15826 (73)	229	16026	16055 (139)	0.5	0.9	4.8	5.1	5.8	6.1	5.9	6.2
May	15884	15968 (142)	178	16062	16146 (91)	0.9	0.6	5.8	5.7	6.1	6.6	5.8	6.3
June (1/5) @	16224	16104 (278)	215	16439	16319 (173)	0.9	1.1	5.7	6.1	8.6	6.8	9.0	7.3
Latest 4 weeks @	15945	15999 (136)	193	16138	16191 (126)	0.9	0.8	6.0	5.8	6.5	6.7	6.4	6.5

Weekly data	Level £ million (Change in brackets)			Percentage change on previous week
	Notes(sa) and Coin	Bankers' Deposits	M0 (sa)	M0 (sa)
May				
4th	15981 (119)	155	16136 (-23)	-0.1
11th	15945 (-36)	161	16106 (-30)	-0.2
18th	15985 (40)	247	16232 (126)	0.8
25th	15960 (-25)	148	16108 (-124)	-0.8
June				
1st	16104 (144)	215	16319 (211)	1.3

@ Weekly data for the current month so far include estimates for the unbacked note issue. The latest week also includes an estimate for coin.
The changes for the current month so far use as a base the previous full month and the full month a year ago.
The latest four week changes use as a base the four week averaged level four weeks ago and a year ago.

U.K. RATE MOVE TO KEEP CONDITIONS FIRM - TREASURY NRBB

LONDON, JUNE 2, REUTER - THE HALF POINT RISE IN THE BANK OF ENGLAND'S MONEY MARKET LENDING RATE WAS AIMED AT KEEPING MONETARY POLICY FIRM, TREASURY OFFICIALS SAID.

THE CIRCUMSTANCES WHICH LED TO THE LAST INTEREST RATE MOVE -- A HALF POINT CUT TO 7-1/2 PCT IN MID-MAY -- HAVE NOW REVERSED THEMSELVES, THEY ADDED. THE SCALE OF THE RISE WAS IN LINE WITH THE PREVIOUS SEVEN INTEREST RATE MOVES, ALL OF WHICH WERE HALF POINT CHANGES, THEY SAID.

NEITHER TREASURY NOR BANK OF ENGLAND OFFICIALS REFERRED SPECIFICALLY TO THURSDAY'S SHARP FALL IN STERLING, WHICH BEGAN TO REVERSE ITSELF SHORTLY AFTER THE INTEREST RATE MOVE.

02-JUN-1143. MON448 MONQ

ENDS

P

MON/SHIP - SEE AAAA1218

STERLING RALLIES AFTER U.K. RATE HIKE NRBC

LONDON, JUNE 2, REUTER - THE POUND RALLIED TWO PFENNIGS AFTER THE BANK OF ENGLAND SIGNALLED A HALF POINT RISE IN U.K. BASE RATES, DEALERS SAID.

AT 1134 GMT, IT TRADED AT AROUND 3.1350 MARKS, UP FROM A 3.1150 LOW TOUCHED BEFORE THE BANK RAISED ITS MONEY MARKET LENDING RATE.

BUT MOST DEALERS DOUBTED IT COULD RALLY MUCH FURTHER, AFTER THE SHARP TURN IN SENTIMENT YESTERDAY FUELLED BY TRADE AND INFLATION WORRIES IN THE U.K.

02-JUN-1144. MON449 MONQ

CONTINUED ON - NRBD

P

MON/SHIP - SEE AAAA1218

STERLING RALLIES =2 LONDON NRBD

SOME DEALERS SAID THE INTEREST RATE MOVE BY THE BANK OF ENGLAND REFLECTED THE TREASURY'S EAGERNESS TO ENSURE A STABLE EXCHANGE RATE FOR STERLING, AFTER ITS RECENT SHARP FALL, AS WELL AS THE DESIRE TO KEEP MONETARY CONDITIONS TIGHT.

THEREFORE, THEY WERE WARY OF CENTRAL BANK INTERVENTION SHOULD THE POUND RALLY MUCH FURTHER.

02-JUN-1153. MON464 MONQ

CONTINUED FROM - NRBC

ENDS

P

MON/SHIP - SEE AAAA1218

BANK OF ENGLAND RAISES MONEY MARKET RATE 1/2 POINT NRAO

LONDON, JUNE 2, REUTER - THE BANK OF ENGLAND SAID IT RAISED ITS MONEY MARKET LENDING RATE BY 1/2 POINT TO EIGHT PCT.

THIS IS A CLEAR SIGNAL TO THE MARKET THAT THE BANK SEEKS A 1/2 POINT RISE IN CLEARING BANK BASE LENDING RATES TO EIGHT PCT, AND A MOVE FROM THE CLEARING BANKS IS EXPECTED IMMINENTLY, DEALERS SAID.

THE BANK'S MOVE COMES AFTER A SHARP RISE IN MONEY MARKET RATES FOLLOWING A STEEP DECLINE IN STERLING WHICH BEGAN WEDNESDAY MORNING.

02-JUN-1111. MON396 MONP

CONTINUED ON - NRAP

P

MON/SHIP - SEE AAAA1218

BANK OF ENGLAND RAISES =2 LONDON NRAP

THE BANK SAID DISCOUNT HOUSES WISHING TO ITS BORROWING FACILITIES TODAY ARE INVITED TO DO SO AT 1330 GMT, WHEN THE INTEREST RATE WILL BE EIGHT PCT.

IT SAID IT WOULD NOT BE BUYING BILLS FROM THE HOUSES TODAY.

SPOKESMEN FOR THE MAJOR U.K. CLEARING BANKS TOLD REUTERS THEY WERE REVIEWING THEIR BASE RATES IN LIGHT OF THE BANK OF ENGLAND'S MOVE. BASE RATES HAVE STOOD AT 7-1/2 PCT SINCE MAY 17, WHEN THE RATE WAS CUT BY 1/2 POINT.

02-JUN-1130. MON425 MONP

CONTINUED FROM - NRAO

CONTINUED ON - NRBT

P

MON/SHIP - SEE AAAA1218

BANK OF ENGLAND RAISES =3 LONDON NRBT

THE BANK HAD FAILED TO SIGNAL ANY MOVE ON INTEREST RATES DURING ITS ROUTINE MONEY MARKET FORECAST EARLY THIS MORNING AND THIS EASED FEARS OF AN IMMINENT RISE. HOWEVER, STERLING CONTINUED TO SLIDE AND THE PRESSURE BECAME TOO MUCH WHEN IT FELL BELOW 3.12 MARKS, DEALERS SAID.

THE KEY THREE MONTH STERLING INTERBANK RATE WAS THEN 5/16 POINT UP AT 8-5/16 3/16, DISCOUNTING AT LEAST A 1/2 POINT RISE IN BASE RATES. STERLING RALLIED QUICKLY AFTER THE RATE RISE TO AROUND 3.1350 MARKS AND MONEY RATES STEADIED, WITH SEPTEMBER THREE MONTH STERLING FUTURES RECOVERING TO STAND 14 TICKS DOWN AT 90.65 AFTER EARLIER HITTING 90.48.

AAMM 1157 BARCLAYS SAYS IT RAISING BASE LENDING RATE BY 1/2 POINT TO EIGHT PCT ENDS

P

MON/SHIP - SEE AAAA1218

mjd 3/147m

CONFIDENTIAL

FROM: MISS M P WALLACE
DATE: 2 June 1988

PS/ECONOMIC SECRETARY

cc Sir P Middleton
Sir T Burns
Sir G Littler
Mr Scholar
Mr Peretz

NATIONAL SAVINGS INTEREST RATES

The Chancellor has seen and was grateful for Sir P Middleton's minute of 1 June. He would be most grateful if the Economic Secretary could consider the suggestion that it would be good funding to get in considerably more in national savings, while buying in long gilts. However, in the meantime, and in the current market conditions, his view is that no action of any kind should be taken on national savings interest rates.

MPW

MOIRA WALLACE

91/G.LCLD.4515.030

55/6

cc PPS
PS/EST
Sir P Middleton
Sir T. Burns

This may be of interest!

MR PERETZ

FROM: T PIKE
DATE: 3 June 1988

cc Mr Scholar
Mr Grice o/r
Miss O'Mara
Mrs Ryding
Ms Bronk o/r
Mr Wheatley
File: MAMC B7

3/6

EFFECT ON MORTGAGE LENDING OF BUDGET MEASURES

You asked Ms Bronk for a time series of building societies' commitments figures, broken down by commitments for house purchase and other uses (mostly home improvements). The table attached shows these figures back to 1980, together with comparable figures for advances.

2. The table shows that both commitments for house purchase and other uses jumped up in February and again in March and, although they fell back slightly in April, both were still very high in comparison with other months. The advances figures show a similar pattern, both series jumping up in March and remaining very high in April. But the figures suggest that if the Budget measures have been partly responsible for the high level of commitments in March and April, they have not fed through yet into advances. It appears that the jump in advances, both for house purchase and other uses, in March may have reflected February's jump in commitments. (The one month lag between commitments and advances is also evident in December/January.) However, there is little correlation between advances in April and commitments in March, suggesting that the bulk of the increase in March's commitments figures will appear in advances for May and future months.* (Ms Bronk's note of 19 May to the Economic Secretary pointed out that to forestall the tax changes, borrowers only require a commitment from the lender, which might not be drawn-down for several months.)

T. Pike

T PIKE

*An econometric analysis of the advances and commitments figures since January 1984 gives the following results:

House purchase (logs)

Adv =	0.336	+	0.694 Com (-1)	+	0.260 Com (-3)
	(1.0)		(14.0)		(4.7)

Other (logs)

Adv =	0.298	+	0.600 Com (-1)	+	0.352 Com (-3)
	(1.0)		(8.4)		(4.6)

(t statistics in brackets)

The House Purchase equation explains 92 per cent of the variation in the dependent variable; the 'Other' equation explains 88 per cent. Hence both equations indicate a well determined relationship between advances and commitments lagged one month and, to a lesser extent, commitments lagged three months.

Based on the above equations, the predicted level of advances for house purchase in April is 6000, compared with an outturn of 3267, an error of over 80 per cent. Similarly, the predicted level of advances for other uses in April is 1300, compared with an outturn of 632, an error of over 100 per cent. This suggests that if the Budget measures were inflating commitments in March, they have not yet appeared in the advances figures.

BUILDING SOCIETIES' COMMITMENTS AND ADVANCES FOR HOUSE PURCHASE AND OTHER USES (MONTHLY AVERAGES)

£ million

	COMMITMENTS			ADVANCES		
	Total	o/w House Purchase	Other	Total	o/w House Purchase	Other
1980	852	850	2	801	799	2
1981	996	893	103	999	905	94
1982	1408	1238	170	1278	1129	149
1983	1613	1442	171	1605	1433	172
1984	2053	1837	216	2003	1795	208
1985	2314	2016	298	2208	1940	268
1986	3154	2694	460	3078	2640	438
1987	3065	2687	378	2946	2540	406
1986 Q1	2620	2278	342	2275	1964	311
Q2	3793	3234	559	3147	2709	438
Q3	3578	3016	562	3684	3153	531
Q4	2626	2248	378	3206	2734	472
1987 Q1	2526	2215	311	2330	1987	343
Q2	3212	2812	400	2929	2533	396
Q3	3282	2878	404	3220	2786	434
Q4	3240	2841	399	3304	2852	452
1988 Q1	4385	3707	678	3386	2867	519
1987 Oct	3441	3044	397	3319	2887	432
Nov	3351	2952	399	3346	2878	468
Dec	2928	2527	401	3248	2791	457
1988 Jan	2891	2489	402	2793	2328	465
Feb	4321	3761	560	3106	2666	440
March	5943	4871	1072	4260	3608	652
April	4817	4160	657	3899	3267	632

Source: Financial Statistics, Table 7.8. Note: The figures are grossed up from the returns of the 15 largest building societies.

Moira
~~Isn't X~~ such
~~sh~~ amended?

SECRET UNTIL ANNOUNCED

INTEREST RATE INCREASE

cc PPS
PS/EST
Mr Peretz
Mr Gieve
Mr Bush
Mr Nelson

spoke

A...

FACTUAL

1. At noon today the Bank of England announced a 1/2 per cent increase in its dealing rates.

2. Interest rate moves since 7 August 1987

pmp

1987	7 August	10%
	26 October	9 1/2%
	5 November	9%
	4 December	8 1/2%
1988	2 February	9%
	18 March	8 1/2%
	11 April	8%
	18 May	7 1/2%
	2 June	8%
	6 June	8 1/2%

LINE TO TAKE

Decided it was appropriate to tighten monetary conditions a little.

POSITIVE

1. Short term interest rates will continue to be held at the levels necessary to keep monetary conditions on track. Will not take risks with inflation.

DEFENSIVE

1. Why moving again so soon? Why didn't you do 1% last Thursday? Exchange rate not very different from then?

Interest rate movements are normally 1/2% (12 out of last 13), and exchange market conditions changed very suddenly last week: it was only sensible to see how conditions developed.

2. Government applies formula whereby interest rates moved by 1 per cent for each 4 per cent opposite change in exchange rate?

No. No mechanical formula applies. Interest rate decisions taken within continuous and comprehensive assessment of monetary conditions, taking all evidence into account. Exchange rate a key indicator of monetary conditions, but not the only factor.

X

SECRET UNTIL ANNOUNCED

3. Further increases on the way?
Never speculate.

4. Increase will damage industry?
Industry has more to fear from resurgence of inflation. 1% rise in interest rates, even if sustained for whole year, increases costs by quarter of amount by which 1% rise in pay settlements increases them.

5. Why defend level of sterling which is damaging industry?
If firms accept financial discipline inherent in Government strategy and contain their costs, no need for any loss of competitiveness. Greatest threat to output and employment would come if Government relaxed its anti-inflationary stance.

6. Treasury model shows that interest rates should be raised by 1 per cent for each 4 per cent fall in the exchange rate?
Interest rate changes are not decided by Treasury model, but by the authorities exercising their judgement as in any other well-conducted country.

7. Is Government operating a floor at DM3.10 [or any other level]?
Not helpful to talk about any specific level. But Government has made it clear on numerous occasions that it will not allow sterling to depreciate to accommodate excessive increase in domestic costs.

8. Monetary conditions too loose?
No. Interest rate decisions based on continuous and comprehensive assessment of monetary conditions so as to ensure downward pressure on inflation. Will not take risks with inflation.

9. Economy overheating?
No.
- Continued growth does not necessarily mean economy is overheating.
- Supply-side improvements since 1970s allow firms to operate more efficiently at higher levels of capacity utilisation.
- CBI's latest quarterly survey (April) found little evidence of widespread overheating. 86 per cent of firms reported capacity adequate or more than adequate to meet expected demand.
- Foundations for continued supply side flexibility reinforced by strong growth in fixed investment. 32% of respondents in CBI's April quarterly survey expect to authorise increased capital expenditure over next 12 months; highest since 1973.

10. Why raise interest rates rather than intervene?
Judgement of best course at time.

11. Have you intervened as well?
Never comment.

12. What does this mean for mortgage rates?
Matter for mortgage lenders - ask them.

MG1 Division

6 June 1988

pup

10 DOWNING STREET

LONDON SW1A 2AA

From the Private Secretary

6 June 1988

Dear Alex,

INTEREST RATES

The Chancellor came to see the Prime Minister this morning to discuss the position in the markets. He said that, following last week's half percent interest rate increase, the exchange rate had continued to fall a little further. But the position had then stabilised, and remained calm this morning. He had concluded, however, that a further half percent interest rate increase would be appropriate in order to tighten monetary conditions; he saw considerable attraction in making adjustments of half percent, rather than waiting for the possible need for a larger adjustment.

After a brief disussion, it was agreed that the Bank of England should signal a half percent interest rate increase at noon today, and that it would be necessary then to keep the position in the markets - and the possible need for any further adjustments - under review.

Yours,

Paul

(PAUL GRAY)

Alex Allan, Esq.,
HM Treasury.

90/G.jfw.45/024

CONFIDENTIAL

FROM: T PIKE
DATE: 9 June 1988

1. MR ~~GRICE~~

2. ECONOMIC SECRETARY

Although the weekly figures are erratic, it would be more reassuring if the growth rates began to decline towards the target range, rather than accelerating.

JWG 9.6.88

cc PS/Chancellor
Sir P Middleton
Sir T Burns
Sir G Littler
Mr Scholar o/r
Mr Sedgwick
Mr Culpin
Mr Peretz o/r
Mrs Lomax
Miss O'Mara o/r
Ms Ryding o/r
Mr Hurst
Ms Bronk

File: MAMC C9

M0 FIGURES

The latest weekly figures for M0, covering the second week of June, are attached. They show that the 12 month growth rate of M0 to the latest four week period was 6.7 per cent (6.7 per cent not seasonally adjusted). The sa and nsa 12 month growth rates of notes and coin to the same period were also 6.7 per cent.

2. Six month annualised growth of notes and coin to the latest four week period was 6.0 per cent, compared to 5.8 per cent in May.

T Pike

T PIKE

TABLE 16

CONFIDENTIAL (Until Publication)

M0 : THE WIDE MONETARY BASE

Monthly data	Level £ million (Change in brackets)					Percentage change on previous month		6 month % growth annualised		Percentage change on previous year			
	Notes and Coin (nsa)	Notes and Coin (sa)	Bankers' Deposits	M0 (nsa)	M0 (sa)	Notes(sa) and Coin	M0 (sa)	Notes & Coin (sa)	M0 (sa)	Notes and Coin (nsa)	Notes and Coin (sa)	M0 (nsa)	M0 (sa)
1987 October	15299	15456 (80)	203	15501	15659 (98)	0.5	0.6	7.4	7.3	5.1	5.2	5.5	5.6
November	15365	15525 (69)	183	15548	15707 (48)	0.4	0.3	7.4	7.0	4.8	4.8	4.9	4.9
December	16447	15661 (136)	186	16633	15846 (139)	0.9	0.9	7.9	8.5	4.7	4.8	4.2	4.3
1988 January	15458	15620 (-41)	181	15638	15801 (-45)	-0.3	-0.3	6.1	5.3	4.7	4.5	4.8	4.6
February	15353	15659 (39)	124	15477	15783 (-18)	0.2	-0.1	5.3	4.5	5.7	5.7	5.3	5.3
March	15588	15753 (94)	162	15750	15916 (133)	0.6	0.8	5.0	4.6	6.9	6.4	6.4	5.8
April	15797	15826 (73)	229	16026	16055 (139)	0.5	0.9	4.8	5.1	5.8	6.1	5.9	6.2
May	15884	15968 (142)	178	16062	16146 (91)	0.9	0.6	5.8	5.7	6.1	6.6	5.8	6.3
June (2/5) a	16087	16085 (259)	225	16312	16310 (164)	0.7	1.0	5.5	5.9	7.6	6.7	8.2	7.2
Latest 4 weeks a	15989	16029 (123)	211	16200	16240 (116)	0.8	0.7	6.0	6.4	6.7	6.7	6.7	6.7

Weekly data	Level £ million (Change in brackets)			Percentage change on previous week
	Notes(sa) and Coin	Bankers' Deposits	M0 (sa)	M0 (sa)
May				
4th	15981 (119)	155	16136 (-23)	-0.1
11th	15945 (-36)	161	16106 (-30)	-0.2
18th	15985 (40)	247	16232 (126)	0.8
25th	15960 (-25)	148	16108 (-124)	-0.8
June				
1st	16104 (144)	215	16319 (211)	1.3
8th	16066 (-38)	235	16301 (-18)	-0.1

a Weekly data for the current month so far include estimates for the unbacked note issue. The latest week also includes an estimate for coin.
The changes for the current month so far use as a base the previous full month and the full month a year ago.
The latest four week changes use as a base the four week averaged level four weeks ago and a year ago.

SECRET AND PERSONAL

Tony D. pl
Thanks

FROM: T PIKE
DATE: 9 June 1988

1. MR GRICE
2. CHANCELLOR

Comfort from the drop in the M3 growth rate has to be tempered by the other considerations in para 2. But the bank lending figures look better.
JWG 9.6.88

cc Economic Secretary
Sir P Middleton
Sir T Burns
Mr Scholar o/r
Mr Peretz
Miss O'Mara o/r
Mrs Ryding o/r
Mr Wheatley
Ms Bronk
Mr Gray No 10

MONEY SUPPLY IN MAY: "FIRST GUESS" FOR M3 AND OUTTURN FOR M0

(All figures are unadjusted unless specified otherwise)

Table 1 summarises the Bank's "first guess" at the M3 figures for May, which are still subject to significant revision, and shows the confirmed outturn figures for M0 that were circulated on 2 June.

Table 1: Growth of Monetary Aggregates in May

per cent

	M0	M3**
Annual growth rate*	5.9 (6.3)	17.3 to 18.1
Change in month*	0.2 (0.6)	0.3 to 1.1 (-0.4 to 0.4)
Target range	1-5	-

* Figures in brackets are seasonally adjusted

** The actual outturn has been within the range forecast on this basis in 15 of the last 19 months.

2. 12 month growth of M3 in May of around 17¾ per cent compares with 19¼ per cent in the 12 months to April. The low outturn for 12 month M3 growth suggested by these figures may reflect in part an M3 overfund of over £6½ billion in the 12 months to May (equivalent to 4 per cent growth of M3). There are as yet no figures for M4, but another month of strong retail inflows to building societies (probably about £1.8 billion sa, including interest credited, compared to £1.6 billion in April) suggests that the slowdown in M4 growth will not be as sharp as that of M3 growth.

3. The increase in sterling bank lending in May is likely to be in the range £2.3-4.3 billion both nsa and sa. This shows some slackening from recent levels. This owes something to the unwinding of last month's lending to GEMM's.

M3 components and counterparts

4. Table 2 (attached) compares the changes in M3 components underlying the "first guess" with the average monthly change over the previous 12 months. Table 3 (attached) provides a similar comparison for M3 counterparts.

Timetable

5. We expect to receive provisional May figures on Wednesday 15 June. They will be published on Monday 20 June. Full money and banking figures for May will appear on Wednesday 29 June.

T. Pike

T PIKE

TABLE 2: M3 COMPONENTS - MAY 1988

"First Guess" compared with average monthly change in the previous year.

£ millions

	First Guess	**Average monthly change in previous 12 months**
Notes and coins in circulation	- 180	90
Non-interest bearing sight	212	370
Interest bearing sight	2257	940
Time deposits (including (CDs)	-1067	1220
Grossing up to full population	165	-
	-----	-----
Change in M3	1387	2620
	-----	-----

SECRET AND PERSONAL

TABLE 3 : M3 COUNTERPARTS - MAY 1988

"First guess compared with average monthly change in the previous year

£ millions

		First Guess		Average change in previous 12 months
CGBR (O) (ex bank deposits)		-308		-570
Other public sector:				
LABR)				
PCBR)		-178		120
OPS debt sales)				
		------		------
Modified PSBR*		-486		-450
CG debt: Gilts	460		-250	
Treasury bills	32		-20	
National Savings	-89		-170	
CTD's etc.	117		0	
		------		------
Total CG debt sales (-)		520		-440
External and fc finance of public sector (-)		289		470
		------		------
Public sector contribution		323		-420
		------		------
Sterling lending to nbps (incl Issue Dept commercial bills)		3321 #		3980
Net private externals		-630		-590
Residual (includes NNDLS and reporting differences)		-1627		-350
		------		------
Change in M3		1387		2620
		------		------
(Monthly percentage change)		(0.7%)		(1.5%)
(12 month percentage change)		(17.7%)		(20.9%)

---

* Modified PSBR equals PSBR less OPS debt sales

\# £3338 million after seasonal adjustment.

sw11 RESTRICTED

FROM: S W MATTHEWS
DATE: 10 June 1988

CHANCELLOR

cc: Economic Secretary
Sir P Middleton
Sir T Burns
Sir G Littler
Mr Byatt
Mr Lankester
Mr Monck
Mr Scholar
Mr Evans
Mr Mountfield
Mr Odling-Smee
Mr Peretz
Mr Sedgwick
Mr Turnbull
Mr Bottrill
Mr S Davies
Mr Grice
Mr Hibberd
Mr Mowl
Mr Dolphin
Mr Savage
Mr Allen
Mr Cropper
Mr Tyrie

Thanks. I am surprised at 3% growth forecast for G7 in 1988. The German numbers only expect around 2%. N

WORLD ECONOMIC PROSPECTS: JUNE 1988

I attach a report on the latest WEP exercise.

2. Since the update of the forecast of the domestic economy is not yet complete the report contains no numbers for the UK. As usual, forecasts are presented for the major seven industrialised countries as a whole: possible revision to the UK figures within this aggregate would effect the overall picture only marginally.

SM.

S W MATTHEWS

td21

WORLD ECONOMIC PROSPECTS: JUNE 1988

Table 1 summarises the forecast. The main points are:

a. Activity in the major industrialised countries grew particularly rapidly in the second half of 1987. There appears to have been little loss of momentum in the first quarter of 1988 and real GNP in the major seven is expected to be 4 per cent higher in 1988 than in 1987.

b. The strengthening of activity was not confined to the major seven, and world trade volumes picked up sharply towards the end of 1987. They are forecast to continue to grow strongly in 1988.

c. Stronger activity has contributed to large rises in industrial materials prices (except oil), although in real terms they remain below their average levels of the past 20 years.

d. The average rate of consumer price inflation in the major seven remains low, but the rise in commodity prices may lead to a small rise in 1989.

e. Some tightening of macroeconomic policy in 1989 in the US (with no offsetting easing of policy elsewhere) is assumed. Real exchange rates remain unchanged from current levels.

Table 1: Output, Inflation and Trade

Percentage change on year earlier	1986	1987	1988	1989	1990
Major 7 real GNP	2.7	3.0	4	2¾	2½
Major 7 real domestic demand	3.7	3.1	4	2½	2½
Major 7 industrial production	0.9	3.3	6½	4¼	3¾
Major 7 consumers' expenditure deflator	2.3	2.9	3	4	3½
World trade					
- total	5.2	5.4	8¾	4¾	5
- manufactures	2.0	6.0	10	5	5¼

I. ACTIVITY IN THE MAJOR INDUSTRIALISED COUNTRIES

2. After the sharp recovery in 1983-84 from the recession of the early 1980s, real GNP in the major countries has grown at around 3 per cent a year. From roughly mid-1986 to mid-1987 growth dipped to around 2½ per cent, partly as a consequence of the collapse in oil and other commodity prices: the boost that this gave to consumers' expenditure and domestic demand in the industrial countries being more than offset initially by the decline in their exports to OPEC and other developing countries, which experienced corresponding terms of trade losses and cut their imports sharply.

3. Output in the major industrialised countries picked up strongly in the second half of 1987, particularly in North America and Japan. Business investment, exports and industrial production all grew quickly, while consumers' expenditure growth levelled off as saving ratios stopped falling. Early indicators for 1988 (including further sharp increases in commodity prices) suggest that activity has continued to grow strongly, though annual growth rates of industrial production have levelled off. The fall in stockmarkets in October has had little effect on activity so far.

4. The main factors behind the strengthening of activity appear to be:

a. some recovery in developing countries' imports (helped by stronger commodity prices);

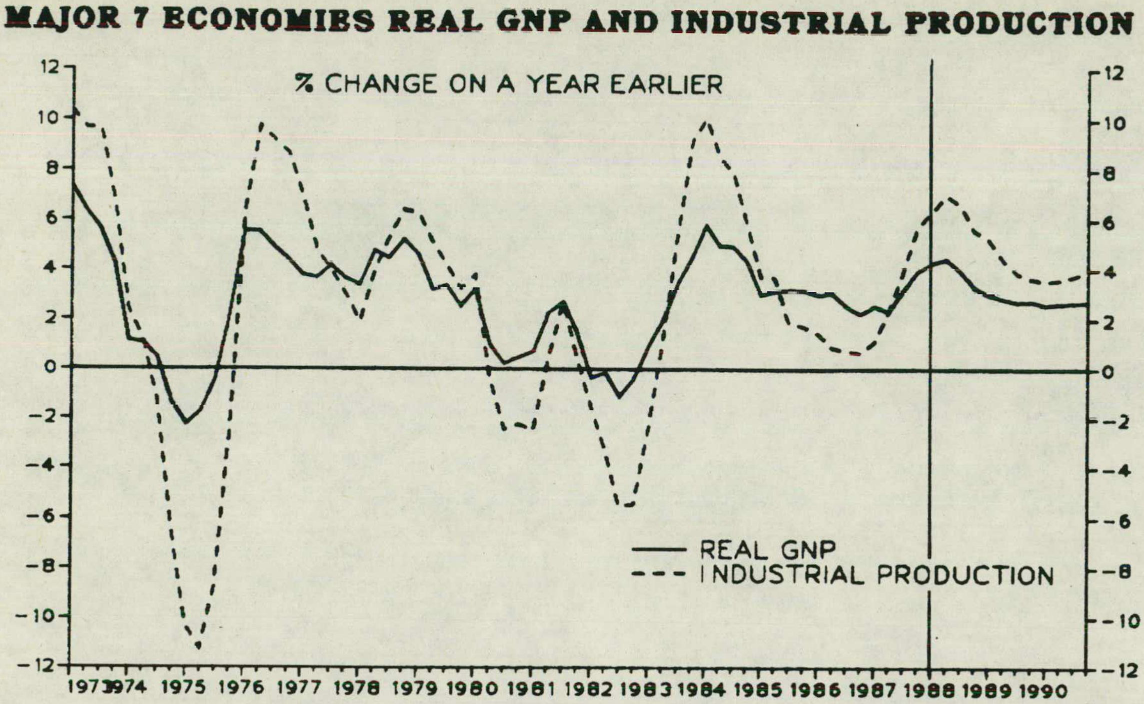
b. lower nominal and real interest rates;

c. relatively stable exchange rates; and

d. a relaxation of Japanese fiscal policy.

Though few data are available for other countries, it is clear from trade data that the strengthening of activity towards the end of 1987 was not confined to the major seven. In the fourth quarter in particular world trade seems to have expanded very strongly.

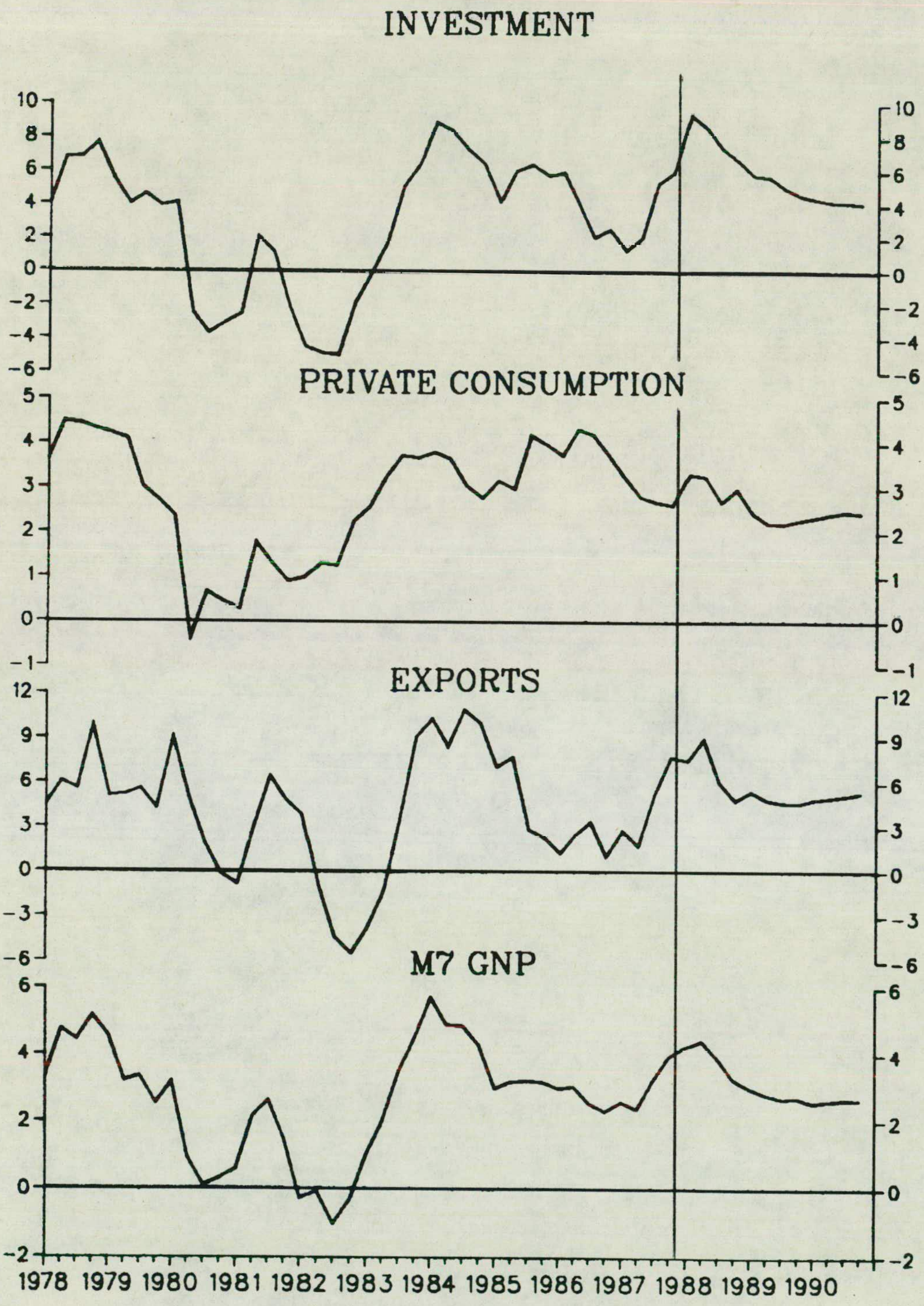
Chart 1: Real GNP and Industrial Production Growth



5. The key short-term judgement in this forecast is how long activity will continue to grow as strongly as in the second half of 1987. There is little indication yet of any slowing down. First quarter national accounts data for the United States, Germany and France show strong growth, major seven industrial output was about 6 per cent higher in March 1988 than a year earlier, and commodity prices continue to increase rapidly. (More details of recent indicators are given in the World Economic Developments note circulated on 6 June).

6. The upswing in fixed investment in the major countries during 1987 is expected to be shorter and less strong than previous upswings because the preceding weakening of growth was only modest. As a result activity is projected to slow during 1988. Thus the major seven grow by 3¼ per cent in the year to 1988Q4 (compared to 4 per cent in the year to 1987Q4). This nevertheless produces a year-on-year growth rate of 4 per cent for 1988. Although growth could be a little higher, if the upswing is more

CHART 2 : COMPONENTS OF MAJOR SEVEN GROWTH



PERCENTAGE CHANGE OVER YEAR EARLIER

extended than expected, there are also downside risks to this outlook and most other forecasters currently put growth for 1988 at nearer 3 per cent.

Table 2: Growth of Real GNP and Contribution of Domestic Demand

Percentage change on year earlier	GDP/GNP 1987	1988	1989	1990	Estimated Growth of Productive Potential
US	2.9	3.8	2.3	2.1	2¼-2¾
Japan	4.2	5.7	4.5	4.1	3½-4½
Germany	1.7	3.0	2.3	2.7	2 -2½
France	2.2	2.9	2.2	2.6	2 -2½
Major 7	3.0	4.0	2.8	2.6	2½-2¾

Percentage change on year earlier	Domestic Demand Contribution 1987	1988	1989	1990
US	2.2	2.7	1.4	1.4
Japan	4.9	6.9	5.3	4.7
Germany	2.8	4.2	2.6	3.6
France	3.3	3.9	2.3	2.5
Major 7	3.3	4.3	2.8	2.7

7. Real GNP growth in the major seven is forecast to fall back in 1989 and 1990 to a rate broadly in line with productive potential. Section VI of the report discusses the risks of a more sustained (and inflationary) boom on the one hand and a more marked slowdown (or even recession) on the other.

8. In the **United States** real GNP growth is forecast to exceed domestic demand growth over the next few years as competitiveness gains from the fall in the dollar over the last few years continue to produce rapid export growth. But as these effects wear off export and business investment growth are expected to fall. With the assumed policy-induced slow growth of government and consumers' expenditure, GNP growth could fall below potential during 1989 and 1990 but this is hardly a recession.

9. In Japan and continental Europe the reverse is true. Domestic demand in **Japan** is already growing more than fast enough to offset the decline in net exports consequent on the yen's appreciation, and it is expected to continue to grow strongly. In **Europe** growth has been below potential for the last two years, but there are now some signs of a recovery. This should be maintained, and growth at, or just above potential is forecast for the next few years.

II. WORLD TRADE

10. World import volumes are estimated to have grown by about 5½ per cent in 1987, with developed countries' imports growing less rapidly than in 1986, but developing countries' imports accelerating. As with activity, world trade growth in both developed and developing countries seems to have been particularly strong in the second half of the year. The recovery in developing countries' imports has boosted trade in manufactures, which is estimated to have grown by 6 per cent, compared with just 2 per cent growth in 1986. All these figures are still subject to a substantial error margin.

Table 3: World Import Growth

Percentage change on year earlier	(Share of 1986 imports)	1986	1987	1988	1989	1990
Total developed economies*	(75)	8½	6½	8½	4½	4½
of which:						
US	(18)	14	5	8	-½	-½
Japan	(6)	13½	8	14½	8½	9
EC(6)**	(33)	6½	7	8½	4½	5½
OPEC	(5)	-22	-10	7	1	2
NICs	(6)	19	23	18	12	12
Other NODCs	(9)	-3½	-	7	4	4
Total***	(100)	5	5½	8½	4½	5
World trade in manufactures		2	6	10	5	5

* OECD plus South Africa
** Belgium, France, Germany, Italy, Netherlands and UK
*** Includes net imports by centrally planned economies.

11. The rapid growth at the end of 1987 means that year-on-year world trade growth will inevitably be high in 1988. Some fall in the growth of developed countries' imports is expected during 1988, in line with activity (see paragraph 6), but this may well be offset by markedly higher imports by developing countries. As a result total world imports could grow by around 8½ per cent - much the same as in the sharp upswing of 1984 (although this was still somewhat below earlier upswings). However, world trade growth is likely to be more broadly based than in 1984, when US imports grew by 25 per cent, with rapid growth in imports worldwide. Trade in manufactures is expected to grow by around 10 per cent.

12. One of the main features of the world trade forecast is the continued strength of US imports, reflecting the continued buoyancy of domestic demand and relatively high rates of capacity utilisation in US industry. In 1984-85 US imports grew strongly as a result of the consumer boom. High imports now appear to be related to the strength of business investment, which in turn is associated with rapid export growth.

13. Non-OPEC developing countries' prospects are summarised in Table 4. The overall picture is for continued fast growth in export volumes combined with a pick up in import volumes. There is already some evidence that the latter were expanding rapidly towards the end of 1987.

Table 4: NODCs Current Account

Percentage change on a year earlier	1986	1987	1988	1989	1990
Export volume growth	5.0	12.7	8.1	5.6	5.6
Import volume growth	2.2	4.9	10.2	6.1	6.2
Terms of trade	-0.2	-1.5	1.7	0.6	0.2
Current account ($bn)	-13	7	8	6	6

14. The aggregate forecast conceals a wide diverge of experience. The four Asian NICs (Taiwan, Korea, Singapore and Hong Kong) have been increasing their share of world trade for several years, and their aggregate trade surplus has widened. There is now evidence

that their import volumes have begun to increase rapidly - by almost 25 per cent in 1987. This rapid import growth should be maintained in line with continued strong export growth (reflecting their continuing competitiveness), and with only modest reductions in their current account surplus.

Table 5: Asian NICs

Percentage change on year earlier	1986	1987	1988	1989	1990
Export volumes	17	19	12	10	10
Import volumes	19	23	18	12	12
Terms of trade	4	-1	2	0	0
Current Account ($bn)	23	32	32	31	30

15. Data on other developing countries' trade for 1987 is still sketchy. It appears that rapid export volume growth and some recovery in commodity prices combined with modest import growth to produce a significant improvement in their current account deficit. On the assumption that financing constraints will not compel any further improvement in these countries' aggregate current account position, the forecast is that increases in export values will be matched by increases in imports this year. With commodity prices so strong in 1988 (see below) this should mean rapid import growth this year. While this is far from being a transformation in the position of developing debtor countries it does represent a marked change in their fortunes.

16. The trade data for OPEC are extremely unreliable, but it appears that their import volumes have now levelled off following sharp falls in 1986 and the first part of 1987 in response to the collapse in oil prices.

III. PRICES AND INFLATION

a. The oil market

17. Trends in demand and non-OPEC supply suggest modest increases in the demand for OPEC oil over the next few years. Consequently, oil prices look likely to remain weak. This may seem somewhat surprising given the buoyancy of the world economy, but the discord within OPEC appears to be such that any short-term strengthening of demand would call forth additional oil production, rather than lead to a more concerted (and restrictive) OPEC supply policy. The forecast is therefore an average oil price (for OECD imports) of $16 per barrel in the second half of 1988 and the first half of 1989, with broadly unchanged real prices thereafter. The margins of error around this forecast continue to be substantial.

Table 6: The Oil Market

Millions of barrels per day	1986	1987	1988	1989	1990
Total Demand	48.3	48.6	49.5	50.2	51.1
Supply					
Non-OPEC	28.8	29.3	29.3	29.5	29.7
OPEC	19.5	19.3	20.2	20.7	21.4
Oil price* ($ pb)	14.3	17.2	15.8	16.2	17.0

* Average price of oil imported into OECD countries (fob).

b. Non-oil commodity prices

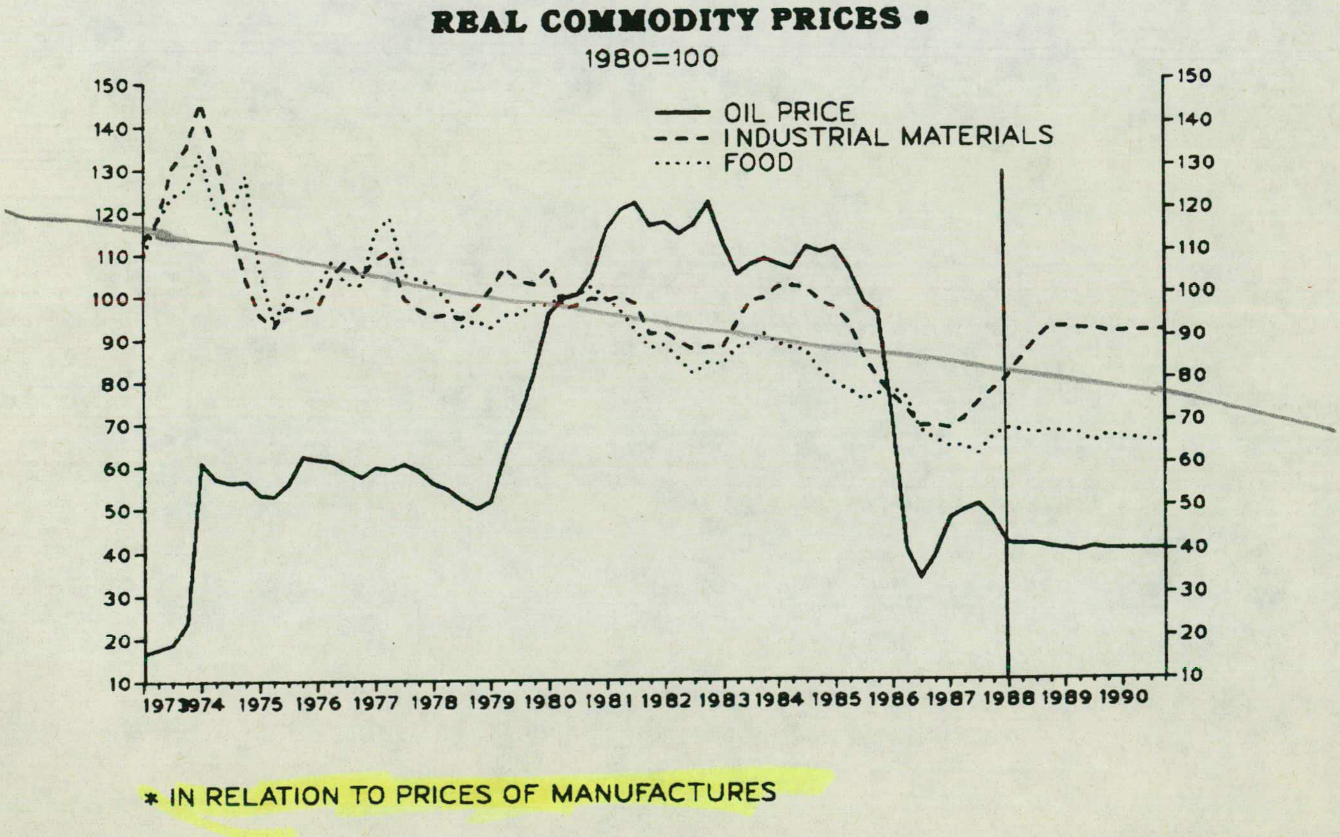
18. Non-oil commodity prices have been rising strongly since the beginning of 1987. In SDR terms, the Economist index of spot prices has risen almost 50 per cent over the past twelve months, with prices of metals doubling. Even food prices have recovered somewhat recently. The WEP model uses a wider measure of

commodity prices than the Economist index and incorporates long-term contract prices not just spot prices. This series tends to fluctuate rather less than measures of spot prices. Even this measure has non-food commodity prices 17 per cent higher in SDR terms than a year earlier in 1988Q1.

19. The recent strength of commodity prices is undoubtedly associated with the surge in world industrial activity, and because activity is expected to remain buoyant, further significant rises are expected during the remainder of 1988. Indeed, because it tends to lag spot prices, further increases in the WEP commodity price measure are almost inevitable.

20. By 1988Q4 real, non-food commodity prices are forecast to be some 35 per cent above their 1986 trough. Thereafter, as the rate of growth of world activity falls back to average levels, real non-food prices are expected to level off. Given the continuing over-supply of many foodstuffs - encouraged by high levels of support in many OECD countries - there may be some reversal of the recent rises in food prices.

<u>**Chart 3: Real Commodity Prices**</u>



C. Inflation in the major countries

21. Consumer price inflation in the major industrial countries has averaged around 3 per cent a year since the effects of the fall in oil prices dropped out in the middle of 1987. In Japan prices are still lower than two years ago, while in Germany they have risen just 1 per cent over the same period. Recent monthly figures provide no evidence of a pick up in consumer price inflation.

Table 7: Consumer Prices

Percentage change on year earlier	Consumers' Expenditure Deflator			
	1987	1988	1989	1990
US	4.1	3.9	4.9	4.8
Japan	-0.1	1.1	3.1	2.3
Germany	0.5	1.4	2.0	1.4
France	3.2	2.5	2.6	2.7
Major 7	2.9	3.1	3.9	3.5

22. There are, however, some signs pointing to some build up of inflationary pressures. The rise in non-oil commodity prices, is expected to lead to some increase in inflation, though because prices are rising from very low levels, the effect on consumer prices is not expected to be very severe. In the United States and Japan capacity utilisation is high and unemployment has fallen - in the US to its lowest level of over a decade. Wage settlements in both countries are higher this year, though in the US they continue to run below the rate of price inflation. Some further small increases in wage inflation are forecast over the next couple of years, leading to a modest pick up in inflation in both countries.

23. Both the Japanese and German Governments have announced plans to raise indirect taxes in 1989. These contribute about ¼ percentage point to the projected rise in major seven inflation.

CURRENT BALANCES

24. The current account imbalances, expressed in dollars, of the United States, Japan and Germany reached new peaks in 1987. But the Japanese surplus fell sharply when expressed as a percentage of GNP. Trade volumes in all three countries have been adjusting to exchange rate changes since 1985, but US exports are so much smaller than imports (about 65 per cent) that substantial adjustment there is required to set the deficit on a downward trend.

Table 8: External Balances and Trade Ratios

	1986	1987	1988	1989	1990
Current balance ($bn)					
US	-141	-161	-144	-120	-93
Japan	85	87	85	76	71
Germany	38	46	40	41	33
NODCs	-13	7	8	6	6
OPEC	-14	2	-17	-16	-14
Current balance (% GNP)					
US	-3.3	-3.6	-3.0	-2.3	-1.7
Japan	4.3	3.6	2.9	2.3	1.9
Germany	4.2	4.1	3.2	3.0	2.2
Trade balance ($bn)					
US	-144	-159	-142	-117	-88
Japan	83	81	79	69	62
Germany	53	65	60	61	53
Trade ratio (exports/imports, volumes, 1980=100					
US	53	57	63	70	77
Japan	113	101	88	82	78
Germany	111	108	103	102	99

25. The projected outlook for demand in the three major countries suggests continuing, but unspectacular, reductions in current account imbalances over the next few years. By 1990 the US deficit and the Japan surplus are forecast to be less than 2 per cent of GNP, while the German surplus is put at just over 2 per cent. The error margins on these forecasts is large. For instance, even in the short-term US exports could be less than forecast (and imports higher) if capacity constraints are more severe than we think.

26. The projected fall in the US current account deficit between 1987 and 1990 is $68 billion. This is offset in part by a fall of $29 billion in the combined Japanese and German surplus. With little change expected in the current account position of developing countries as a group, the remaining $39 billion is accounted for by a deterioration in other OECD countries' current accounts. Particular problems are likely for Canada, Australia, New Zealand, and some European countries.

V. FISCAL AND MONETARY POLICIES

27. The forecasts for general government financial deficits are set out in Table 9. The aggregate deficit for the major countries excluding UK fell in 1987, primarily as a result of developments in the United States. Little change in the aggregate deficit is expected in 1988, but further cuts are assumed in 1989 and 1990.

Table 9: General Government Financial Deficits

% of GNP	1986	1987	1988	1989	1990
US	3.5	2.4	2¼	2	1½
Japan	1.1	0.2	0	0	0
Germany	1.2	1.7	2½	2	2
France	2.9	2.3	2¼	2	2
Major 6	3.1	2.5	2½	2¼	2

28. In **Germany** tax cuts have been implemented in 1988 and more are planned for 1990, but there are plans to raise indirect taxes in 1989 by DM 5 billion. In **Japan,** although there was an ex-ante loosening of fiscal policy in 1987, rapid growth created buoyant revenues and an ex-post fall in the government deficit. Policy is expected to remain broadly unchanged over the next few years. In the **United States** last December's joint Administration and Congress budget package effectively set the course of fiscal policy for 1989. Little further progress in cutting the Federal deficit is expected, even with rapid growth. Some tightening of fiscal policy after the Presidential election seems likely but this will probably have no impact until 1990.

29. Average real interest rates have fallen by about 1 percentage point since mid-1986 as inflation has picked up. More recently interest rates have edged up in the US. Average nominal rates in the major countries excluding the UK are forecast to rise in 1989 broadly in line with inflation. Within the aggregate, higher real rates are expected in the United States. The projected widening of interest differentials in favour of the dollar should support the orderly financing of current account balances.

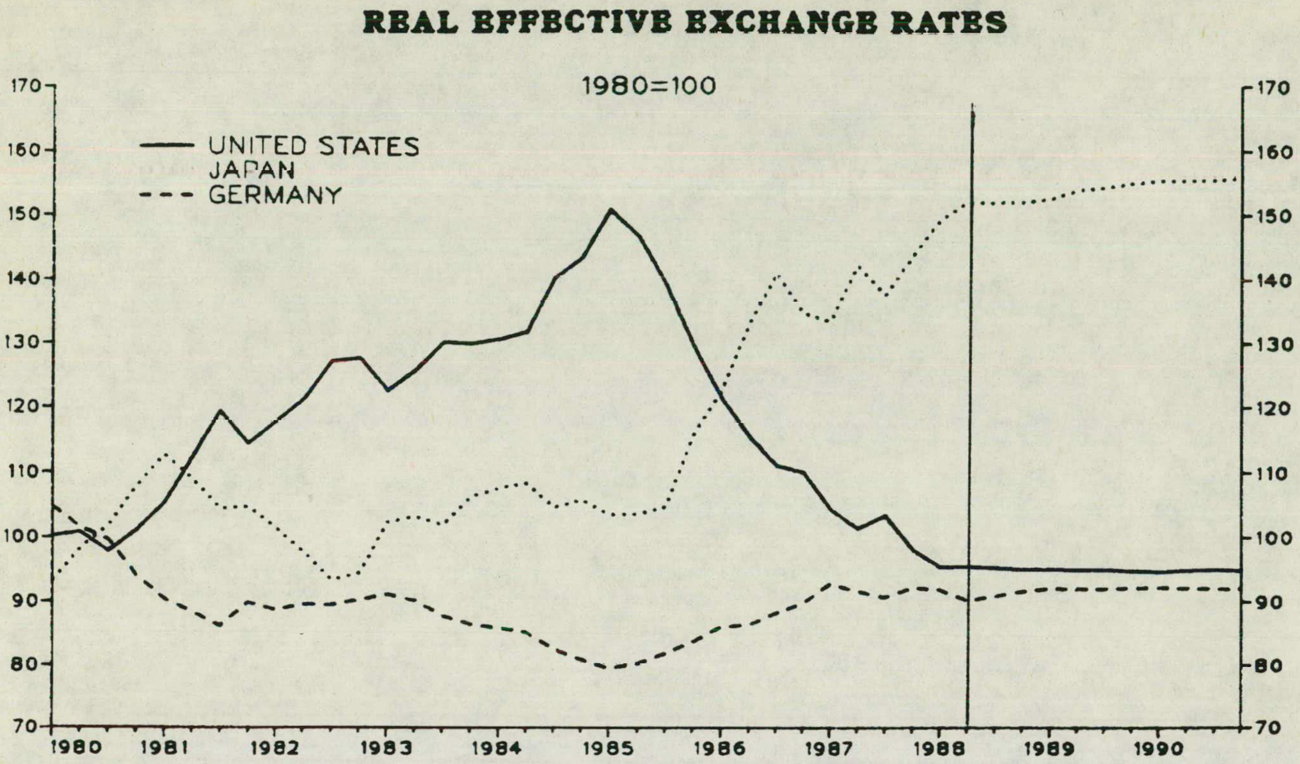
Table 10: Short-Term Interest Rates

	Nominal				Real*			
%	1987	1988	1989	1990	1987	1988	1989	1990
US	6.9	7.5	9.1	9.3	2.7	3.4	4.1	4.2
Japan	3.9	4.0	4.4	4.0	4.0	2.8	1.3	1.7
Germany	4.0	3.6	4.3	4.0	3.5	2.1	2.2	2.5
France	8.2	8.0	7.8	7.0	4.9	5.4	5.0	4.2
Major 6	6.5	6.7	7.7	7.5	3.3	3.4	3.4	3.7

* Average annual three month interest rate less change in consumers' expenditure deflator over the previous year.

30. This forecast is based on an assumption of broadly constant real effective exchange rates. Given the difficulties of forecasting exchange rates this is the most convenient conventional assumption to make.

Chart 4: Real Effective Exchange Rates



VI. RISKS

31. The forecast presented in this report would, if realised, represent a pretty good performance by the world economy, with sustained economic growth, low inflation, a reduction in the major current account imbalances and an improvement in the position of debtor countries. This section outlines some of the risks to this prospect.

32. Prospects for 1988. Section I on "Activity" set out the reasons for the forecast of 4 per cent real GNP growth in the major seven for 1988. This is rather above outside forecasts (see Annex 1) and downside risks might be:

a. capacity constraints in the US and Japan might limit output by more than has been allowed;

b. there might be a more marked slowdown in consumers' expenditure in the US, eg because of delayed wealth effects from the October stockmarket collapse and (more recently) falls in bond prices; or because exchange market or commodity price developments may lead the Fed to tighten monetary policy more sharply than assumed;

c. confidence has so far improved only modestly in continental Europe, and few people as yet appear to expect growth as strong as projected here.

33. Inflation. Factors which could lead to a greater than forecast pick up in consumer price inflation include:

a. the relationship between activity and commodity prices is an uncertain one, so forecast error margins are large - for any given level of output, commodity prices could be significantly higher;

b. the outlook for oil prices also remains enormously uncertain;

c. the investment cycle could be more sustained and multiplier effects on consumers' expenditure stronger, so that the forecast slowdown in GDP growth rates could be less marked or occur later - and a higher pressure of demand could mean faster inflation;

d. the rapid growth in liquidity (outside the US) due to the large scale intervention to defend the dollar in 1987 and early 1988 and to lower interest rates could feed more strongly into increased expenditures and thence increased inflation;

e. the assumed tightening of US fiscal and monetary policies might turn out to be more modest and/or occur later than assumed;

f. although there has been little response in wages so far to the fall in US unemployment to 5½ per cent (its lowest level for over a decade) and the rise in capacity utilisation rates in some industries to near peak levels, this may partly be because multi-year pay settlements put wage inflation on a long fuse.

34. Recession. The forecast of growth falling back in 1989 and 1990 to broadly in line with potential, with no more marked cyclical downturn, reflects the policy assumptions made and the absence of any significant adverse shocks. The main risks of recession stem from:

a. macroeconomic policies may prove inadequate, eg the Fed might have to tighten monetary policy more drastically if the dollar collapsed, or the German authorities might tighten their policies prematurely or excessively;

b. continuing financial market uncertainties, eg it might prove impossible to contain the problems of certain US banks and saving and loans; US companies are now more highly geared and higher interest rates could produce bankruptcies and weaken confidence; and equity markets in many countries remain nervous and some fear renewed falls on the lines of 1929-30 experience.

35. Current account imbalances and exchange rates. G7 co-operation has had considerable success this year in stabilising exchange rates, helped by lower US current account deficit data and greater US official commitment to exchange rate stability. But the pace at which further reductions in current account imbalances occur is forecast to be gradual. Such forecasts are subject to a substantial margin of error and if US deficits turned out to be higher, the political pressures of an election year could undermine the willingness of the authorities to raise interest rates or participate in joint intervention, if this proved necessary to defend the dollar. The effects of a further depreciation of the dollar would not necessarily net out at a world level:

- the experience of 1986 suggests there could be adverse effects on business confidence in appreciating countries;

- high rates of capacity utilisation in the US would limit the scope for expanding exports and cutting imports in response to a lower dollar, and, with no change in macro policy, inflation could rise;

- the tightening of US policies ultimately needed to restore confidence in the dollar and to control inflation might have to be more severe than otherwise.

COMPARISON OF FORECASTS

		WEP	OECD	IMF
Major 7 real GNP growth	1987	3.0	3.1	3.1
	1988	4.0	3	2.9
	1989	2.8	2½	2.7
Major 7 consumer price inflation	1987	2.9	2.9	2.8
	1988	3.1	3	3.0
	1989	3.9	3¼	3.1
World trade (volume)	1987	5.4	5.2	4.9
	1988	8.7	6¾	5.5
	1989	4.7	6	4.3
World trade in manufactures (volume)	1987	6.0	6.5	n.a
	1988	9.9	8¼	n.a
	1989	5.0	7	n.a

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SECRET AND PERSONAL

FROM: A A DIGHT
DATE: 10 June 1988

MR T PIKE

MONEY SUPPLY IN MAY: "FIRST GUESS" FOR M3 AND OUTTURN FOR MO

The Chancellor has seen and was grateful for your minute of 9 June.

A A Dight

A A DIGHT