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MONTHLY NOTE ON THE BALANCE OF PAYMENTS - JANUARY 1987

* In November the visible trade deficit widened slightly to £1.0 billion and the current balance showed a small deficit of £0.2 billion. The cumulative current account deficit for the first eleven months of 1986 is estimated at £0.2 billion.

* In the year to the fourth quarter of 1986 UK competitiveness, as measured by relative unit labour costs, appears to have improved by around 15 per cent. This reflects sterling's depreciation along with a rapid slowdown in the growth of UK unit labour costs relative to those of other countries. The firmer trend in sterling over the last two months, however, suggests that the gains in competitiveness may have come to an end.

* Domestic demand in G5 countries on average continued to grow in the third quarter although not as rapidly as in the UK. World trade in manufactures may also have picked up slightly in the second and third quarters.

* Export volumes (excluding oil and erratics) in the UK rose sharply in November, continuing the upward trend evident since the spring. In the five months to November they were 6½ per cent higher than in the first half of 1986.

* Import volumes (excluding oil and erratics) in the UK also rose sharply in November, following the slight falls recorded in September and October. In the five months to November they were 9 per cent higher than in the first half of 1986.

* The terms of trade have moved erratically in recent months but on balance have shown little change as the oil price has stabilised. The deterioration in the terms of trade in November, however, may reflect the lagged effects of sterling's depreciation in earlier months.

* Independent forecasts for the current account have on average edged upwards to a deficit of £3 billion in 1987, which compares with the Industry Act's forecast deficit of £1½ billion.

S KING
EA2 Division

MONTHLY NOTE ON THE BALANCE OF PAYMENTS - JANUARY 1987

Current Account

1. The November trade figures, published on 23 December, showed a deficit on non-oil trade of £1.4 billion, which was only partially offset by a surplus on oil trade of £0.3 billion. The non-oil deficit, which rose sharply between the second and third quarters of 1986 has continued to run at a high level in October and November. The oil trade surplus, however, which declined in the second quarter and again in the third quarter of 1986 reflecting the fall in the price of oil, improved on average in October and November as prices firmed. Overall, the visibles balance showed a deficit of £1.0 billion in November leaving the current account in deficit by £0.2 billion.

TABLE 1: CURRENT ACCOUNT

£ billion

	Current Balance	Visible Total	of which: Oil	Manufactures	Other goods	Invisibles Balance
1982	3.9	2.3	4.6	2.4	-4.7	1.6
1983	3.1	-0.8	7.0	-2.3	-5.5	4.0
1984	1.2	-4.4	6.9	-3.9	-7.4	5.6
1985	3.5	-2.1	8.2	-3.0	-7.3	5.7
1986 Q1	0.5	-1.5	1.9	-1.5	-1.9	2.0
Q2	0.3	-1.6	0.8	-0.6	-1.7	1.9
Q3	-0.8	-3.0	0.7	-1.9	-1.9	2.3
September	-0.1	-0.9	0.3	-0.6	-0.6	0.8
October	0.1	-0.8	0.2	-0.5	-0.5	0.8*
November	-0.2	-1.0	0.3	-0.8	-0.5	0.8*
Jan-Nov	-0.2	-7.9	3.9	-5.4	-6.4	7.7*

* CSO projection

CHART 1: CURRENT ACCOUNT

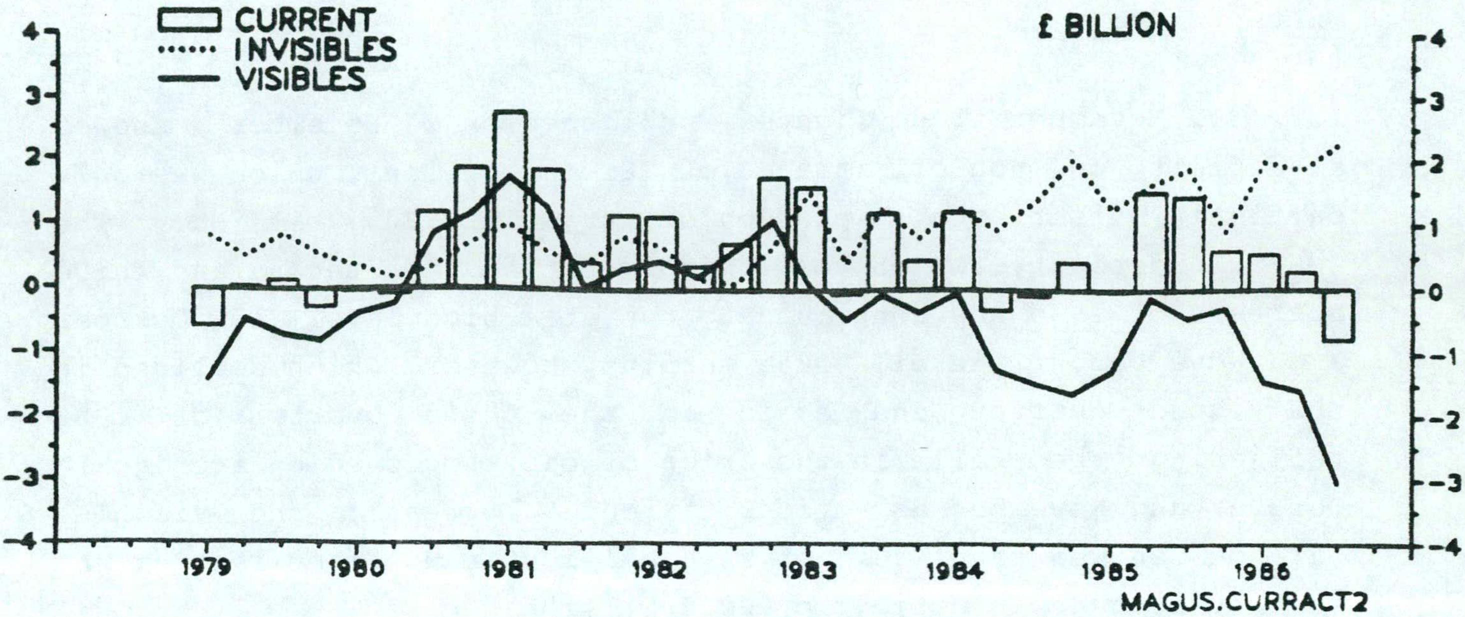


CHART 1A: VISIBLE BALANCE

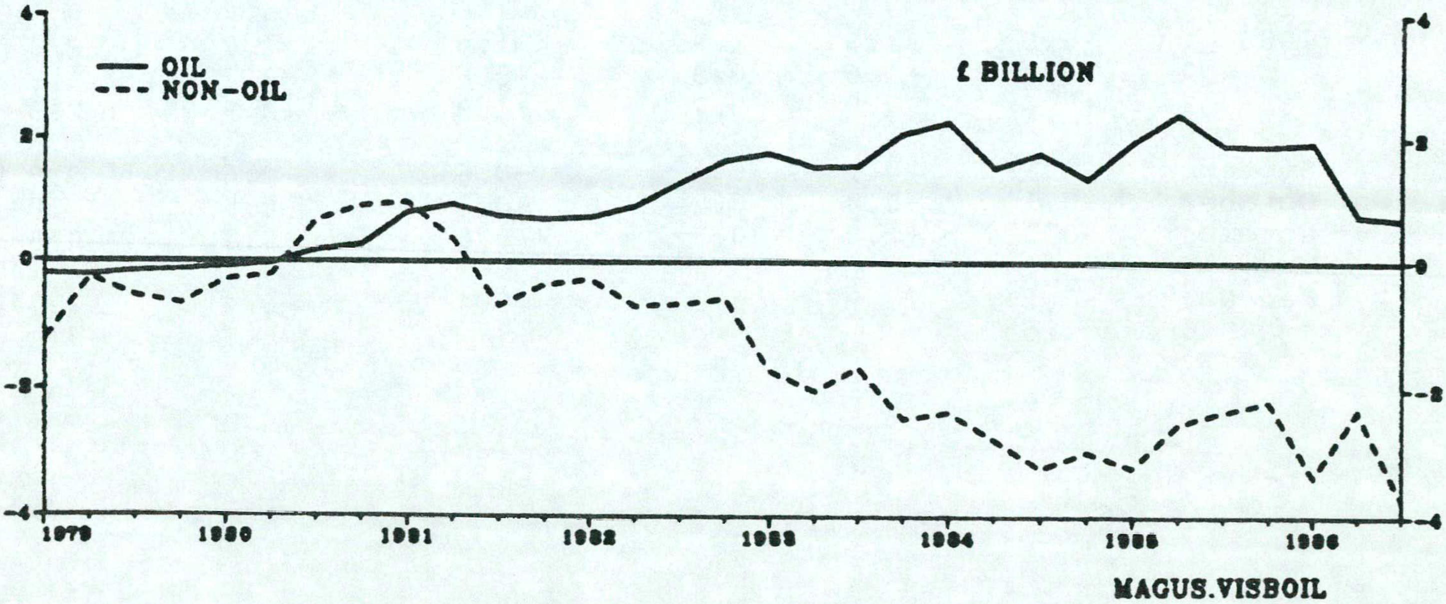


TABLE 2: RELATIVE UNIT LABOUR COSTS IN MANUFACTURING

Indices

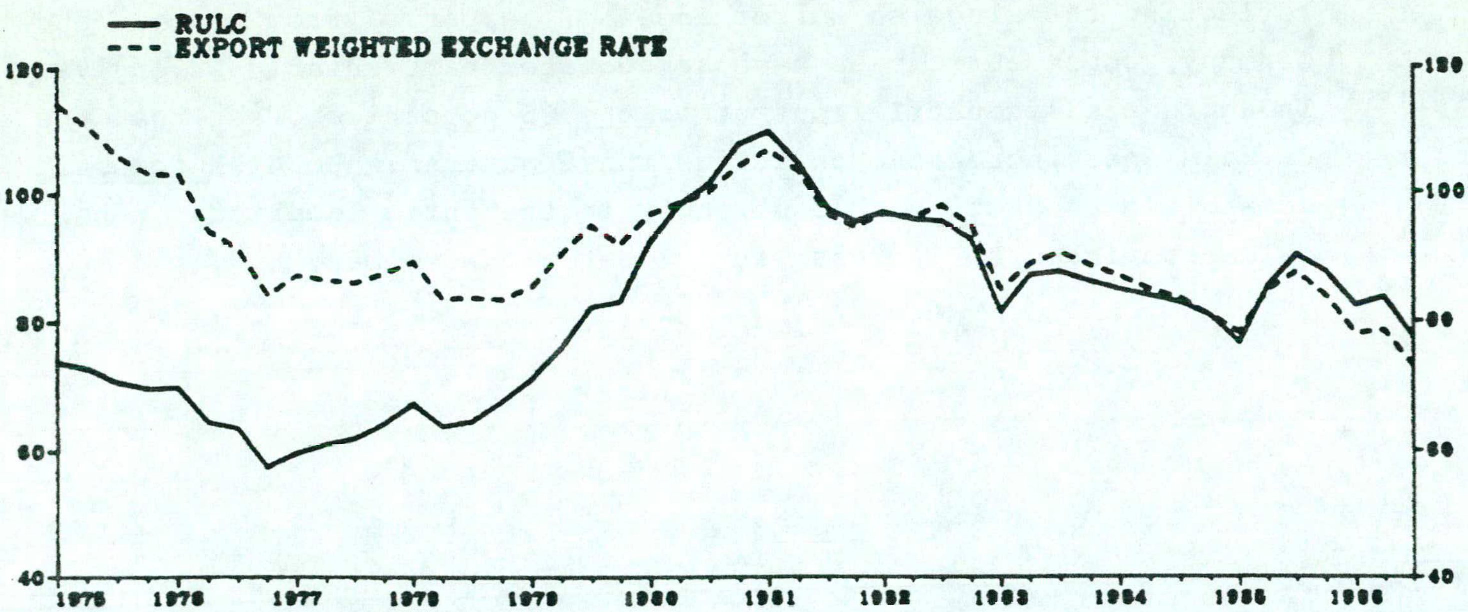
(% changes on a year earlier in brackets)

	Relative Unit Labour Costs in domestic currencies 1980=100	Export weighted Exchange Rate Index 1975=100	Relative Unit Labour Costs in common currencies 1980=100	Sterling Exchange Rate Index 1975=100
1982	98.7 (-2.9)	89.0 (-3.8)	95.2 (-6.6)	90.7 (-4.5)
1983	96.9 (-1.8)	81.4 (-8.5)	85.6 (-10.1)	83.4 (-8.1)
1984	98.9 (2.1)	77.5 (-4.8)	83.2 (-2.8)	78.7 (-5.5)
1985	101.7 (2.8)	77.0 (-0.6)	84.9 (2.0)	78.2 (-0.6)
1985 Q1	98.1 (0.5)	72.1 (-10.0)	76.7 (-9.7)	72.1 (-11.8)
Q2	100.7 (1.8)	78.1 (-0.3)	85.3 (1.5)	78.9 (-1.1)
Q3	103.1 (3.8)	80.7 (4.8)	90.2 (8.8)	82.1 (5.3)
Q4	104.7 (4.7)	77.3 (3.6)	87.7 (8.4)	79.8 (6.3)
1986 Q1	105.8 (7.8)	71.9 (-0.3)	82.5 (7.6)	75.1 (4.2)
Q2	106.6 (5.9)	72.3 (-8.4)	83.6 (-2.0)	76.0 (-3.7)
Q3	105.8* (2.6)	67.3 (-16.6)	77.2* (-14.4)	71.9 (-12.4)
October				67.8 (-15.7)
November				68.5 (-14.4)
December				68.4 (-13.5)

* estimate

CHART 2: UNIT LABOUR COSTS IN MANUFACTURING

1980=100



MAGUS.EXPEXANCY

DETERMINANTS OF UK TRADE

Competitiveness

2. UK competitiveness (as measured by relative actual unit labour costs in manufacturing) improved substantially during 1986 largely reflecting the fall in the nominal exchange rate. But also, unit labour costs measured in domestic currencies have grown at about the same rate in the UK as elsewhere since the first quarter of 1986, following sharp rises in UK relative costs in the second half of 1985. (This recent improvement may reflect in part temporary factors - in particular, a sharp fall in manufacturing employment in the UK - and therefore the figures may overstate the underlying improvement.) Information for the fourth quarter is incomplete but assuming no major change in relative cost performance, competitiveness may have improved by around 15 per cent in the year to the fourth quarter. However, these gains may have come to an end in the last two months of the year as the exchange rate firmed.

World Trade and Domestic Demand

3. In aggregate, G5 countries' domestic demand showed further growth in the third quarter following a sharp rise in the second quarter of 1986, although latest information suggests that the recovery in export volume growth was relatively modest (possibly reflecting the sluggish performance of exports from Japan and Germany, whose currencies have appreciated particularly strongly). In aggregate, industrial output in the G5 countries other than the UK did not increase much in the third quarter. Both UK domestic demand and production rose strongly in the third quarter; retail sales continued to increase in October and November.

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TABLE 3: INDICATORS OF DEMAND

% change

Indices 1980=100

	World			UK		
	G5 Export Volumes*	G5 Domestic Demand	G5 Industrial Production	Export Volumes**	Domestic Demand	Manufacturing Production
1982	99	100.9	96.7	99.3	100.4	94.2
1983	99	104.4	100.4	98.2	105.1	96.9
1984	107	109.9	108.5	107.6	107.9	100.7
1985	110	113.2	111.9	115.0	111.0	103.9
1985 1	110	111.5	110.7	114.8	111.1	103.6
2	112	112.5	111.9	115.3	110.1	104.5
3	106	114.1	112.4	115.4	111.3	103.8
4	114	114.9	112.7	114.4	111.7	103.6
1986 1	107	115.5	112.6	111.4	114.0	102.8
2	112	117.3	112.8	115.1	113.5	103.5
3		118.4	113.3	118.0	115.1	104.6
July	113		113.5	119.3		104.5
August	90		113.1	113.7		104.1
September			113.3	121.1		105.3
October			113.1	120.8		105.6
November				127.3		

percentage change on previous year

	World			UK		
	G5* Export Volumes	G5 Domestic Demand	G5 Industrial Production	Export** Volumes	Domestic Demand	Manufacturing Production
1982	-3.4	0.0	-3.5	0.5	2.2	0.2
1983	-0.3	3.4	3.8	-1.1	4.7	2.9
1984	8.6	5.3	8.0	9.6	2.7	3.9
1985	2.9	3.0	3.1	6.9	2.9	3.2
1985 1	5.2	2.6	3.5	11.3	4.1	4.1
2	5.7	2.6	4.2	9.6	1.0	4.3
3	1.9	3.3	2.7	7.1	3.2	2.3
4	-0.9	3.6	2.2	1.8	2.0	1.9
1986 1	-2.9	3.6	1.7	-3.0	2.6	-0.8
2	0.1	4.3	0.8	-0.2	3.1	-1.0
3		3.7	0.8	2.3	3.4	0.7
July	0.3		0.8	2.3		1.1
August	-8.6		0.7	-1.0		0.0
September			0.9	7.8		1.3
October			0.5	7.6		2.1
November				11.6		

* Not seasonally adjusted
** Excluding oil and erratics

VISIBLE TRADE

Summary

TABLE 4: VISIBLE TRADE VALUES AND VOLUMES

	Values (£ billion)			Volumes* (1980=100)		
	Exports	Imports	Balance	Exports	Imports	Ratio Exports: Imports
1982	55.6	53.2	2.3	101.9	101.5	100.4
1983	60.8	61.6	-0.8	103.8	109.7	94.6
1984	70.4	74.8	-4.4	112.5	121.9	92.3
1985	78.1	80.2	-2.1	118.6	125.8	94.3
1986 1	18.1	19.6	-1.4	116.9	125.7	93.0
2	17.8	19.4	-1.6	121.8	128.6	94.7
3	17.5	20.6	-3.0	123.3	139.1	88.6
September	6.1	7.0	-0.9	126.5	139.5	90.7
October	6.2	7.0	-0.8	125.3	140.6	89.1
November	6.5	7.5	-1.0	131.5	146.8	89.6
3 mths to Nov on same period previous year	-½	12		8½	12½	-4
3 mths to Nov on previous 3 mths	8½	7½		5	4½	½
November on October	5	7		-5	4½	½

* including oil and erratics

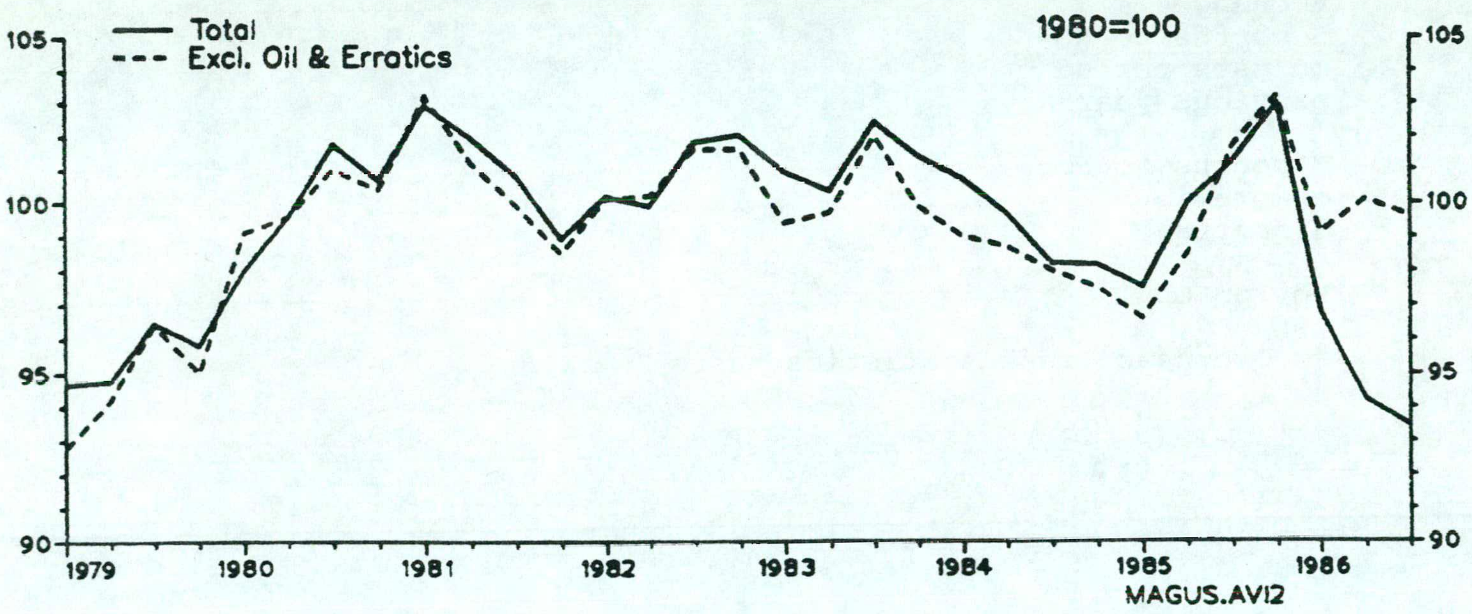
4. Tables 4 and 5 show recent movements in trade values, volumes and prices. The rise in the visible deficit, which in the first half of 1986 reflected the deterioration in the terms of trade associated with the fall in the oil price, has in the second half-year reflected mainly a very rapid growth of import volumes relative to export volumes. The terms of trade have moved erratically in recent months but on balance have shown little change as the oil price has stabilised. There was, however, a deterioration in November as a result of an increase in import prices - probably reflecting to some extent the lagged effects of the depreciation of sterling in earlier months.

TABLE 5: VISIBLE TRADE PRICES

Average Value Indices 1980=100

	Total			Excluding oil and erratics		
	Exports	Imports	Terms of trade	Exports	Imports	Terms of Trade
1982	115.0	113.9	101.0	111.5	110.6	100.9
1983	123.5	121.9	101.3	119.2	118.9	100.2
1984	131.9	133.1	99.1	126.4	128.7	98.3
1985	138.8	138.3	100.3	134.1	134.2	100.0
1986 1	130.8	135.1	96.8	134.6	135.4	99.5
2	123.2	130.8	94.2	134.2	134.1	100.0
3	119.8	128.3	93.4	134.6	135.3	99.5
September	121.5	129.9	93.5	134.6	135.1	99.6
October	125.3	130.5	96.1	136.9	137.4	99.6
November	125.4	133.9	93.6	135.2	138.1	97.9
3 mths to Nov on same period previous year	-8	-½	-7½	2	5½	-3
3 mths to Nov on previous 3 mths	3½	2½	1	1	1½	-½
November on October	0	2½	-2½	-1	½	-1½

CHART 3: TERMS OF TRADE



Exports

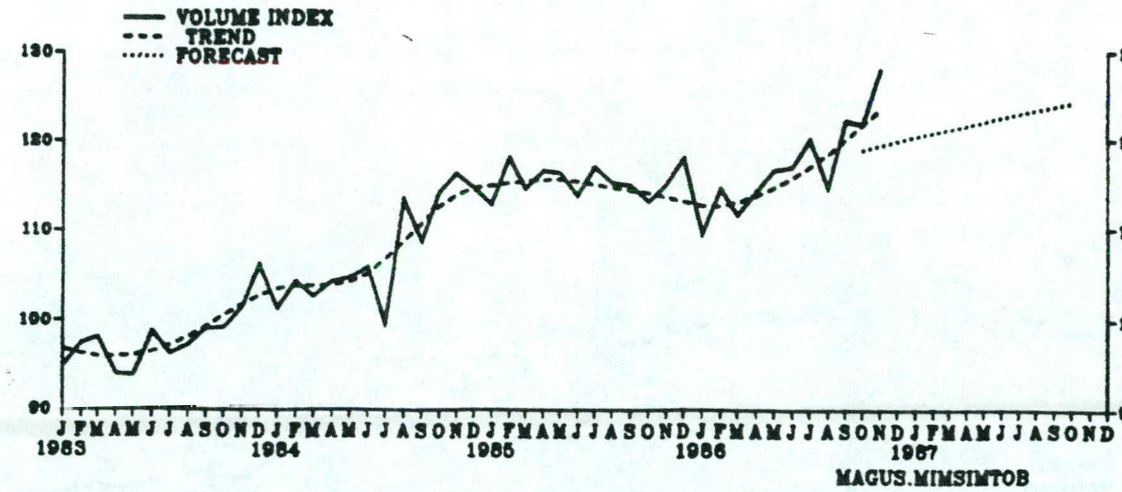
5. The upward trend in exports, which appears to have begun in March 1986 (see Chart 4), has continued, with the volume of non-oil exports (excluding erratics) 5½ per cent higher in the three months to November than in the previous three months. The figures have benefitted from an abnormally high level of non-manufactured exports: the increase in manufactures (excluding erratics) was 4 per cent, while food, drink and tobacco and basic materials rose by 17½ and 8½ per cent respectively. The CBI's December enquiry indicated a further improvement in the balance for manufactures' export orders, following the sharp rise in November.

TABLE 6: EXPORT VOLUMES

1980=100	Goods less erratics	Goods less oil and erratics	Manufactures less erratics*
1982	104.0	99.3	97.8
1983	105.2	98.2	96.2
1984	115.4	107.6	107.0
1985	123.0	115.0	115.7
1986 1	121.0	111.4	111
2	122.7	115.1	116
3	127.6	118.0	117
September	129.9	121.1	119
October	128.8	120.8	120
November	134.1	127.3	124
% change			
3 months to Nov on same period previous year	7½	8	6
3 months to Nov on previous 3 months	4½	5½	4
Nov on Oct	4	5½	3½

* Overseas trade statistics basis

CHART 4: NON OIL EXPORT VOLUMES EXCLUDING ERRATICS



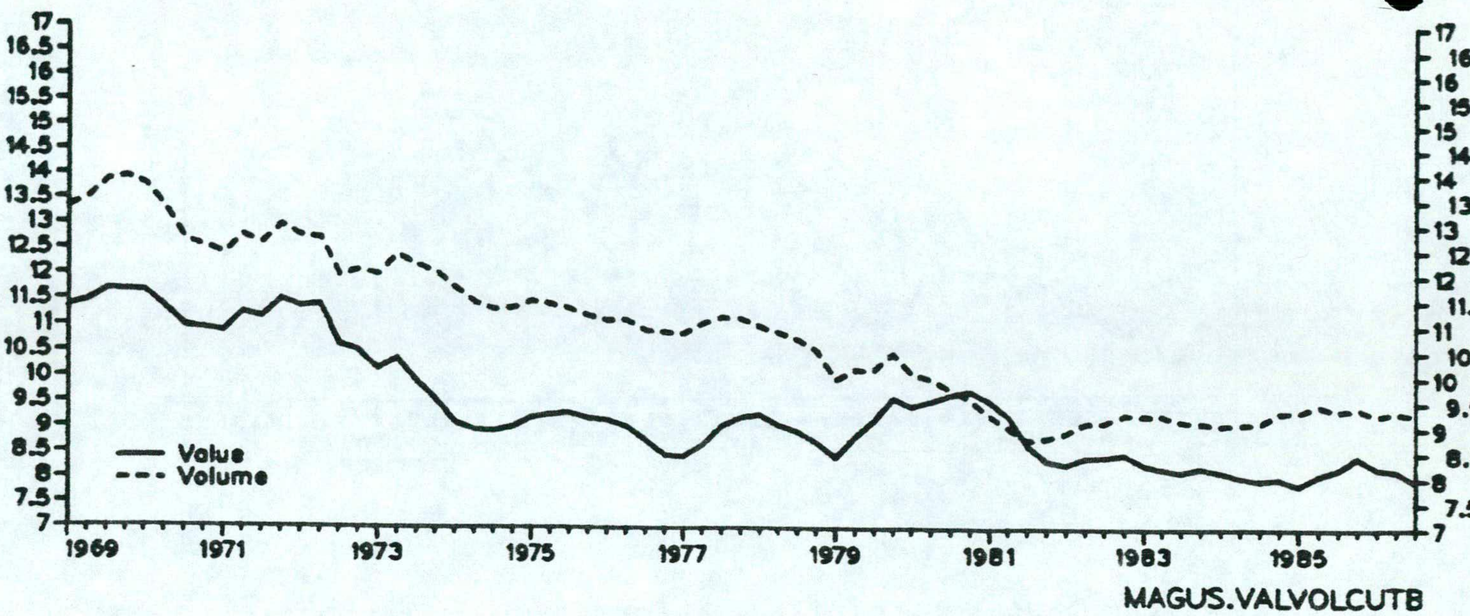
6. On the basis of limited information, it appears that UK export volume growth has been good compared with relatively weak growth in main manufacturing countries' exports, and this would suggest that there may have been some improvement in the UK's underlying performance compared to other industrial countries.

TABLE 7: UK MANUFACTURERS' SHARE OF MAIN MANUFACTURING COUNTRIES' EXPORTS

		Per cent
	Volume	Value
1980	9.7	9.7
1981	8.8	8.6
1982	8.8	8.5
1983	9.1	8.1
1984	9.2	8.0
1985	9.4	8.2
1985 1	9.3	7.7
2	9.5	8.5
3	9.2	8.4
4	9.5	8.4
1986 1	9.1	7.8
2*	9.4	8.3
3*	9.3	7.8

* Based on WEP estimates

CHART 5: UK SHARE OF MAIN MANUFACTURING COUNTRIES' EXPORTS



7. Manufacturers' export prices, which remained broadly flat through the early part of 1986, rose significantly in the three months to November reflecting higher domestic costs and the opportunities afforded by sterling's depreciation to improve profit margins. After the sharp increases recorded in September and October, there was no further rise in fuel export prices in November; the effects of the most recent firming of oil prices will probably not show until the January and February figures. Food prices have continued to rise, whilst basic materials prices, which had begun to pick up, faltered in November. This may partly reflect the fact that the pick up in commodity prices in September and October has proved to be short-lived.

TABLE 8: EXPORT PRICES*

Indices 1980=100

	Manufactures	Food, Drink and Tobacco	Basic Materials	Fuel
1982	111.9	113.9	98.8	131.2
1983	120.6	118.2	108.3	138.0
1984	128.5	122.9	129.2	148.6
1985	136.1	128.1	138.4	152.1
1986 1	137.1	126.6	124.9	111.5
2	136.2	131.6	119.2	70.0
3	137.8	127.8	118.7	57.4
September	139.4	125.5	117.9	60.7
October	140.3	132.3	125.0	68.6
November	139.1	134.6	121.2	68.3
% change				
3 months to Nov on same period previous year	3½	1½	-9	-52
3 months to Nov on previous				
3 months	2½	1	2½	10½
Nov on Oct	-1	2	-3	-½

* Average Value Indices - Overseas Trade Statistics basis

8. The volume of exports going to the US picked up sharply in November, mainly due to an increase in exports of oil. Exports to the EC fell by 2 per cent in November compared with October although, in the latest three months, they were 9½ per cent above the level of the previous three months. The volume of exports going to oil exporting countries rose for the third successive month, although in the latest three months, exports were still 3½ per cent lower than in the previous three months, and 8½ per cent lower than a year earlier. Exports to non-oil developing countries remain broadly flat.

TABLE 9: GEOGRAPHICAL DESTINATION OF EXPORTS

£ million, 1980 prices

	EC	US	Oil Exporters	Other
1982	20875	6472	5796	14943
1983	22445	6860	5119	14628
1984	24796	7690	4554	16246
1985	27225	8291	4416	16396
1985 1	6891	1978	1245	3987
2	6505	2247	1104	4386
3	6872	2002	1048	3986
4	6958	2062	1016	4169
1986 1	6962	2137	1044	4138
2	7389	2099	1175	4515
3	7857	2008	964	4592
September	2673	667	291	1558
October	2768	628	295	1472
November	2716	809	304	1579
3 months to Nov on same period previous year	14½	3	-8½	16
% change 3 months to Nov on previous 3 months	9½	4½	-3½	2
Nov on Oct	-2	29	3	7½

Imports

9. Imports, excluding oil and erratics, rose by 3½ per cent in the three months to November compared with the previous three months, to a level 12 per cent higher than in the same period a year earlier. Imports of basic materials rose particularly sharply, and increases were also recorded in fuels and semi-manufactures - all three are consistent with high domestic stockbuilding and rising manufacturing output. Imports of capital goods continued to recover and imports of consumer and intermediate goods recovered sharply in November from the lower levels of the previous two months.

TABLE 10a: IMPORT VOLUMES

1980=100

	Goods less erratics*	Goods less oil and erratics*	Food Drink and Tobacco	Basic materials	Fuels†	Manufactures less erratics
1982	107.1	112.7	108.1	93.0	74.5	116.5
1983	115.0	123.4	107.8	104.6	66.8	131.1
1984	128.8	137.0	112.3	101.7	86.5	146.7
1985	133.4	142.7	113.6	102.2	85.0	154.5
1986 1	132.8	144.1	126.3	105.4	73.9	154.5
2	136.5	144.7	119.5	105.6	87.3	156.8
3	148.0	155.1	126.1	106.0	112.2	168.8
September	146.6	156.0	125.4	118.6	103.6	167.5
October	149.6	153.1	115.5	110.2	142.2	167.3
November	156.8	168.3	128.4	124.9	91.2	182.3
% change 3 months to Nov on same period previous year	12	9½	5	12	45½	9½
3 months to Nov on previous 3 months	3½	4	-2	16	7½	3
Nov on Oct	5	10	11	13½	-36	9

† Figures affected by coal strike
* Balance of payments basis

TABLE 10b IMPORT VOLUMES OF MANUFACTURES

	Semi manufactures	Finished manufactures	of which: Passenger motor cars	Other consumer goods	Intermediate goods	Capital goods
1982	111.3	120.0	110.1	113.3	122.8	128.2
1983	123.3	136.4	125.5	124.9	136.2	153.1
1984	137.2	153.0	119.9	139.6	161.4	172.9
1985	143.9	161.5	127.9	139.6	172.8	187.2
1986 1	147.7	159	130	145	171	175
2	148.6	162	126	154	182	168
3	156.2	177	144	166	193	186
September	159.5	172.8	125.4	163.1	184.9	189.4
October	155.5	175.3	136.7	154.5	190.5	195.4
November	160.3	196.8	136.4	180.8	224.3	209.0
% change 3 mths to Nov on previous year	9	10	5½	15½	13½	4
3 mths to Nov on prev 3 mths	3	3	-10	1	2	9
Nov on Oct	3	12½	0	17	17½	7

CHART 6: NON OIL IMPORT VOLUMES EXCLUDING ERRATICS

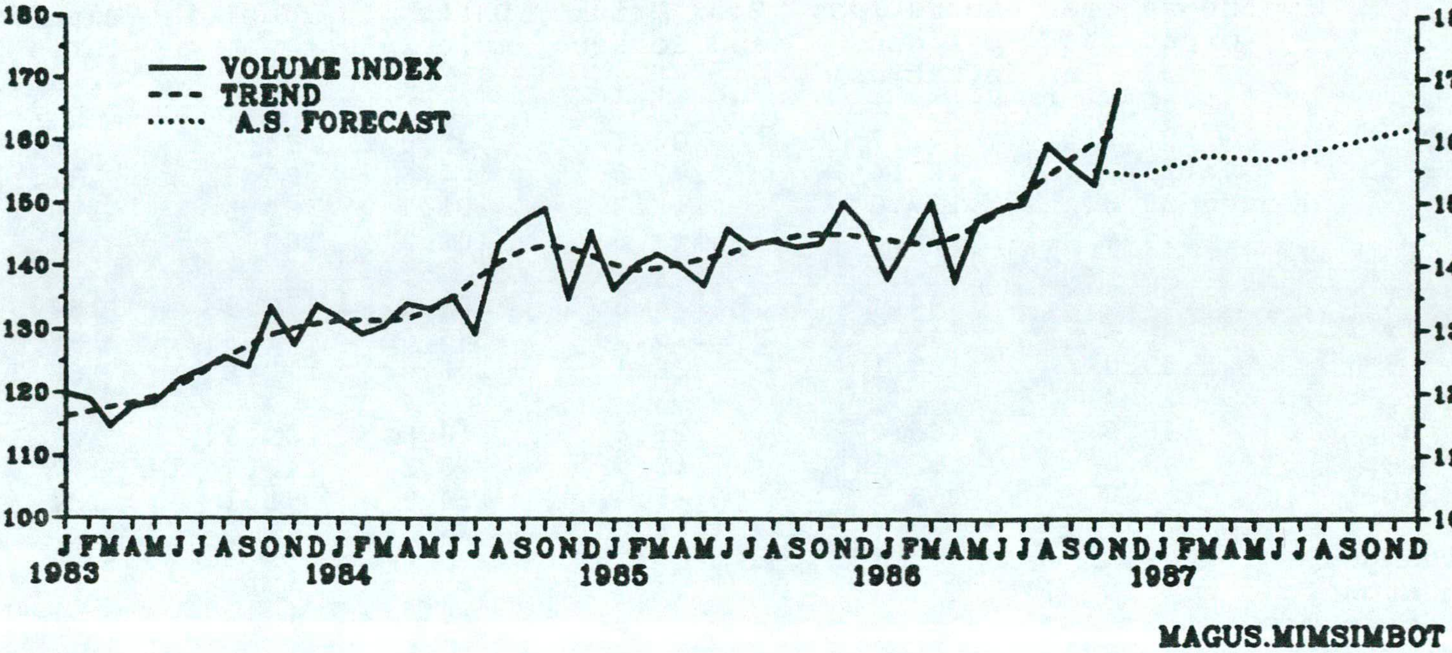
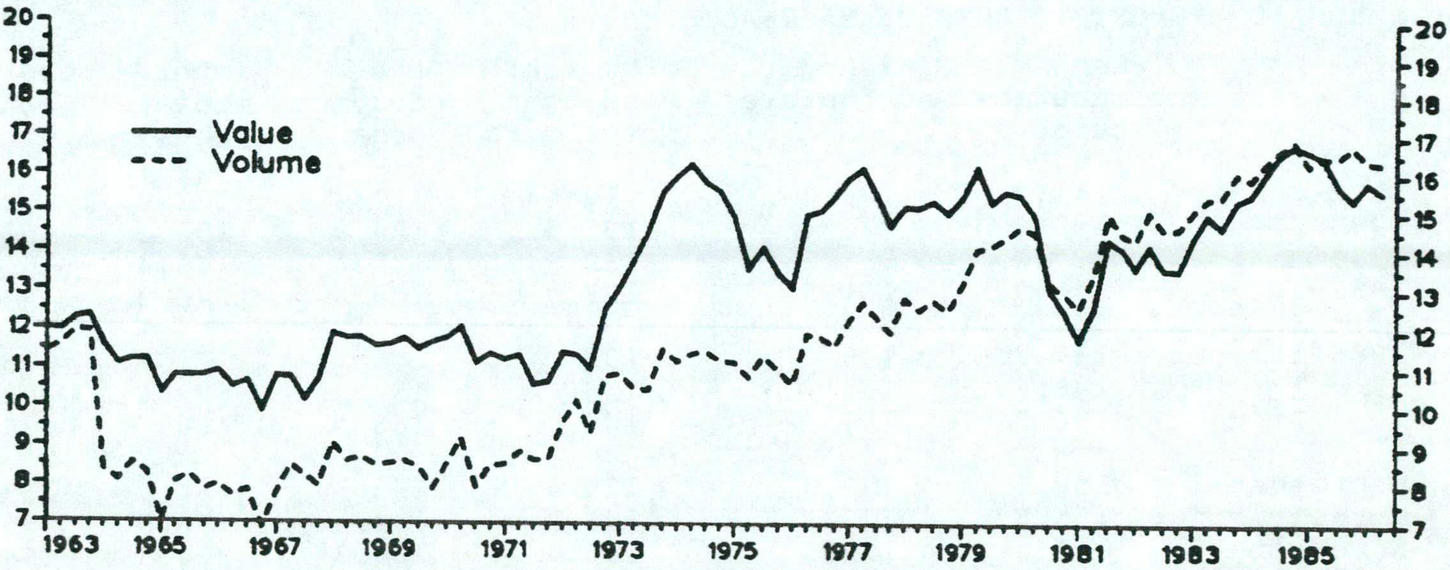


CHART 7: IMPORT PENETRATION*



* share of import of goods (excluding oil) in total final expenditure

10. The growth of imports in the third quarter was faster than growth of total final expenditure, implying a substantial rise in import volume penetration; this trend appears to have continued in October and November. It is not yet possible to be sure whether the latest deterioration is merely a temporary phenomenon, associated with the particularly strong recent rise in domestic demand or whether, after a period in 1985 where volume penetration appeared to have levelled off, it marks a return to more adverse trends.

TABLE 11: IMPORT PENETRATION*

		Per cent
	Volume	**Value**
1980	13.9	14.0
1981	13.9	13.2
1982	14.6	13.7
1983	15.5	14.8
1984	16.5	16.2
1985	16.5	16.1
1985 1	16.3	16.6
2	16.5	16.5
3	16.5	15.7
4	16.8	15.4
1986 1	16.4	15.8
2	16.3	15.6
3**	17.3	16.4

* Imports (excluding oil) as a percentage of total final expenditure
** Projection

11. Import prices continued to rise across the board in November as the lagged effects of sterling's earlier depreciation came through. Import prices of manufactures and of food, drink and tobacco in the latest three months rose by 3 and 2½ per cent respectively compared with the previous three months. Prices of basic materials imports continued to rise, despite the continuing underlying decline in world commodity prices (the pick up in world commodity prices in September and October appears to have been temporary, November's fall being consistent with the trend of the last year or so). Fuel prices rose by 2 per cent in the latest three months compared with the previous three months although given the erratic movements in the volume but not the value of fuel imports in recent months, it is not clear whether this figure is wholly reliable.

TABLE 12: IMPORT PRICES*

1980=100

	Manufactures	Food Drink and Tobacco	Basic Materials	Fuel
1982	110.9	109.0	104.4	144.7
1983	118.6	118.6	112.8	154.1
1984	126.8	129.3	131.6	173.8
1985	132.9	132.7	130.2	180.0
1985 3	130.6	129.5	125.8	165.9
4	128.7	127.5	115.8	156.4
1986 1	135.0	129.4	115.2	141.3
2	133.7	130.9	113.0	103.0
3	134.7	133.0	110.9	77.4
September	135.9	134.0	110.2	81.0
October	137.9	136.3	112.7	80.6
November	140.0	137.2	115.6	84.8
% change				
3 mths to Nov on same period previous year	7	6	-5½	-47½
3 mths to Nov on previous 3 mths	3	2½	1	2
Nov on Oct	1½	½	2½	5

* Average Value Indices - Overseas Trade Statistics basis

INVISIBLES

12. The invisibles balance was estimated to have been in surplus by a little under £2.3 billion in the third quarter of 1986, compared with a revised outturn of £1.9 billion in the second quarter. A revised invisibles projection for the fourth quarter, of £800 million a month, was published with the November trade figures press notice. It compares with an initial projection of £900 million a month.

TABLE 13: INVISIBLES BALANCE

£ billion

	Services	IPD	Transfers	Total
1982	2.6	1.0	-2.0	1.6
1983	3.7	2.4	-2.1	4.0
1984	3.7	4.2	-2.3	5.6
1985	5.8	3.4	-3.5	5.7
1986 1	1.2	1.0	-0.2	2.0
2	1.3	1.1	-0.6	1.9
3	1.6	1.5	-0.9	2.3
October				0.8*
November				0.8*

* projection

CAPITAL FLOWS AND NET OVERSEAS ASSETS

13. Despite the current account deficit in the third quarter, net capital outflows were recorded, although, at £0.9 billion, they were considerably less than the £2.6 billion recorded in the second quarter. The balancing item was £1.9 billion in the third quarter, similar to the quarterly average for the first half of the year. Some of this may represent errors in the current account, but the major part probably reflects as yet unidentified capital inflows.

TABLE 15: NET TRANSACTIONS ON CAPITAL ACCOUNT

£ million

	1985	1986 Q1	Q2	Q3
Direct investment	-3937	+1205	-210	-1781
Portfolio investment	-11171	-4078	-4864	-2931
Net foreign currency lending abroad	+4909	+788	+2901	+6002
Net sterling lending abroad	+2513	+1818	-1389	-722
Other	+1821	-729	+1249	+856
Official reserves	-1758	-580	-296	-2321
Total	-7623	-1576	-2609	-897

\- = net outflow, + = net inflow.

14. Although there was probably little net capital outflow in 1986, given the deterioration in the current account, net overseas assets are nevertheless likely to have grown strongly because of the depreciation of sterling against most currencies other than the US dollar and the strength of overseas stock and bond markets.

PROSPECTS

15. Independent forecasters are on average expecting a current deficit of £3 billion in 1987 compared to the Industry Act forecast's £1½ billion deficit but there are wide differences of view. The latest forecast for the UK economy produced by the OECD projects a current account deficit of £3½ billion in 1987, and a further deterioration in the first half of 1988. Whilst similar to the IAF in terms of volume changes, the OECD are less optimistic on the outlook for the terms of trade.

TABLE 16: CURRENT ACCOUNT (£ billion)

	1986	1987	1988	1989	1990
OECD (Dec)	-0.2	-3.4	-6.0*	-	-
National Institute (Nov)	-1.8	-5.6	-7.2	-	-
LBS (Nov)	-0.4	-2.4	-1.2	-0.9	-0.4
Phillips & Drew (Jan)	-0.1	-2.8	-4.0	-2.7	-1.9
Goldman & Sachs (Jan)	0.3	-2.3	-2.8	-2.7	-1.9
Henley (Dec)	-0.8	-2.1	-2.9	-2.5	-8.1
Oxford (Nov)	-1.0	-2.2	0.1	-0.5	-0.1
Outside Average (Nov)	-0.5	-3.1	-3.1	-1.8	-1.5

* 1988H1, annualised

INTERNATIONAL COMPARISONS

16. The US current deficit levelled off in the first two quarters of 1986, although the renewed deterioration of the trade deficit suggests that the current deficit may have begun to widen again. The German and Japanese surpluses have shown no sign of falling from the very high levels reached at the beginning of this year.

TABLE 17 COMPARISON OF CURRENT ACCOUNTS AS % OF NOMINAL GDP/GNP FOR THE G5

		US	Japan	Germany	France	UK	Total
1984		-2.8	2.8	1.1	-0.1	0.4	-0.6
1985		-2.9	3.7	2.1	0.0	1.1	-0.7
1985	1	-2.7	3.1	1.4	-0.5	0.0	-0.5
	2	-3.0	3.9	2.1	0.4	2.4	-0.1
	3	-2.8	3.6	2.6	0.0	2.1	-0.0
	4	-3.3	4.0	2.4	0.7	0.8	-0.3
1986	1	-3.2	3.6	3.9	0.6	0.8	-0.1
	2	-3.3	4.9	3.7	0.6	0.4	-0.0
	3	N/A	4.4	4.7	N/A	-1.4*	N/A

Circulation List

Chancellor
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Mr Dolphin
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Mr Owen
Mr Patterson
Ms Turk
Mr McLaren
Mr Segal

RC6.17

PERSONAL

Treasury Chambers, Parliament Street, SW1P 3AG
01-233 3000

5 January 1987

Nigel Wicks Esq
10 Downing Street
LONDON
SW1

Dear Nigel,

PUBLICATION DATES OF STATISTICS

You asked for publication dates for the major economic statistics in 1987. These are attached.

The date of the IMF spring meeting is within the period 6-13 April and the annual meeting 24-30 September

Yours
Alex

A C S ALLAN
Principal Private Secretary

ATTACHMENT

Provisional Money Figures

Published: Monthly:

20 January 1987;	19 February 1987;	19 March 1987;
22 April 1987;	20 May 1987;	18 June 1987;
20 July 1987;	20 August 1987;	18 September 1987;
20 October 1987;	19 November 1987;	18 December 1987;
(20 January 1988)		

Index of Production

Published: 2 monthly in arrears - ie August figures in October:

19 January 1987;	16 February 1987;	17 March 1987;
14 April 1987;	19 May 1987;	18 June 1987;
14 July 1987;	13 August 1987;	16 September 1987;
14 October 1987;	13 November 1987;	15 December 1987
(19 January 1988;	16 February 1988)	

Reserves

Published: Monthly - 2nd Working Day of every month.

5 January 1987;	3 February 1987;	3 March 1987;
2 April 1987;	4 May 1987;	2 June 1987;
2 July 1987	4 August 1987;	2 September 1987;
2 October 1987;	3 November 1987;	2 December 1987

PSBR

Published: Monthly: 12th Working Day

19 January 1987;	17 February 1987;	17 March 1987;
16 April 1987 (Financial Year Outturn).		19 May 1987
16 June 1987;	16 July 1987;	18 August 1987;
16 September;	17 November;	16 December

Note: The Autumn Statement and the Budget are two further occasions when PSBR announcements are made.

RPI and TPI

Published the same day as the RPI, ie:

16 January 1987;	13 February 1987;	20 March 1987;
10 April 1987;	15 May 1987;	12 June 1987;
10 July 1987;	14 August 1987;	11 September 1987;
9 October 1987;	13 November 1987;	11 December 1987;

Consumers' Expenditure

Preliminary quarterly figures expected:

22 January 1987;	23 April 1987;	23 July 1987
22 October 1987		

Adjusted final figures expected:

20 March 1987;	22 June 1987;	21 September 1987;
18 December 1987		

Retail Sales

Provisional:

16 February 1987;	16 March 1987;	29 April 1987;
18 May 1987;	15 June 1987;	20 July 1987;
17 August 1987;	14 September 1987;	14 October 1987;
16 November 1987;	14 December 1987	

Final:

9 March 1987;	6 April 1987;	11 May 1987;
8 June 1987;	6 July 1987;	10 August 1987;
7 September 1987;	5 October 1987;	9 November 1987;
7 December 1987;	11 January 1988	

CBI Quarterly Survey/Monthly Enquiry

27 January 1987*;	23 February 1987;	23 March 1987;
28 April 1987*;	(May)1 June 1987;	22 June 1987;
28 July 1987*;	28 August 1987;	21 September 1987;
27 October 1987*;	23 November 1987;	14 December 1987

* Quarterly Survey

Trade Figures

27 February 1987;	26 March 1987;	28 April 1987;
28 May 1987;	25 June 1987;	24 July 1987;
25 August 1987;	24 September 1987;	23 October 1987;
24 November 1987;	23 December 1987;	28 January 1988

Unemployment Figures

15 January 1987;	12 February 1987;	19 March 1987;
15 April 1987;	14 May 1987;	18 June 1987;
16 July 1987;	13 August 1987;	17 September 1987;
15 October 1987;	12 November 1987;	17 December 1987

MR 11/27

Treasury Chambers, Parliament Street, SW1P 3AG
01-233 3000

The Rt Hon Norman Tebbit MP
Conservative Central Office
32 Smith Square
LONDON
SW1P 3HH

6 January 1987

Dear Norman

PUBLICATION DATES OF STATISTICS

... Further to my letters of 17 October and 20 November I attach publication dates for economic statistics not covered in those letters.

Nigel

NIGEL LAWSON

MR 11/26

ATTACHMENT

Retail Sales

Provisional:

16 February 1987;	16 March 1987;	29 April 1987;
18 May 1987;	15 June 1987;	20 July 1987;
17 August 1987;	14 September 1987;	14 October 1987;
16 November 1987;	14 December 1987	

Final:

9 March 1987;	6 April 1987;	11 May 1987;
8 June 1987;	6 July 1987;	10 August 1987;
7 September 1987;	5 October 1987;	9 November 1987;
7 December 1987;	11 January 1988	

CBI Quarterly Survey/Monthly Enquiry

27 January 1987*;	23 February 1987;	23 March 1987;
28 April 1987*;	(May)1 June 1987;	22 June 1987;
28 July 1987*;	28 August 1987;	21 September 1987;
27 October 1987*;	23 November 1987;	14 December 1987

* Quarterly Survey

Trade Figures

27 February 1987;	26 March 1987;	28 April 1987;
28 May 1987;	25 June 1987;	24 July 1987;
25 August 1987;	24 September 1987;	23 October 1987;
24 November 1987;	23 December 1987;	28 January 1988

Unemployment Figures

15 January 1987;	12 February 1987;	19 March 1987;
15 April 1987;	14 May 1987;	18 June 1987;
16 July 1987;	13 August 1987;	17 September 1987;
15 October 1987;	12 November 1987;	17 December 1987

Cyclical Indicators

Definite 1987 dates:

20 January 1987;	19 February 1987;	23 March 1987;
15 April 1987;	21 May 1987;	23 June 1987;
15 July 1987;	19 August 1987;	22 September 1987;
15 October 1987;	19 November 1987;	21 December 1987;
(19 January 1988)		

CONFIDENTIAL

FROM: MRS A F CASE
DATE: 6 January 1987

PS/CHANCELLOR

C/Mr Hibbert is coming to see you at 3pm on Friday. PEM said he would like to come, but I think it would be better for you to see him on your own.
Content with speaking note and longer aide memoire?
CR 6/1

cc PS/Chief Secretary
PS/Economic Secretary
Sir P Middleton
Mr F E R Butler
Sir G Littler
Mr Lavelle
Mr Mountfield
Mr Turnbull
Mrs Butler
Mr Bush

ECGD GUARANTEED VEHICLES

I attach an abbreviated speaking note for the Chancellor's talk with Mr Hibbert on Friday, together with a longer aide memoire.

2. As Mr Bush explained to you resolution of this issue is urgent. Not only are we losing credibility in our negotiations with the banks - we have been stalling for four months - and weakening our negotiating position in the process but GEFCO (the Lloyds Merchant Bank vehicle which has refinanced Yugoslav and Philippine Paris Club debt) are pressing to fund that loan by a bond issue now and are supported by the Bank of England who judge market conditions to be favourable. When the issue is made we need to be able to answer questions about its PSBR treatment and the possibility of similar future exercises in relation to these or other country debts on which we are currently stalling.

AFC

MRS A F CASE

SPEAKING NOTE

11/141

EXPORT FINANCE : CLASSIFICATION

Speaking Note

- Present export finance system traditionally private sector affair, though facilitated by ECGD. Government wants to keep it that way and to obtain benefit of securitisation in lower costs for the taxpayer.

2. CSO proposal helpful in operational terms but raises unhelpful wider policy issues.

3. Four points of concern.

4. First, CSO proposal splits flow of export finance in accounting terms between public and private sectors. Export finance would switch from one to another in response to relative interest rates.

5. Second - more substantive problem - if transactions fall within public sector, scheme designed to reduce cost to taxpayer of existing arrangement ends by looking as if it adds to costs. Financial benefits same but will look unappealing by comparison with NLF rather than bank finance.
- If to minimise HMG's subsidies, part of finance is brought within public sector, could be unwelcome pressure for purely public sector operation.

6. Third - other countries now copying bond guarantee ideas to encourage "pure cover" (no subsidy) operations in rich markets. Classification of vehicles to public sector involves real risk that under Consensus rules UK exporters may be denied these advantages.

7. Finally - very ingenuity of solution proposed may be damaging. Public sector classification will be unexpected. Special treatment - vehicles in public sector but borrowing

and lending excluded from public expenditure and PSBR - will inevitably raise suspicions of Treasury and CSO fiddling the books.

8. Difficult issues. Share concern not to jeopardise rules. Recognise help given by CSO. No easy alternative. Vehicles essential to tap capital markets and secure savings.

9. Solution which minimises policy problems ie treat vehicles as in private sector, cuts across existing rules. Conclusion - exception least damaging way to achieve what all agree is in the general interest. Defensible on pragmatic grounds: no difference in rationale, only form, between new proposals and traditional bank funded FREF and refinancing.

EXPORT FINANCE : CLASSIFICATION

Aide Memoire

The Treasury has given much careful thought to the difficult problem of classification of export finance.
We share the CSO's concern that the rules which have been carefully devised should not be put in jeopardy. The work which the CSO has done on these problems has gone a long way and has shown considerable ingenuity in trying to meet our requirements whilst retaining the integrity of the normal rules.

2. The CSO proposal (taking export finance through vehicles transactions outside PSBR and public expenditure) is helpful in operational terms but, if adopted, would raise wider policy issues for HMG.

3. Because of this Treasury officials have looked again to see if there is any alternative way through the classification issues raised by the use of vehicles to tap the capital market. We can find no easy solution. The negotiations with the banks are already difficult for other reasons. The banks would want to use vehicles for market reasons, even if, like current FREF. funding remained on their balance sheet. Other approaches would considerably reduce the prospective savings. We cannot therefore go back to scratch.

4. Yet the case for tapping the capital markets and obtaining the benefits of securitisation in lower funding costs for the taxpayer is simple and self-evident.

5. Against the background that the Government has no wish to change the basic rationale of the present export finance system ie essentially a private sector affair, though facilitated by ECGD, the CSO proposal gives rise to four points of concern.

6. <u>First</u>, although no change is proposed in the basic rationale for the provision of export finance, the CSO proposal would split the flow of export finance in accounting terms

between public and private sectors. Export finance would switch from one to another in response to relative interest rates. Transactions would start off in the private sector with funds drawn from interbank market, switching to the public sector when funds from capital market were substituted. It would be odd to reclassify a single export finance transaction, possibly more than once during life of a credit, from one sector to another. Such accounting treatment would obscure rather than clarify the size of the transactions and the extent of HMG assistance.

7. Second - a more substantive problem - if the transactions fall within the public sector, a scheme designed to reduce the cost to the taxpayer of the existing arrangements ends by looking as if it adds to costs. Financial benefits will be the same but will look unappealing by comparison with NLF rather than bank finance.

8. The presentation will be awkward in another respect. The Government has no wish to change the present private sector basis of the system. Obviously we need to ensure HMG's subsidies (the difference between Consensus and market rates) are minimised. If the process of minimising these brings part of the finance within the public sector, this could cause unwelcome pressure for a purely public sector operation.

9. Third - other countries, including French, are beginning to copy our capital market guarantee ideas, also on cost reduction grounds. Their intention is to encourage "pure cover" (no subsidy) operations in rich markets where bond finance may enable their exporters to offer lower interest rates. This was one of the early incentives to the UK banks' development of vehicle/bond market schemes. The classification of vehicles to the public sector involves a real risk that UK exporters may be denied these advantages. Our competitors will claim that as public corporations rather than private companies the vehicles must be official institutions bound by Consensus rules and must offer Consensus interest rates. There is already argument within the Consensus about the status of particular

countries' financing institutions. (Other countries classify their export credit institutions differently eg Coface and Hermes - French and German agencies - are both private sector companies.)

10. Finally - a point which most closely involves the CSO's own interests - the very ingenuity of the solution proposed will inevitably attract attention. Public sector classification will be unexpected. There is a long history of private sector classification and the purpose of limited change now proposed is known by banks and exporters to be cost saving. The special treatment proposed - vehicles in public sector but their borrowing and lending excluded from public expenditure and PSBR - will inevitably raise suspicions of HMG fiddling the books. Such suspicions will be difficult to dispel. They will be just as bad for CSO as for Treasury.

11. The solution which seems least likely to present these problems is the one which cuts across the existing rules ie to treat vehicles as in the private sector.

12. The application of the CSO's normal guidelines has understandably led to the CSO ruling that vehicles would be in the public sector. But the policy problems arising from straightforward application of these principles have to be recognised. Our conclusion is that an exception should be made for these operations on pragmatic grounds. The justification for doing so would be that there is no difference in basic rationale, merely in form, between the new proposals and traditional bank funded FREF and refinancing. It would be preferable not to have to do this. But for wider reasons this would provide the least damaging way to achieve what is in the general interest.

FROM: MRS A F CASE
DATE: 9 January 1987

1. SIR PETER MIDDLETON
2. CHANCELLOR OF THE EXCHEQUER

cc Mr Lavelle
Mr Mountfield
Mr Bush

ECGD GUARANTEED VEHICLES

I understand that you asked for "plain man's guide" to paragraph 9 of the aide memoire which deals with the possible use of ECGD guaranteed vehicles for pure cover operations.

2. Under the Consensus rules, official financing institutions eg ECGD are required to abide by the minimum interest rate levels prescribed by the Consensus. The present rates range from 9.8% to 7.4% depending on the status of the importing country. They are subject to change at 6 month intervals, in the light of observed movements in international interest rates. However, where the only support provided is an export credit guarantee (so called pure cover) and finance is provided on commercial terms, these minima do not apply. This may offer competitive advantages for the exporter and benefits for the Exchequer (as interest make up subsidies do not have to be provided). UK policy is to encourage such pure cover arrangements.

3. The extent to which opportunities exist to use pure cover arrangements obviously varies with relative interest rate movements. It is clearly greatest in rich markets. But these possibilities lay behind the agreement in 1983 to allow ECGD to guarantee bond issues for export finance and were an important factor behind Lloyds Merchant Bank's enthusiasm for the creation of an ECGD guaranteed vehicle. In their view use of the capital markets, including swaps, could lead to the provision of attractive sub-Consensus rates in rich and intermediate markets. The recent French encouragement of guaranteed bond issues seems to be fuelled by the same interest in securing a possible competitive advantage for French exporters together with cost savings for the Government.

4. However in recent international Consensus discussions concern has emerged about the extent to which some export financing institutions, predominantly private sector owned but with some official links or operating two windows (official and non-official) are taking advantage of the pure cover system. We clearly want to maximise our opportunities to do so through ECGD guaranteed vehicles. Classification of such vehicles to the public sector would provide valuable ammunition for competitors who sought to challenge their ability to do so.

AFC

MRS A F CASE

3741/003

CONFIDENTIAL

FROM: P D P BARNES
DATE: 12 January 1987

c/ I understand that when you spoke to the EST about this last Friday, he had not read the papers. He has now done so and these are his views.

CR 12/1.

PS/CHANCELLOR

cc PS/Chief Secretary
Sir P Middleton
Mr F E R Butler
Sir G Littler
Mr Lavelle
Mr Mountfield
Mr Turnbull
Mrs Butler
Mrs Case
Mr Bush

ECGD GUARANTEED VEHICLES

The Chancellor asked for the Economic Secretary's views on this subject. Following his discussion with the Chancellor last Friday, the Economic Secretary cannot really see the point of these vehicles. The benefit of securitisation is already available to banks if they want it. And the banks can guarantee the vehicles themselves if they wish. The Economic Secretary can see no case for Government backing beyond ECGD cover.

I have much sympathy with this reaction. I would add that I cannot see the need to renegotiate with the banks so that the simplicity of securitisation is spoilt and does not allow outsiders to the banks.

RB

P D P BARNES
Private Secretary

CONFIDENTIAL

1496/013/ISS

FROM: H P EVANS
DATE: 14 January 1987

CHANCELLOR

Thanks.
I shall be interested
to see the results.

cc: Sir P Middleton
Sir T Burns
Sir G Littler
Mr Odling-Smee
Mr Grice
Mr Dolphin

OECD STUDY OF "SUSTAINABILITY"

Following discussion in WP3 last year, the OECD Secretariat have began a study on the concept of "sustainability" in economic policies. The study is designed to illuminate the following questions:

(1) What were the factors that gave rise to situations that were eventually judged unsustainable?

(2) What factors prompted a policy response?

(3) Were there advance warnings in these situations which, if they had been heeded, might have permitted more timely adjustment?

2. The examination of particular historical episodes within this framework will, it is hoped, provide useful insights into how the notion of sustainability can be made more operational.

3. For the United Kingdom, the particular episode chosen - after consulting us - is the 1972 to 1976 period. We are not being singled out: all other members of WP3 will, we understand, have one of their periods of history scrutinised by the Secretariat.

4. We have been promised full opportunities to see and comment on the conclusions drawn by the Secretariat. It is expected that papers will be discussed at the June meeting of WP3. No decisions about publication have yet been taken.

5. Two members of the Secretariat will be in London for a day or so at the end of this month to discuss with officials in HMT, and the Bank, and with a few others (including some, like Sir Douglas Wass, and Sir Kit McMahon who were closely involved in policies in the 1970's).

6. This is for information only: no action required.

HPE

H P EVANS

7/003

PPS 12/2

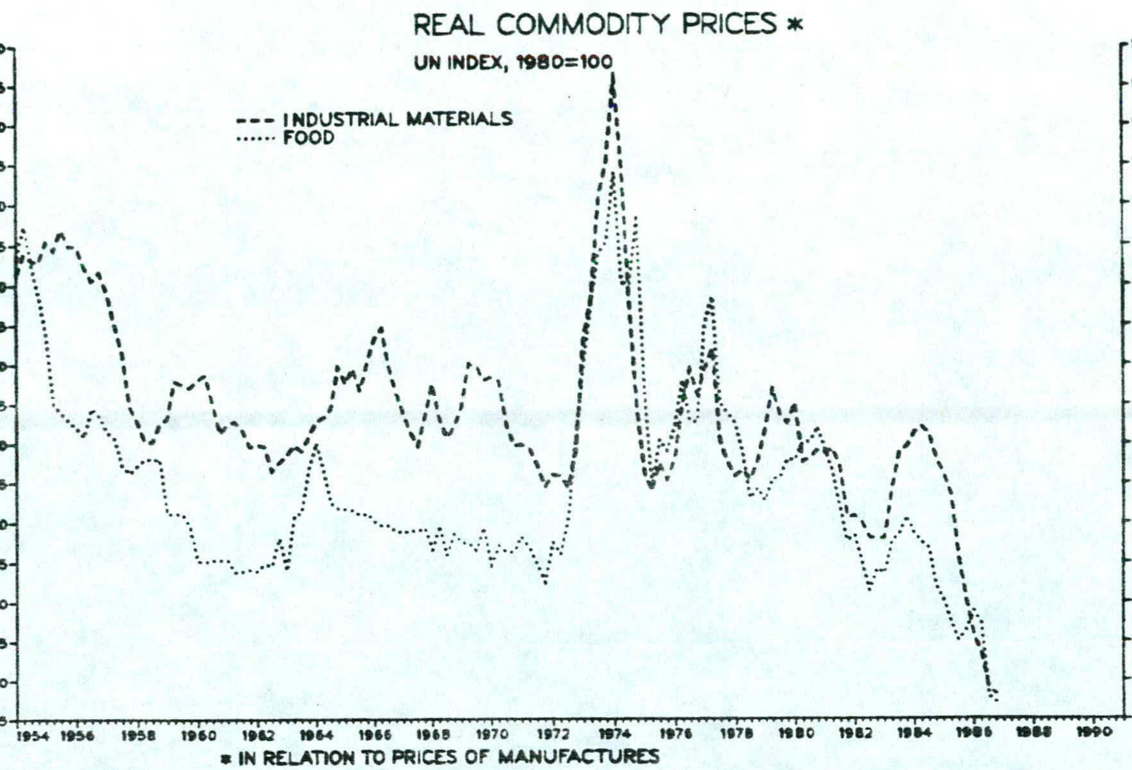
ECONOMIST COMMODITY PRICE INDICES

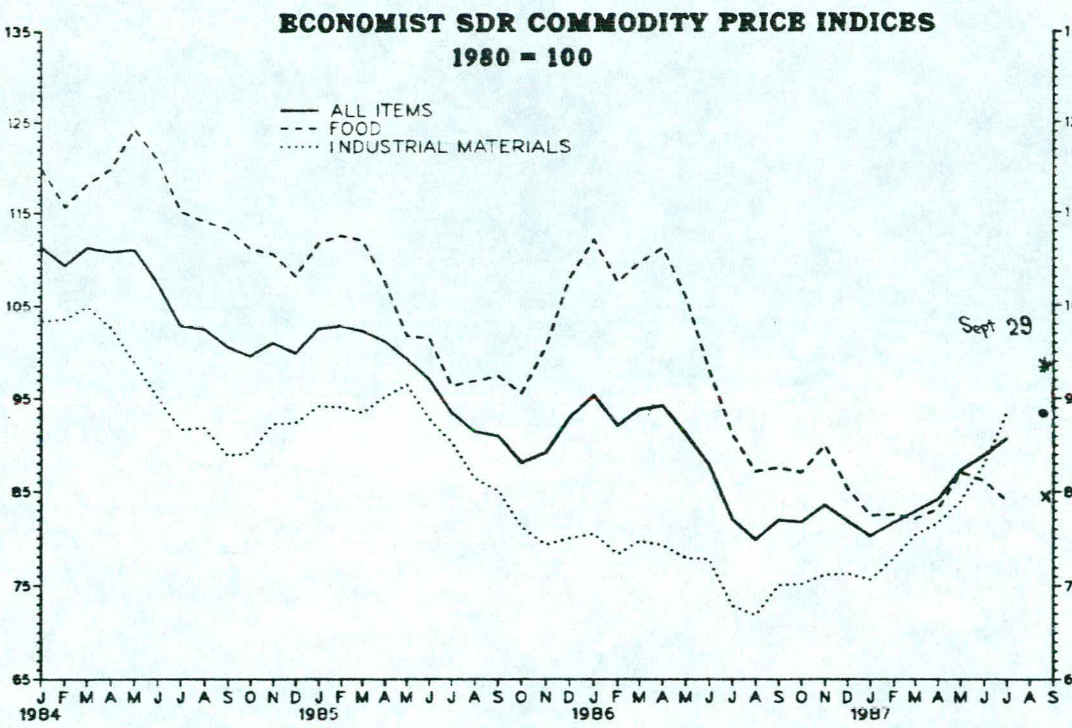
1980=100

	All items indices				SDR indices		
	SDR	Dollar	Sterling	Real*	Food	Nfa**	Metals
Annual							
1980	100.0	100.0	100.0	100.0	100.0	100.0	100.0
1981	95.1	86.2	99.4	91.1	96.9	98.6	89.5
1982	87.9	74.7	99.2	81.6	92.3	90.4	79.1
1983	102.7	84.3	129.4	95.5	105.5	109.8	92.8
1984	105.7	83.4	144.9	97.8	116.1	105.1	89.5
1985	95.8	74.8	135.2	86.5	103.4	94.2	84.3
1986	86.9	77.7	124.0	74.5	97.3	85.0	70.5
Quarterly							
1985 Q4	90.1	74.7	121.0	80.3	101.4	86.9	75.0
1986 Q1	93.7	80.9	130.8	81.7	109.7	87.1	73.6
Q2	91.0	81.1	125.0	79.5	104.9	86.9	71.8
Q3	81.4	75.2	117.4	70.3	88.8	80.1	68.3
Q4	82.4	76.4	123.9	70.1	87.4	86.5	68.4
1987 Q1	81.6	79.2	119.2	68.9	82.4	91.0	69.0
Q2	86.8	86.4	122.2	73.3	85.5	98.0	75.2
Q3 (prov)	91.4	89.6	128.9	75.9	82.6	107.1	87.5
Monthly							
October	81.8	76.2	123.9		87.1	84.6	68.3
November	83.6	76.9	125.4		90.0	87.0	68.4
December	81.9	76.1	122.7		85.4	87.5	68.4
January	80.3	77.0	118.8		82.5	88.8	66.7
February	81.7	79.6	120.5		82.6	91.7	68.5
March	82.9	81.0	118.2		82.1	92.4	71.8
April	84.2	83.8	119.0		83.2	94.8	72.6
May	87.3	87.6	122.0		87.1	97.2	74.8
June	88.9	87.8	125.2		86.2	101.7	78.3
July	90.7	88.4	127.8		84.0	105.1	84.7
August	92.2	89.8	130.9		81.2	109.7	90.2
September (prov)	91.4	90.6	128.2		82.7	106.6	87.6
Weekly							
July 7	90.9	88.9	127.5		84.7	105.1	84.2
14	90.9	88.8	128.1		84.6	105.5	84.4
21	90.3	87.6	127.6		83.9	104.8	83.9
28	90.7	88.2	128.2		82.9	105.1	86.3
August 4	91.4	88.3	130.7		81.1	107.4	89.4
11	92.6	89.2	132.0		81.5	107.9	92.0
18	93.4	91.2	131.1		81.6	112.7	91.6
25	91.4	90.5	130.0		80.9	110.9	88.0
September 1	90.0	89.4	126.7		81.4	109.6	83.8
8	90.4	90.3	126.4		81.8	107.2	85.7
15	91.3	90.4	127.8		83.1	107.8	86.0
22	91.8	91.0	128.8		82.8	104.5	89.8
29 (prov)	93.5	91.9	131.2		84.4	104.0	92.8

* In relation to prices of manufactured exports. Recent figures are estimated.

** Non-food agriculturals





• All Items
× Food
* Industrial Materials

77003

PPS 12/2

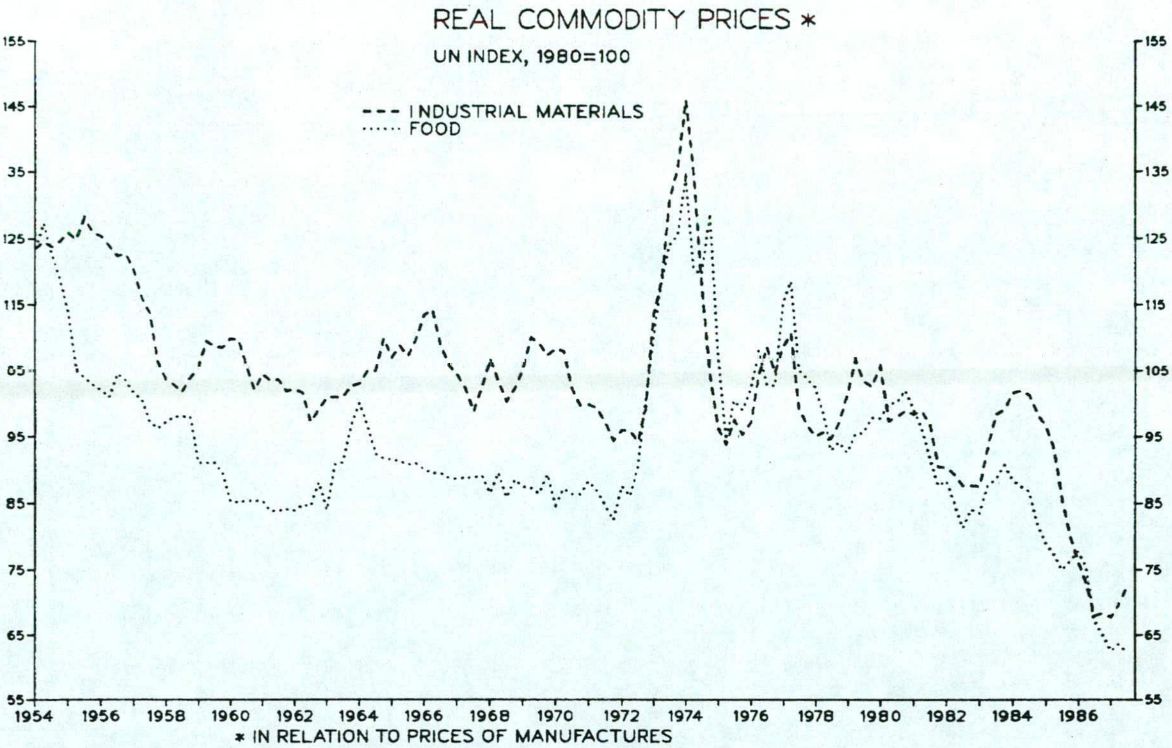
pmp

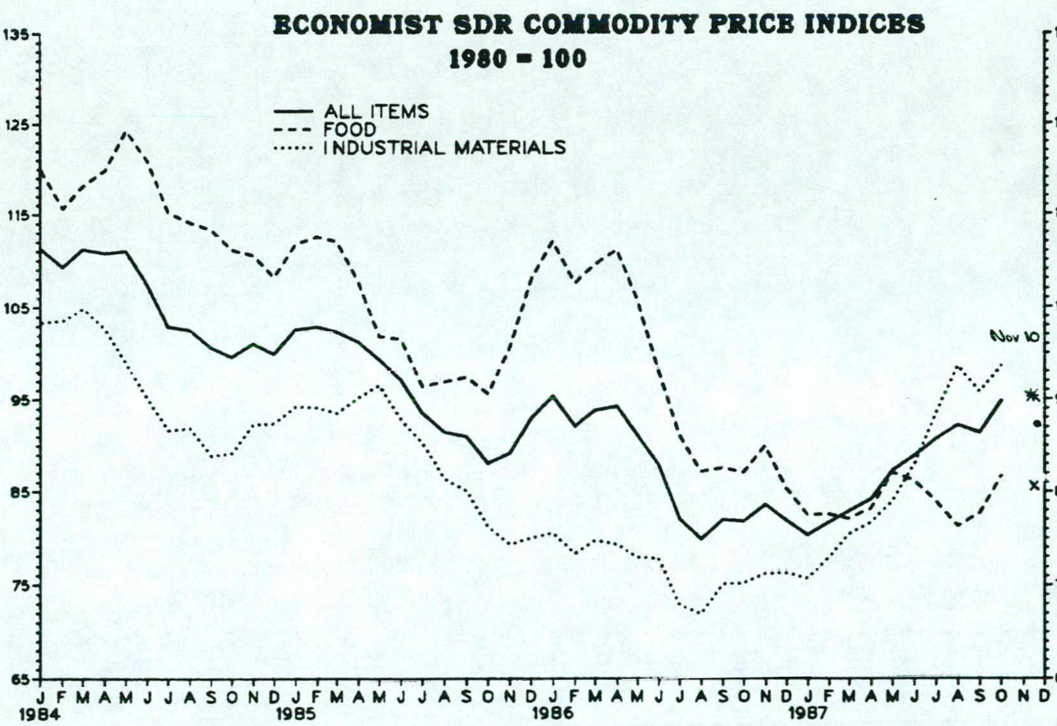
ECONOMIST COMMODITY PRICE INDICES 1980=100

	All items indices				SDR indices		
	SDR	Dollar	Sterling	Real*	Food	Nfa**	Metals
Annual							
1980	100.0	100.0	100.0	100.0	100.0	100.0	100.0
1981	95.1	86.2	99.4	91.1	96.9	98.6	89.5
1982	87.9	74.7	99.2	81.6	92.3	90.4	79.1
1983	102.7	84.3	129.4	95.5	105.5	109.8	92.8
1984	105.7	83.4	144.9	97.8	116.1	105.1	89.5
1985	95.8	74.8	135.2	86.5	103.4	94.2	84.3
1986	86.9	77.7	124.0	74.5	97.3	85.0	70.5
Quarterly							
1985 Q4	90.1	74.7	121.0	80.3	101.4	86.9	75.0
1986 Q1	93.7	80.9	130.8	81.7	109.7	87.1	73.6
Q2	91.0	81.1	125.0	79.5	104.9	86.9	71.8
Q3	81.4	75.2	117.4	70.3	88.8	80.1	68.3
Q4	82.4	76.4	123.9	70.1	87.4	86.5	68.4
1987 Q1	81.6	79.2	119.2	68.9	82.4	91.0	69.0
Q2	86.8	86.4	122.2	73.3	85.5	98.0	75.2
Q3	91.4	89.6	128.9	75.9	82.6	107.1	87.5
Monthly							
November	83.6	76.9	125.4		90.0	87.0	68.4
December	81.9	76.1	122.7		85.4	87.5	68.4
January	80.3	77.0	118.8		82.5	88.8	66.7
February	81.7	79.6	120.5		82.6	91.7	68.5
March	82.9	81.0	118.2		82.1	92.4	71.8
April	84.2	83.8	119.0		83.2	94.8	72.6
May	87.3	87.6	122.0		87.1	97.2	74.8
June	88.9	87.8	125.2		86.2	101.7	78.3
July	90.7	88.4	127.8		84.0	105.1	84.7
August	92.2	89.8	130.9		81.2	109.7	90.2
September	91.4	90.6	128.2		82.7	106.6	87.6
October	94.8	94.2	132.2		86.7	101.9	94.3
Weekly							
August 25	91.4	90.5	130.0		80.9	110.9	88.0
September 1	90.0	89.4	126.7		81.4	109.6	83.8
8	90.4	90.3	126.4		81.8	107.2	85.7
15	91.3	90.4	127.8		83.1	107.8	86.0
22	91.8	91.0	128.8		82.8	104.5	89.8
29	93.5	91.9	131.1		84.4	103.9	92.8
October 6	95.7	94.1	134.1		86.6	105.2	95.2
13	96.1	95.4	134.7		86.7	102.5	97.9
20	93.4	93.3	131.0		86.2	101.1	91.5
27	93.9	94.2	129.1		87.2	98.9	92.7
November 3	91.0	93.6	124.9		84.3	96.8	89.8
10 (prov)	92.2	96.6	125.7		85.3	96.0	92.3

* In relation to prices of manufactured exports. Recent figures are estimated.

** Non-food agriculturals





• All Items

x Food

✱ Industrial Materials

PPS 12/2

ECONOMIST COMMODITY PRICE INDICES

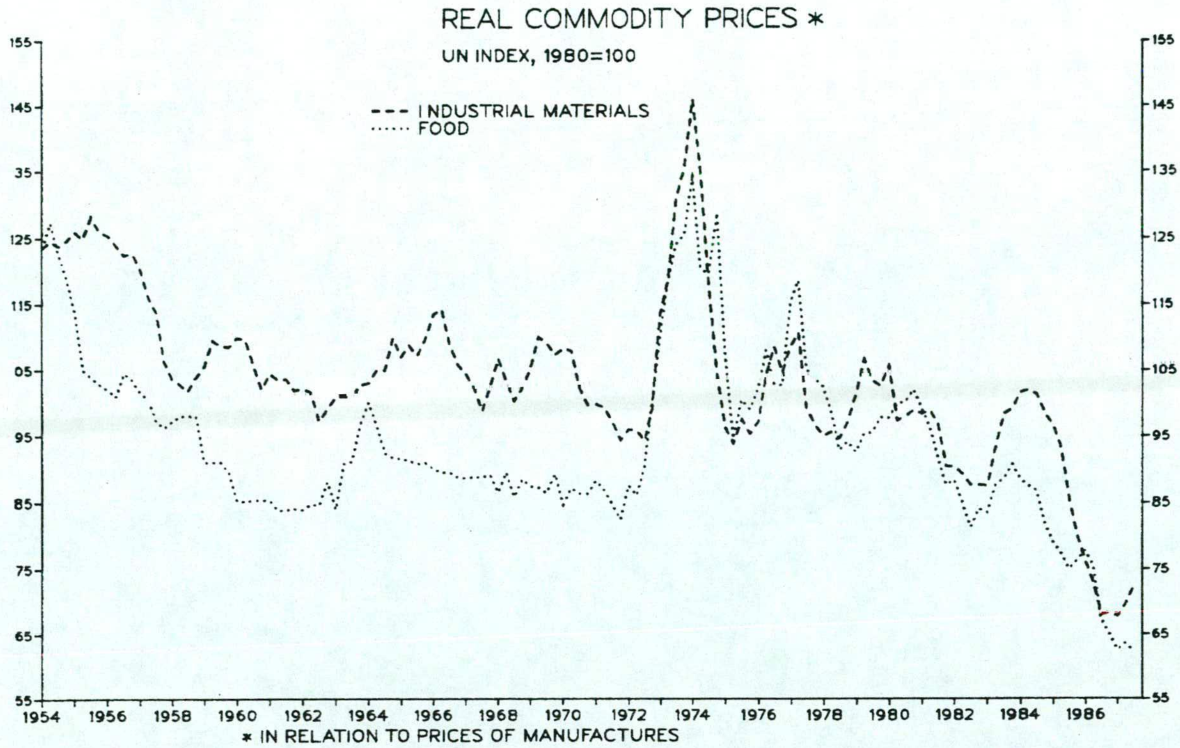
1980=100

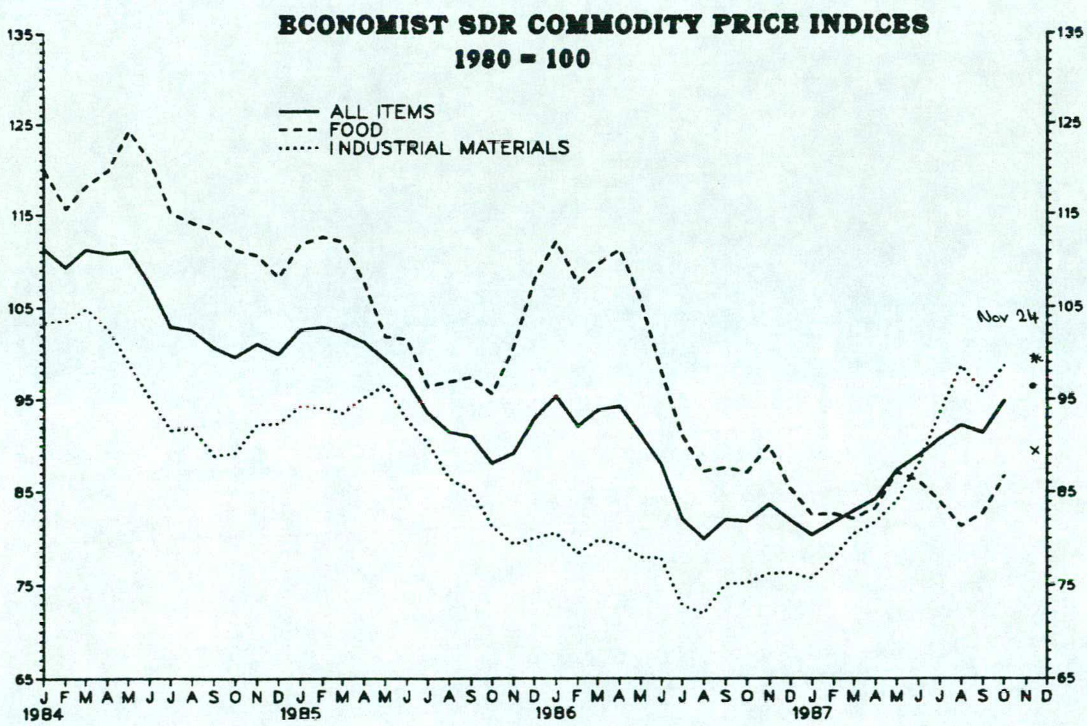
pmp

	All items indices				SDR indices		
	SDR	Dollar	Sterling	Real*	Food	Nfa**	Metals
Annual							
1980	100.0	100.0	100.0	100.0	100.0	100.0	100.0
1981	95.1	86.2	99.4	91.1	96.9	98.6	89.5
1982	87.9	74.7	99.2	81.6	92.3	90.4	79.1
1983	102.7	84.3	129.4	95.5	105.5	109.8	92.8
1984	105.7	83.4	144.9	97.8	116.1	105.1	89.5
1985	95.8	74.8	135.2	86.5	103.4	94.2	84.3
1986	86.9	77.7	124.0	74.5	97.3	85.0	70.5
Quarterly							
1985 Q4	90.1	74.7	121.0	80.3	101.4	86.9	75.0
1986 Q1	93.7	80.9	130.8	81.7	109.7	87.1	73.6
Q2	91.0	81.1	125.0	79.5	104.9	86.9	71.8
Q3	81.4	75.2	117.4	70.3	88.8	80.1	68.3
Q4	82.4	76.4	123.9	70.1	87.4	86.5	68.4
1987 Q1	81.6	79.2	119.2	68.9	82.4	91.0	69.0
Q2	86.8	86.4	122.2	73.3	85.5	98.0	75.2
Q3	91.4	89.6	128.9	75.9	82.6	107.1	87.5
Monthly							
December	81.9	76.1	122.7		85.4	87.5	68.4
January	80.3	77.0	118.8		82.5	88.8	66.7
February	81.7	79.6	120.5		82.6	91.7	68.5
March	82.9	81.0	118.2		82.1	92.4	71.8
April	84.2	83.8	119.0		83.2	94.8	72.6
May	87.3	87.6	122.0		87.1	97.2	74.8
June	88.9	87.8	125.2		86.2	101.7	78.3
July	90.7	88.4	127.8		84.0	105.1	84.7
August	92.2	89.8	130.9		81.2	109.7	90.2
September	91.4	90.6	128.2		82.7	106.6	87.6
October	94.8	94.2	132.2		86.7	101.9	94.3
November (prov)	93.6	97.0	127.6		86.5	97.2	93.8
Weekly							
September 8	90.4	90.3	126.4		81.8	107.2	85.7
15	91.3	90.4	127.8		83.1	107.8	86.0
22	91.8	91.0	128.8		82.8	104.5	89.8
29	93.5	91.9	131.1		84.4	103.9	92.8
October 6	95.7	94.1	134.1		86.6	105.2	95.2
13	96.1	95.4	134.7		86.7	102.5	97.9
20	93.4	93.3	131.0		86.2	101.1	91.5
27	93.9	94.2	129.1		87.2	98.9	92.7
November 3	91.0	93.6	124.9		84.3	96.8	89.8
10	92.1	96.5	125.5		85.3	95.4	92.3
17	94.8	97.8	128.8		87.3	98.3	95.4
24 (prov)	96.5	100.1	131.2		89.2	98.3	97.7

* In relation to prices of manufactured exports. Recent figures are estimated.

** Non-food agriculturals





• All Items

x Food

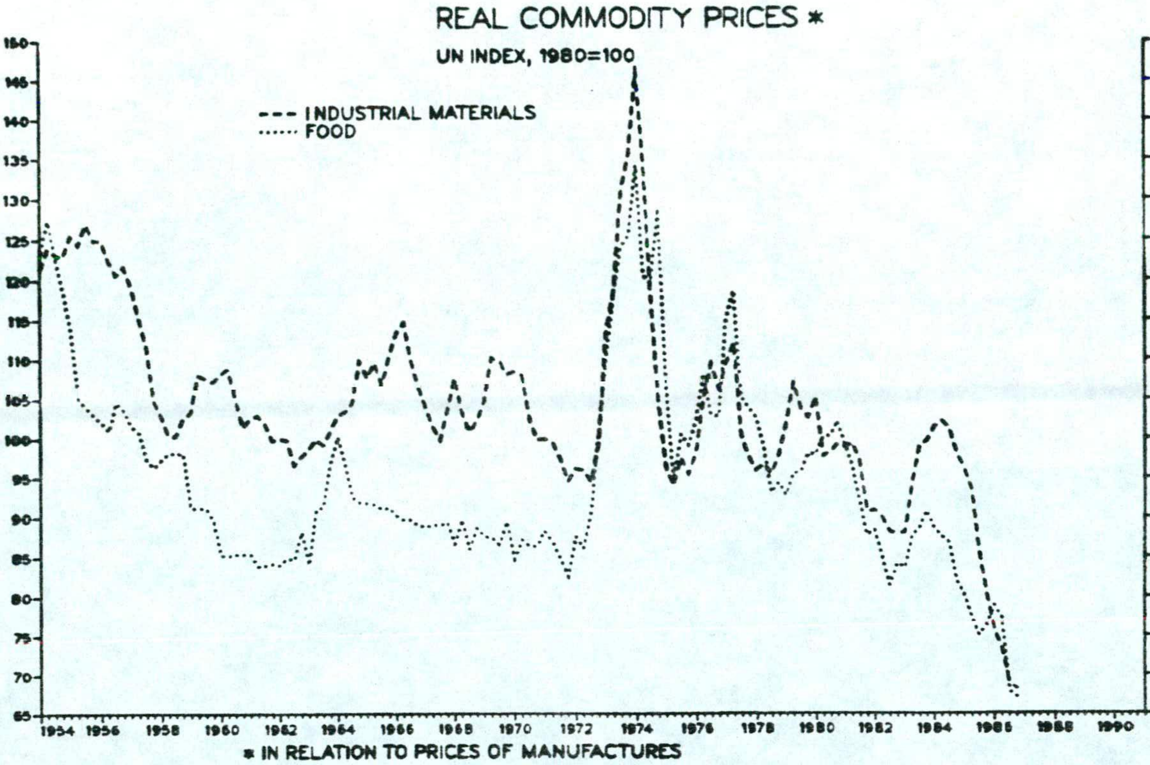
* Industrial Materials

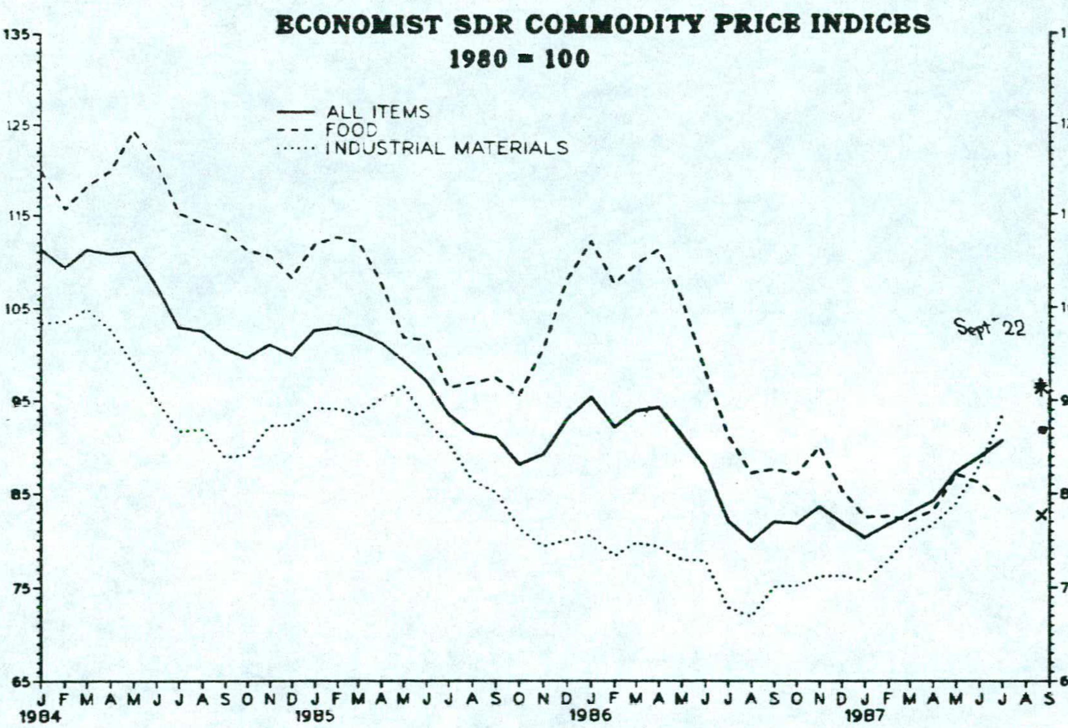
ECONOMIST COMMODITY PRICE INDICES PPS 12/2 **1980=100**

	All items indices				SDR indices		
	SDR	Dollar	Sterling	Real*	Food	Nfa**	Metals
Annual							
1980	100.0	100.0	100.0	100.0	100.0	100.0	100.0
1981	95.1	86.2	99.4	91.1	96.9	98.6	89.5
1982	87.9	74.7	99.2	81.6	92.3	90.4	79.1
1983	102.7	84.3	129.4	95.5	105.5	109.8	92.8
1984	105.7	83.4	144.9	98.1	116.1	105.1	89.5
1985	95.8	74.8	135.2	87.6	103.4	94.2	84.3
1986	86.9	77.7	124.0	76.7	97.3	85.0	70.5
Quarterly							
1985 Q3	92.1	72.7	122.9	82.6	96.9	93.2	82.7
Q4	90.1	74.7	121.0	80.3	101.4	86.9	75.0
1986 Q1	93.7	80.9	130.8	81.7	109.7	87.1	73.6
Q2	91.0	81.1	125.0	80.3	104.9	86.9	71.8
Q3	81.4	75.2	117.4	73.7	88.8	80.1	68.3
Q4	82.4	76.4	123.9	71.4	87.4	86.5	68.4
1987 Q1	81.6	79.2	119.2	70.3	82.4	91.0	69.0
Q2	86.8	86.4	122.2	74.7	85.5	98.0	75.2
Monthly							
September	82.0	76.3	120.7		87.6	82.5	69.5
October	81.8	76.2	123.9		87.1	84.6	68.3
November	83.6	76.9	125.4		90.0	87.0	68.4
December	81.9	76.1	122.7		85.4	87.5	68.4
January	80.3	77.0	118.8		82.5	88.8	66.7
February	81.7	79.6	120.5		82.6	91.7	68.5
March	82.9	81.0	118.2		82.1	92.4	71.8
April	84.2	83.8	119.0		83.2	94.8	72.6
May	87.3	87.6	122.0		87.1	97.2	74.8
June	88.9	87.8	125.2		86.2	101.7	78.3
July	90.7	88.4	127.8		84.0	105.1	84.7
August	92.2	89.8	130.9		81.2	109.7	90.2
Weekly							
July 7	90.9	88.9	127.5		84.7	105.1	84.2
14	90.9	88.8	128.1		84.6	105.5	84.4
21	90.3	87.6	127.6		83.9	104.8	83.9
28	90.7	88.2	128.2		82.9	105.1	86.3
August 4	91.4	88.3	130.7		81.1	107.4	89.4
11	92.6	89.2	132.0		81.5	107.9	92.0
18	93.4	91.2	131.1		81.6	112.7	91.6
25	91.4	90.5	130.0		80.9	110.9	88.0
September 1	90.0	89.4	126.7		81.4	109.6	83.8
8	90.4	90.3	126.4		81.8	107.2	85.7
15	91.3	90.4	127.8		83.1	107.8	86.0
22 (prov)	91.8	91.0	128.8		82.8	104.6	89.8

* In relation to prices of manufactured exports. Recent figures are estimated.

** Non-food agriculturals





• All Items
× Food
✱ Industrial Materials

A01036

C/ Rather surprisingly, Mr Hibbert has agreed to private sector classification. But, he intends to press ahead with his review of public/private sector classification

CR 15/1

Rup

CH/EXCHEQUER
REC. 15 JAN 1987 ✓ 15/1
ACTION SIR P MIDDLETON
COPIES TO

CABINET OFFICE

Central Statistical Office

Great George Street, London SW1P 3AQ Telephone 01-~~233-6117~~ 270 6155

From the Director: J. Hibbert

15 January 1987

Dear Peter,

EXPORT FINANCE VEHICLES

Following my meeting with the Chancellor last Friday, and our study of the aide-memoire "Export Finance: Classifications", I am now writing to let you know what I have decided about the classification of the proposed vehicles in our national accounts statistics.

2. You will not need reminding that consideration of the issues arising has been particularly tortuous and protracted. Those involved have spent many hours thinking about and discussing what is to be a wholly new type of financial arrangement, to which our existing criteria for classification could not readily, or easily, be applied to yield a solution which was seen as sensible and workable.

3. The criteria for the institutional sector classification of a body which have been followed in the past are concerned with ownership and control. Over the years the degree of control has come to be seen as a more important criterion than ownership because it was thought that this was the more crucial factor in determining behaviour, one major rationale underlying the institutional sector classification being that those units in the same sector might be expected to behave in a similar fashion.

4. The detailed controls which ECGD would have over the establishment and functioning of the proposed vehicle, which seem to arise wholly from the existence of a Government guarantee on borrowing, pointed heavily in the direction of public sector classification. The reasons for the requirement that the vehicle's borrowing should be guaranteed by the Government have still not been explained to my full satisfaction but, as I now understand the situation, in order that the capital market can be tapped on a continuing basis in the way proposed the Government

Sir Peter Middleton
HM Treasury
Parliament Street
SW1P 3AG

guarantee of borrowing is needed since, even though potential lenders might be willing to invest in the vehicle on the basis of its prospective assets (Government guaranteed export loans), absence of the guarantee would necessarily lead to action by the Bank of England under the Banking Act. There would seem to be two possible ways of interpreting this situation in terms of the statistical classification of the vehicle. On one interpretation one might say that, since the Government guarantee is a necessary condition for the existence of the vehicle, the vehicle should therefore be regarded as being in the public sector. A second interpretation, however, would be that the Government guarantee is simply a formality which, although rendering possible the existence of the vehicle, does so in order to meet a purely legal requirement, not because there would be any doubts about the financial standing of the vehicle, since the funds it is to borrow are to be invested in assets subject to ECGD guarantees. Thus, in this very new type of financial arrangement application of the criterion of control, which here arises as a result of the Government guarantee on borrowing, apparently leads us to a conclusion which on one interpretation would be seen as correct and sound, but on another only formally correct and in conflict with the underlying realities.

5. These conceptual imponderables have led me to the following conclusions:

(a) If my understanding of the reasons for the existence of the Government guarantee on the proposed vehicle's borrowing is correct, we should now accept that its institutional sector classification should be settled on pragmatic considerations based on the uses to which the resulting statistics are to be put. From this point of view I agree that the vehicle should be classified as a private sector financial institution.

(b) It follows from (a) that, if any dispute should arise about the status of a new vehicle in such a context as international discussion of the Consensus rules, it will not be possible to argue that classification of the vehicle in the UK national accounts to the private sector clearly indicates that it is a private sector body. If the status of a new vehicle has to be defended, it will have to be done purely on the legal and other characteristics of the vehicle itself, rather than on the basis of its statistical classification which has been decided on pragmatic rather than conceptual grounds.

A01036

(c) The present criteria for the distinction between public and private sector bodies are unsatisfactory and, if possible, need to be simplified so that the frequency with which difficult borderline cases arise may be reduced. I am accordingly putting in train a review of this. There are several good reasons for doing so, not the least of which is that a system which has consumed so much time of highly-paid staff (not only in the case of the proposed vehicles but in numerous previous instances where public/private sector classification problems have arisen) needs to be reviewed on value for money grounds. As I have already indicated to both you and the Chancellor, the way forward may be to move towards a set of criteria which would take more account of the political/administrative dimension of the distinction between public and private sector bodies, perhaps by linking the criteria more directly to Parliamentary control and accountability. I cannot say how long this will take but we shall, of course, liaise closely with the Treasury.

6. I am copying this to the Chancellor's private secretary.

Yours sincerely

Jack Hibbert

J HIBBERT

c/ Back papers are with you. I have passed on to Anthea the gist of your conversation with PEM this morning

FROM: MRS A F CASE
DATE: 16 January 1987

SIR PETER MIDDLETON

cc Principal Private Secretary
PS/Chief Secretary
PS/Economic Secretary
Mr F E R Butler
Sir G Littler
Mr Lavelle
Mr Mountfield
Mr Turnbull
Mr Scholar
Mrs Butler
Mr Bush

Ch
I have passed your thanks to Mr Hibbert's office
AA

CC 16/1

Obs suggestion ?

phoned through.

ECGD : EXPORT FINANCE VEHICLES

Mr Hibbert's letter to you of 15 January contains the welcome news that the CSO have decided that the proposed ECGD guaranteed vehicles should be classified to the private sector. Mr Hibbert also indicates his intention, in consultation with the Treasury of carrying out a review of the criteria for the distinction between public and private sector bodies.

2. From AEF's point of view this outcome is very satisfactory. We can now take forward not only the individual vehicle cases (GEFCO and Guangdong) on the basis originally proposed but can press on with the negotiations with the banking associations. None of the points in Mr Hibbert's letter setting out the grounds on which he has reached his conclusion seem likely to cause difficulties either operationally or presentationally. Essentially, Mr Hibbert has chosen to regard the liability guarantee as a legal formality rather than an expression of Government "control". That seems right. In our discussions with the banks, we were driven from an asset to a liability side guarantee when we realised that without exemption from the Banking Act (which only a liability guarantee would provide) the vehicle would be inhibited in the frequency with which they could go to the market. This would have limited their role to very simple, essentially one off, operations.

3. Mr Hibbert also warns that we will not be able to use private sector classification in the national accounts in international Consensus discussions about whether vehicles are official financing

institutions. This is not too worrying. Our argument in those discussions would be essentially the same as that deployed in discussion with the CSO ie that their structure represented a pragmatic solution to tapping the capital markets.

4. I do not see any need to defend the CSO's conclusion in the near future, although it could come up at ECGD's next appearance before the PAC in March. We will obviously clear any line to take then both within the Treasury and with CSO.

5. I understand that Mrs Butler has already expressed concern that the proposed review should not be seen as offering a quick or easy solution to these classification problems for the future. That thought is reflected in the last paragraph of the attached draft letter which otherwise thanks Mr Hibbert for his helpful decision.

MRS A F CASE

DRAFT LETTER TO J HIBBERT - CABINET OFFICE

EXPORT FINANCE VEHICLES

Thank you very much for your letter of 15 January setting out the conclusions you have reached on the difficult issues posed by classification of ECGD guaranteed vehicles. As you say, these have taken up a tremendous amount of time both in the CSO and in the Treasury and I am grateful for the time and trouble which you have taken.

2. Your decision in favour of private sector classification on pragmatic grounds is very welcome. This will now enable ECGD to take forward their proposal and secure the benefits of a revised FREF structure. We will ensure that they understand what you have said about the implications of the basis of the private sector classification in any international Consensus discussions.

3. You have also indicated your intention to review the present criteria for the distinction between public and private sector bodies. I welcome this, though it ~~This~~ will not be an easy task, nor as you indicate, one likely to produce early results. I am grateful for your offer to keep in close touch with us as the work progresses.

CONFIDENTIAL

hpe9/18.1

Ch
Looks OK to me
AA

FROM: HUW EVANS
DATE: 20 JANUARY 1987

In general fine. 2. Emphasis in para 3, however, is (I assume) that the national projections [illegible] suffer from political inhibitions / stabilisation, whereas Fund projections do not [illegible] [illegible] all projections maybe [illegible]

1. SIR G LITTLER

2. CHANCELLOR

cc Sir P Middleton
Sir T Burns
Mr Odling-Smee
Mr Peretz
Mr Matthews
Ms Symes

I think it would be helpful to put something like this to my colleagues before our meeting. GL 21/1

INDICATORS

In a note of 20 November on this subject, we floated the possibility of a paper to put to G7 Deputies on the UK ideas in this area. I attach a draft paper, for circulation to other G7 Deputies and the IMF in advance of the meeting planned for later this month.

2. The draft covers mainly:

   (a) Fund and national projections (paragraph 3);

   (b) presentation of tables (paragraphs 4-5);

   (c) indicators for the G7 as a whole (paragraphs 7-12);

   (d) commodity prices (paragraphs 13-16).

3. (a) Repeats our line, which we put to the Fund staff in the Autumn, that we need Fund, as well as national, projections. (c) and (d) are ways of taking forward, with examples, the suggestions in the Chancellor's Speech to the Annual Meetings in September.

4. It would be helpful to have comments in the next day or two, so that the paper can be circulated a week or so in advance of the end January meeting.

HPE

H P EVANS

hpe1/18.1

INDICATORS

1. The Venice Declaration in June 1987 noted the wish to continue economic co-ordination efforts and to strengthen surveillance of our economies through:

- "the commitment by each country to develop medium term objectives and projections for its economy, and for the group to develop objectives and projections, that are mutually consistent both individually and collectively";

and

- "the use of performance indicators to review and assess current economic trends and to determine whether there are significant deviations from an intended course that require consideration of remedial actions".

Our Ministers and Governors have since reaffirmed their commitment to economic policy co-ordination efforts, in Washington in September and in the statement issued on 23 December.

The present position

2. At our last G7 Deputies meeting in Washington in September we asked the IMF staff to collect national projections to serve as a basis for further discussion by Deputies of the procedures and format for presenting indicators. The Fund staff's "numero zero" paper of 2 December collects mainly national projections of key variables and is a helpful contribution to the exercise. In particular, it provides an extremely useful commentary and a comprehensive set of questions about the mutual compatibility of countries' policies. It is worth noting that this commentary by the Fund staff is to a considerable extent independent of the precise numbers in the tables, as is most of our discussion of policies and their co-ordination. We should now consider the directions in which we can take this exercise further and improve its presentation, apart from the obvious need for updating, for our collective discussion and appraisal.

Fund or national projections?

3. For earlier discussions in our group, the Fund staff provided its own set of projections on a consistent basis for each of our countries. I continue to see much advantage in inviting the Fund to offer again its own projections, independently but after discussion with countries. Consistent projections are a necessary basis for assessing the sustainability of existing policies and exchange rates and analysing the effects of potential spillovers. Inevitably, and as the recent "numero zero" exercise shows, the numbers provided by national authorities will be compiled at different dates and on different assumptions, making it impractical to convert such national projections to a consistent basis. Moreover, national forecasts will, for good reasons at certain times, be incomplete or outdated. Fund projections can, however, by arrangement, be provided on a timely basis.

Presentation

4. The presentation of indicators in the Fund staff's "numero zero" paper includes both short term forecasts and medium term projections/objectives.

5. I think it would be helpful to draw a clearer distinction between objectives and forecasts/projections. Vertical dividing lines in the tables; a different type of print - both these are possibilities. Having clarified the status of the numbers, the Fund would be able to provide a commentary on whether forecasts were being realised and whether objectives were realistic and mutually consistent. In any event, the notes to the tables should make clear the distinction between **short term forecasts**, which in the case of nationally prepared figures may have been prepared a few months earlier and thus not reflect fully the consequences of recent changes, and **medium term projections** derived from a set of assumptions. The tables setting out the forecasts/projections/objectives of both Fund and National authorities should provide:

(a) the necessary information for inclusion in the tables;

(b) the date at which projections or forecasts were finalised; and

(c) a record of the key assumptions - including exchange rates, monetary and fiscal policy, world trade and oil prices - on which they were based.

Retrospective Analysis

6. Our system is not yet working on the continuing basis which I believe to be necessary. We ought surely to envisage for the future that, at each annual (or more frequent) review, our forecasts/projections for the coming period are accompanied by a review of the latest developments by comparison with what was forecast/projected a year previously. I would want to look to the Fund staff to do this review in the first instance. We could perhaps agree now on the framework for use next year.

Indicators for the G7 as a whole

7. Agreements on compatible policies between members of the group, however successful, cannot provide any assurance that financial developments in the G7 as a whole will be appropriate. The Chancellor, in his speech to the Annual Meetings in September said that:

> "We must ensure that there is no persistent inflationary (or for that matter deflationary) bias for the group as a whole. This can be helped by:
>
> - the development of indicators for the group as a whole; these will be mainly financial but special attention should also be given to the trend of world commodity prices;
>
> - a nominal framework for policy, in terms either of a path for GDP growth for the group as a whole, or one for the average inflation rate; and
>
> - a medium term perspective when setting out the path and in gauging actual performance. We should not become involved in an exercise in short term fine tuning.
>
> In recent meetings we have put a lot of effort into developing performance indicators for individual countries. I have to say that I have considerable doubts whether we can usefully take that exercise much further. I believe it would be far more useful to devote our efforts to monitoring the performance of the group as a whole, so that we can ensure that we maintain the correct non-inflationary policy stance."

8. I would add that, if we can achieve a better judgment of the right stance for the G7 as a whole, this could well help us greatly to identify the direction of necessary changes of policies by individual members of the group, and thus to support the aim of exchange rate stability.

9. For some of the 'global indicators', attention should focus on the latest actuals as a means of assessing the current position of the world economy (e.g commodity prices, nominal and real interest rates, industrial production etc). For others forecasts and projections would be appropriate (as for the national indictors).

10. A consistent set of projections for **G7 countries as a whole** can really be sensibly attempted only by the IMF staff. I think we should ask them to produce a single summary table bringing together data, at the level of G7 as a whole, on all the indicators.

11. As just one example of how it could be instructive to look at the overall picture, in addition to that for individual countries, I draw attention to the **average** level of nominal and real interest rates for our group. Table E in the Fund staff's paper of 2 December records, for the past 3-4 years, the levels of short term interest rates in each of our countries. It is helpful to look in addition at the G7 average. The following figures are weighted by GDP:

	Short term interest rates	
	<u>**nominal**</u>	<u>**real**</u>
1984 average	9.6	4.9
1985 average	8.5	4.4
1986 average	7.0	5.0
1987 average	6.7	4.0
1987 October 12	7.7	4.3
1988 January 18	6.5	3.2

12. Considerable care is of course needed in interpreting **real** interest rates: inflation expectations are not usually the same as recent recorded levels of inflation; oil price shocks can have a once for all effect on the price level, and so on. But the table brings out that the average level of real interest rates, defined as the nominal rate minus the CPI increase for the same (or latest) period, is now clearly lower than the average level in each of the last few years.

Commodity prices

13. Both the US and UK speeches to the Annual Meetings in September referred to the desirability of making greater use of commodity prices as indicators. The Fund staff will be taking forward their work and I hope we can draw on their results. Of course, interpretation is never easy and we shall continue to exercise judgment in this area. No single indicator or group of indicators will ever be an infallible guide.

14. I would like to offer a practical illustration of the use of commodity price indices. Consider the following series, from the Economist, of a basket of commodity prices (excluding oil) compiled from spot quotations:

1980 = 100

	SDR	$
1984	106	83
1985	96	75
1986	87	78
1987	89	88
October 13	93	93
November 3	91	94
December 22	98	105
1988		
January 12	99	105

15. The recovery in commodity prices from very low levels in late 1986 was briefly interrupted by the sharp falls in stock markets in October. But by late December 1987 and January 1988, commodity prices were over 20 per cent (in SDR terms, and over 40 per cent in dollar terms) above the low points in 1986.

16. This behaviour of commodity prices is consistent with the marked strengthening in industrial production that took place in many of our countries in the Summer and Autumn of 1987; and is part of the evidence for judging the strength of activity and inflation in the near future.

Conclusion

17. In recent meetings we had prolonged debate about the choice of indicators for individual countries as a basis for discussion. Looking at these indicators can certainly help in assessing domestic policies and performance. But the indicators exercise was not intended to develop into fine tuning, nor to become a trigger for automatic action or consultation. A large element of judgment and flexibility, together with information that goes much wider than any particular set of indicators, is bound to be involved in arriving at policy conclusions and commitments on exchange rates and economic policies. Part of this wider context is the overall position of the G7. Part is the need for an understanding of the dynamic development of our economies from year to year. This is why I have highlighted these two points.

J G LITTLER

H M TREASURY
LONDON

20 JANUARY 1988

014/2765

CONFIDENTIAL

FROM: JILL RUTTER
21 January 1987

PRINCIPAL PRIVATE SECRETARY

CHANCELLOR'S MEETING WITH THE PRIME MINISTER

The Chief Secretary spoke to the Chancellor about the general concern he faced at the moment about colleagues readiness to pitch in for additional spending regardless of the consequences for good financial control. He asked me to let you have the attached short note that the Chancellor might wish to use in the discussion with the Prime Minister.

Thanks. On the pressure of spending [illegible] raised at Cabinet [illegible] flagged. [illegible] a Speech. time [illegible] Stand [illegible] Arthur but [illegible] Also

Jill Rutter

JILL RUTTER
Private Secretary

5/2765

Last week's reception for Public Expenditure White Paper showed that press and other commentators were sceptical about the credibility of the Government's spending plans. They point to the smaller Reserve in 1987-88 and to the small planned growth between 1987-88 and 1988-89. The Chief Secretary was specifically asked whether colleagues were seeking already to renegotiate PES.

Therefore vital to credibility of numbers that we are <u>not</u> seen to be making adjustments to those numbers before the next financial year even starts. So far the Chief Secretary has agreed 2 additions. £40 million for local authority current expenditure - in effect forced on us by the need to impose rate caps by formula, and £1 million for AIDS research.

But evidence of bids coming in. At H yesterday the Chief Secretary in a minority of one in opposing a proposal to spend £1 million on surveys for RADON in housing, as opposed to asking housebuilders who could afford to pay to meet the costs. In the subsequent discussion on student grants the Paymaster General suggested that an addition of £5 million in 1987-88 (£8 million in a full year) should be made to avoid taking a decision between keeping the student grant level in real terms and slightly increasing the parental contribution, and maintaining the parental contribution but cutting the student grant by 1¼ per cent in real terms (note below). The conclusions of that H meeting - with the Paymaster General's dissent - will be reported to the Prime Minister.

Other problems on the horizon which could give the impression that the Government has lost its will to control public expenditure. In some areas we knew the likelihood at the time of the Survey, but it was not right to make provision. The figures for the restructuring of <u>academic pay</u> - £40/£56/£71 million respectively are likely to emerge soon. Allowance has been made for these, but they are not public knowledge. [Similarly Mr Walker has been guaranteed access to the Reserve for a go-ahead on Sizewell].

Mr Luce will be making an announcement on the completion of Stage I for the British Library involving expenditure not included in PES plans. But is also seeking words of comfort to the arts lobby (i.e. assurance of more spending) for the later Survey years. Mr Fowler is receiving initiatives on breast cancer screening and hepatitis B dropped during the Survey to be financed from switches from non-cash limited programmes. There are bids from DTI e.g. BNSC which has been discussed in E(A). There are still no proposals at Ministerial level on launch aid.

Changes now will emerge in a dribble of announcements but will emerge for closer scrutiny at the time of the Budget when the Estimates are compared with the provision in the Public Expenditure White Paper plans. Commentators and markets perceive is tight in 1987-88 and tighter still in 1988-89. Treasury also aware that the position is very tight. Despite the general optimism on the economy tax objectives will not be achieved without firm control of public expenditure.

There are already accusations of cynical pre-election bribes. That will build up if a welter of new expenditure initiatives are announced. More damaging still would be if we actually have to envisage cuts in 1988-89. The Opposition are already claiming that there will be cuts as soon as the Government is returned. We must not give credibility to notion that we are to fight the election on a false prospectus.

Student Grants

Public expenditure determined by two elements:

(a) level of the student grant;

(b) amount of the parental contribution.

PES provision consistent with full uprating of parental contribution in line with average earnings (7½ %) - and 2½% increase in level of grant.

Mr Baker proposed to H that he should increase student grants by 3¾% to keep them level in real terms but hold to the PES provision by raising the lowest contribution from £20 to £40 and only increasing the parental scale by 6¾%.

Mr Clarke suggested at H that it would be better to avoid making the choice - i.e. uprate grants by 3¾ %, the contribution scale by 7½% and find another £5 million (£8 million in a full year) - with knock-ons in subsequent years. Anyone with a pay increase of less than 6¾% would be paying a lower proportion of the grant (Mr Baker said no real increase in contribution for anyone whose income has not gone up more than the RPI).

Prime Minister's initial reaction in December was to favour 2½%/7½%. Chief Secretary fears more difficult to defend not uprating grant in real terms than the more obscure difference between 6¾% and 7½% for the earnings uprating.

PUBLIC EXPENDITURE – POTENTIAL INCREASES ABOVE PEWP

£m

	1987–88	1988–89	1989–90
Agreed since Survey			
AIDS	1	1	1
LA current	40	–	–
Known about during Survey			
British Library	4	6	9
Academic Pay	40	56	71
Sizewell	105	40	–
Other likely specific bids [maximum]			
Health	(Mr Fowler claims he will offset but from non-cash-ltd programmes)		
Radon	1	–	–
Student grants	5	8	8
Space	75	125	170
Launch aid	50	100	150
EMS realignment ~~/green devaluation~~	19	9	9
Green devaluation	110	100	100
Coal (redundancy pay)	60	5	5

1. Adler
2 plus

PERSONAL & CONFIDENTIAL

FROM: SIR T BURNS
DATE: 22 JANUARY 1987

Thanks: 2. Relevant to Thursday speech/launch

CHANCELLOR

cc Sir P Middleton
Mr Monck
Mr Sedgwick
Miss O'Mara

JANUARY CBI QUARTERLY TRENDS SURVEY

I spoke to John Caff this afternoon in confidence about the next CBI Industrial Trends Survey, which is due to be published next Tuesday at 3.30 pm (a little later than the normal release time of 11.30 am).

2. I have added the figures he gave me to the table from the October Trends Survey.

3. The basic message is of a strengthening of optimism both at home and regarding export prospects. The volume of new orders has also improved. At the same time there is a further increase in the balance of firms planning to increase domestic and export prices. However there are one or two quirks in the responses; an unchanged level of capacity utilisation and a reduction of the number of firms with output limited by a shortage of skilled labour.

4. I also attach:

- the table supplied by EB in October, showing seasonally adjusted figures for the series used in the CSO's leading indicators. I have updated this using the same seasonal factors as applied last January, which should be broadly unchanged;

- the table which was supplied to me in December by the CSO showing actual and seasonally adjusted figures for order books, prices and output. Again I have updated the table using the same seasonal adjustment factors that applied last January.

5. These additional tables reinforce the basic message that there has been a further strengthening of output and orders with the prospect of slightly higher inflation.

6. John Caff said that the CBI's interpretation of these figures was as follows:

- they confirmed the pick-up in output. By the first quarter of 1987 they expect output to be 2.3 per cent higher than a year earlier and that we were on course for 3 per cent growth for the year as a whole;

- manufacturing employment would continue to fall at a rate of 7-8 thousand a month;

- producer price inflation would show little change over the next four months but by April might be up to 4.5 per cent;

- investment in the first three quarters of this year would be up 4 per cent.

7. In discussion at the Economic Situation Committee today a number of points were raised:

- the prospects for 1987 were good even though the media may have been over-playing this in recent days; ! (Mr Cat word)

- firms continued to face a tough competitive situation in the home market which would limit the increase in prices, but they were expecting to increase margins on exports;

- despite the answers to the question on capacity the general view was that there had been some increase in capacity utilisation;

- the pick-up in the growth of output was having a beneficial effect on costs per unit of output;

- they thought the apparent reduction in skilled labour shortages was almost entirely a feature of the electronics industry, and in non-electronics the pressures on skilled labour were as great as before.

T BURNS

ENCS

Table 1 a)

CBI INDUSTRIAL TRENDS SURVEY: SUMMARY OF RESULTS FROM JULY 1985 TO OCTOBER 1986

(All figures are percentage balances * except where otherwise stated)

TOTAL TRADE		Jul 85	Oct 85	Jan 86	Apr 86	July 86	Oct 86	Jan 87
1 Optimism re business situation		0	- 6	- 1	+ 8	- 9	0	+12
3 12 month forecast of capital expenditure authorisations compared with previous 12 months on:								
a buildings		-21	-21	-16	-15	-15	-13	-10
b plant and machinery		0	+ 4	+ 2	+10	+ 5	+ 8	+10
4 Firms working below capacity[1]		45	49	54	57	48	49	50
6 Numbers employed	- past 4 months	-15	- 6	-16	-17	-20	-17	-16
	- next 4 months	-16	-10	-14	-14	-21	-19	-9
7 Volume of new orders	- past 4 months	+10	+11	- 2	0	- 6	0	+14
	- next 4 months	+15	+13	+ 9	+16	+ 4	+18	+20
8 Volume of output	- past 4 months	+18	+10	+ 6	0	- 2	- 1	+9
	- next 4 months	+14	+17	+ 4	+14	+ 5	+13	+15
10a Stocks of raw materials	- past 4 months	+ 1	+ 1	- 1	- 5	- 7	- 4	-8
	- next 4 months	- 8	-12	-13	-12	-17	-19	-6
b Stocks of work in progress	- past 4 months	+ 7	+ 8	- 2	0	- 8	- 2	-8
	- next 4 months	- 6	- 7	- 9	- 8	-13	-12	-5
c Stocks of finished goods	- past 4 months	+ 4	0	- 3	- 3	- 2	- 7	-6
	- next 4 months	- 8	- 8	-15	-10	-16	-14	-5
11 Average unit costs	- past 4 months	+30	+19	+23	+19	+11	+ 6	+15
	- next 4 months	+28	+21	+34	+18	+ 8	+11	+29
12a Average domestic prices	- past 4 months	+23	+13	+ 8	+20	+ 6	+ 3	+13
	- next 4 months	+23	+17	+25	+19	+11	+14	+30
14 Four month forecast of factors likely to limit output[1]								
Orders or sales		73	79	83	81	81	75	82
Skilled labour		15	15	10	13	12	12	9
Other labour		2	1	1	1	1	1	1
Plant capacity		15	17	13	13	14	13	15
Credit or finance		4	4	4	8	4	4	3
Materials/components		7	4	5	3	7	6	5
Other		3	1	1	2	3	3	2

Table 1b

EXPORT TRADE		Jul 85	Oct 85	Jan 86	Apr 86	July 86	Oct 86	
2 Optimism re export prospects		+ 2	- 7	0	+12	-10	+11	+20
7b Volume of new export orders	- past 4 months	+ 7	0	- 6	- 1	-10	-11	+7
	- next 4 months	+ 9	+ 6	+ 7	+17	- 3	+15	+21
9b Volume of export deliveries	- past 4 months	+17	+ 1	+ 3	+ 5	- 7	- 5	+7
	- next 4 months	+14	+10	+ 4	+20	- 1	+11	+21
12b Average export prices	- past 4 months	+12	- 1	1	+ 9	- 3	0	+9
	- next 4 months	+11	+ 7	+21	+11	- 1	+20	+29
15 Four month forecast of factors likely to limit export orders[1]								
Prices		66	71	70	65	60	61	61
Delivery dates		11	11	11	10	8	13	13
Credit or finance		10	8	10	11	9	12	9
Quota and licence		15	10	11	11	11	13	11
Political/economic conditions abroad		27	29	25	30	31	29	26
Other		7	7	10	9	11	11	10

1 Percentage Figures

CBI Monthly Trends Enquiry: Time Series of results from November 1985 to October 1986

In the intervening months between the main quarterly Industrial Trends Surveys the CBI carries out a much abbreviated monthly Trends Enquiry. In the latter participants are only asked to answer five questions. These five questions are also included in the main quarterly Survey and the table below sets out the time series of results for the past year.

		Nov	Dec	Jan	Feb	Mar	Apr	May	Jun	Jul	Aug	Sep	Oct	
1a Total Order Book	(Q.5a)*	- 5	- 7	-19	- 9	-10	-24	-16	-21	-25	-20	-21	-23	-15
1b Export Order Book	(Q.5b)	- 5	-12	-19	-10	- 7	-20	- 9	-19	-25	-25	-23	-22	-13
2 Stocks	(Q.5c)	+13	+12	+16	+13	+11	+15	+14	+18	+16	+15	+12	+10	+10
3 Volume of Output	(Q.8)	+12	+18	+ 4	+23	+13	+14	+14	+10	+ 5	+ 7	+11	+13	+15
4 Average Prices	(Q.12a)	+15	+22	+25	+20	+19	+19	+14	+ 6	+11	+10	+10	+14	+30

* question number in quarterly survey

* The 'balance' is the difference between those replying 'more', 'up', 'above normal' or 'more than adequate' and those replying 'less', 'down', 'below normal' or 'less than adequate'.

EDTRENDS1P

TABLE 1

RECENT TRENDS IN CBI SURVEY QUESTIONS

(CSO seasonally adjusted figures in brackets)

	Apr 85	July 85	Oct 85	Jan 86	April 86	July 86	October 1986	JAN 87	CSO leading indicator Component
Business Optimism	+18 (+3)	0 (+6)	-6 (+5)	-1 (-2)	+8 (-8)	-9 (-3)	0 (+11)	+12 (+11)	Longer
Changes in new orders past 4 months	+24 (+14)	+10 (+11)	+11 (+19)	-2 (-1)	0 (-10)	-6 (-5)	0 (8)	+14 (+15)	Shorter
Expected changes in stocks of raw materials next four months	+1 (-4)	-8 (-8)	-12 (-9)	-13 (-12)	-12 (-17)	-17 (-17)	-19 (-16)	-6 (-5)	Shorter
Firms working below capacity[1]	54	45	49	54	57	48	49	50	Coincident
Chance in stocks of[1] materials past 4 months	0	+1	+1	-1	-5	-7	-4	-8	Coincident
Expected volume of output in next four months	+27 (+21)	+14 (+16)	+17 (+19)	+4 (+6)	+14 (+7)	+5 (+7)	13 (15)	15 (17)	
Volume of output in past four months	+21 (+15)	+18 (+18)	+10 (+14)	+6 (+7)	0 (-5)	-2 (-2)	-1 (3)	9 (10)	

[1] No significant seasonal influences here.

TABLE 3A

CBI MONTHLY SURVEY QUESTIONS (OTHER THAN OUTPUT EXPECTATIONS)

	LEVEL OF ORDER BOOK (compared to normal)				PRICES - next 4 months	
	TOTAL		EXPORT			
	Reported	Seasonally Adjusted	Reported	Seasonally Adjusted	Reported	Seasonally Adjusted
1985						
Nov	-5	-5	-5	-3	15	17
Dec	-7	-9	-12	-12	22	17
1986						
Jan	-19	-13	-19	-15	25	18
Feb	-9	-11	-10	-13	20	14
Mar	-10	-14	-7	-14	19	15
Apr	-24	-21	-20	-21	19	16
May	-16	-21	-9	-16	14	15
June	-21	-24	-19	-22	6	12
July	-25	-23	-25	-23	11	15
Aug	-20	-21	-25	-21	10	15
Sept	-21	-21	-23	-19	10	16
Oct	-23	-17	-22	-16	14	15
Nov	-9	-10	-10	-8	19	21
Dec	-10	-12	-7	-7	26	21
JAN 87	-15	-9	-13	-9	30	23

NB
The monthly question concerning the adequacy of present stock levels is not found to display stable seasonality.

I SURVEY QUESTIONS ON OUTPUT: MONTHLY EXPECTATIONS & QUARTERLY OUTTURN

VOLUME OF OUTPUT

	PAST 4 MONTHS		NEXT 4 MONTHS	
	Reported	Seasonally Adjusted	Reported	Seasonally Adjusted
1985				
Oct	10	14	17	19
Nov			12	15
Dec			18	17
1986				
Jan	6	7	4	8
Feb			23	20
Mar			13	7
Apr	0	-5	14	9
May			14	12
June			10	9
July	-2	-2	5	10
Aug			7	10
Sept			11	14
Oct	-1	3	13	15
Nov			13	15
Dec			10	9
JAN 87	+9	10	15	19

NB

The results have been aligned against the month the survey was conducted and not the reference period. The July expectations questions is therefore predictor for October outturn.

CBI SURVEY QUESTIONS ON OUTPUT: MONTHLY EXPECTATIONS & QUARTERLY OUTTURN

VOLUME OF OUTPUT

	PAST 4 MONTHS		NEXT 4 MONTHS	
	Reported	Seasonally Adjusted	Reported	Seasonally Adjusted
1985				
Oct	10	14	17	19
Nov			12	15
Dec			18	17
1986				
Jan	6	7	4	8
Feb			23	20
Mar			13	7
Apr	0	-5	14	9
May			14	12
June			10	9
July	-2	-2	5	10
Aug			7	10
Sept			11	14
Oct	-1	3	13	15
Nov			13	15
Dec			10	9
JAN 87	+9	10	15	19

NB The results have been aligned against the month the survey was conducted and not the reference period. The July expectations questions is therefore predictor for October outturn.

023/2765

B/F 3/2

SECRET AND PERSONAL

NOT yet discussed *

FROM: JILL RUTTER
DATE: 22 January 1987

CHIEF SECRETARY TO THE TREASURY

PRINCIPAL PRIVATE SECRETARY

CL
meets next week?
AA

cc:
Sir Peter Middleton
Mr F E R Butler
Miss Peirson
Miss Noble
Mr Gibson

BF next CST bilateral

SOCIAL SECURITY MEDIUM TERM OPTIONS

The Chief Secretary has had a preliminary discussion of part of Miss Noble's paper with Mr F E R Butler, Miss Peirson, Miss Noble and Mr Gibson. Some points arose on it which the Chief Secretary would like to discuss with the Chancellor. This minute records those points and also records the areas where the Chief Secretary decided that further work needed to be done, or which were not worth pursuing.

PS/CST TO PPS 22/1

2 The Chief Secretary did not think there was any realistic prospect of abandoning the "pledge" on the retirement pension. But there are two issues on this on which he would like to talk to the Chancellor. First, in order to keep open the option of biennial upratings the Chief Secretary would like to discuss with the Chancellor a possible form of wording of any manifesto pledge on retirement pension. The Chief Secretary noted that Miss Noble's paper said that the Prime Minister had been persuaded before by Mr Fowler that the terms of the previous manifesto pledge implied annual upratings. The Chief Secretary would also like to discuss with the Chancellor the extent to which any pledge on the retirement pension needs to be applied to other benefits.

3 The Chief Secretary has asked Miss Noble to pursue the eligibility criteria for the state pension, and in particular to look at the possible ways of tightening up on credits awarded through the home responsibility protection to married women, (paragraph 12). The Chief Secretary did not see much attraction in offsetting occupational pension against the retirement pension - though Mr F E R Butler pointed out this could be justified much more easily

SECRET AND PERSONAL

if it could be proved that present NICs were actuarially insufficient to pay for the state pension. The Chief Secretary thinks it is important to drop the commitment to abolish the earnings rule and would like ~~hither~~to discuss this with the Chancellor. The Chief Secretary would also like to discuss how the idea of raising the retirement age for women might interact with other policy proposals emerging for the manifesto.

4 The Chief Secretary agreed that there was no mileage in trying to re-open SERPS (Paragraph 15).

5 The Chief Secretary was surprised to learn that the Christmas bonus is not just paid to pensioners but to all recipients of long-term benefits. The Chief Secretary believes the abolition of the Christmas bonus must be a runner. It is therefore necessary to avoid any manifesto commitment. He sees a major presentational difficulty as being the amount of credit the Government has claimed for continuing to pay this bonus. He would like to discuss this with the Chancellor.

6 It was agreed that widow's benefits were a ripe area for picking. The Chief Secretary asked Miss Noble to pursue vigorously. He did however rule out introducing an earnings rule for War Widows.

7 The Chief Secretary felt that there was also more to be squeezed from unemployment benefit and that this was an area where further tightening up would be politically attractive. He was anxious to tighten up on availability for work and asked Miss Noble to pursue this further looking particularly at married women who claimed unemployment benefit after a period of maternity pay, when they were not genuinely available for work. He has also asked Miss Noble to look at the extent to which availability for work testing in DE simply directs people off the count onto DHSS benefits.

8 That summarises the discussion on the paper so far. I will let you have a further note when we have completed deliberations.

SECRET AND PERSONAL

But I think some of these points are quite urgent and the Chief Secretary would welcome a discussion in the near future with the Chancellor on the points emerging, particularly those which are relevant to the manifesto.

Jill Rutter

JILL RUTTER
Private Secretary

0394C

PEm

SECRET

[redacted]

BANK OF ENGLAND
LONDON EC2R 8AH

A.L. Coleby
Assistant Director
01-601 4541

Copies sent 23/1.

23 January 1987

cc Sir T Burns
Mr Cassell
Mr Peretz
Mr Odling-Smee
Mr Lankester
Mr Grice
Mr J Carr
Mr Sedgwick
Mr Richardson
Mrs Lomax
Mr C Kelly
Prof B Griffiths No 10

Sir P Middleton KCB
H M Treasury
Parliament Street
London
SW1P 3AG

Dear Peter,

I enclose our regular monthly note on interest rates over the next few weeks for our meeting on Tuesday afternoon.

Yours ever,

Tony

Mon policy

95

2-3 old age

7-

4

ERM post Budget

JAS

Ex Rate

Funding

32

5/23/1

003/3291

SECRET AND PERSONAL

FROM: **JILL RUTTER**
DATE: **28 January 1987**

RUTTER TO PPS 28JAN

PRINCIPAL PRIVATE SECRETARY

NOTED. The next step is as minutes @ x.

cc:
Sir Peter Middleton
Mr F E R Butler
Miss Peirson
Miss Noble
Mr Gibson

SOCIAL SECURITY MEDIUM TERM OPTIONS

This minute records the outcome of the Chief Secretary's reconvened meeting with Mr F E R Butler, Miss Peirson, and Miss Noble and Mr Gibson to discuss Miss Noble's paper on Social Security Medium Term Options. You will recall that the story so far ended with unemployment benefit (paragraph 18).

Invalidity benefit (paragraph 19)

2 It was argued that there was a distinction between offsetting occupational pensions against invalidity benefit and offsetting occupational pensions against the retirement pension. The retirement pension was something which most people expected to receive. Invalidity benefit was, although a national insurance benefit, more in ~~the~~ way of ~~a~~ safety net benefit. It seemed more reasonable therefore to take account of the private provision which an individual had available. It was agreed that this was an option which should be pursued.

Industrial injuries (paragraph 20)

3 Miss Noble recalled the difficulties which had arisen when this was looked at at the tail-end of the Social Security Review, and DHSS had been forced to redefine the disabilities that it applied to at the last minute. The Chief Secretary asked about the scope for private provision. Employers should be covered by insurance and that should reduce the call on Social Security. It was agreed that this was ~~at~~ another area which should be reviewed, given the substantial amount of spending.

Disablement benefits (Paragraphs 21-23)

4 It was agreed that a list of possible options for reining in the growth in disablement benefits should be drawn up. Miss Noble said that DHSS were likely to be forming ideas for a Green Paper to be launched once the first results of the survey of the disabled came available. It would be legitimate for the Treasury to ask DHSS what options they were identifying and to look at others. That review should not exclude the possibility of means testing disablement benefits. There was considerable evidence that benefits were very badly targetted at present. The position would be exacerbated if the DHSS lost the attendance allowance case currently before the court of appeal.

Means tested benefits (Paragraphs 24-29)

5 The Chief Secretary said that given the unpalatable options that needed to be contemplated in other areas he was most anxious to tighten up on undeserving claimants. The Chief Secretary asked Miss Noble and Mr Gibson to look at the rigour of the availability for work tests. He also asked for figures about the number of claimants who had their benefits suspended each year and for a note on the penalties for fraud. Mr Butler thought that more effort should be devoted towards tackling fraud. He was worried that the present culture in DHSS remained that of handing out benefits rather than ensuring that benefits only went to those who were eligible.

6 The Chief Secretary said that he was also concerned to identify areas where benefits were being claimed legitimately but where the rationale of providing those benefits should be questioned. One area identified was the provision of unemployment benefit to those who retired early. It was noted that this option had been paraded during the 1986 Survey but had not been pursued then. This should be pursued again. The Chief Secretary noted that he would not be attracted toward the ceiling approach on benefit which was being suggested by some for large families.

Family credit (Paragraph 30)

7 The key question here was the rate at which family credit would be paid when introduced in April 1988. Miss Noble warned

of a potential risk that work commissioned by No 10 on the unemployment trap could actually lead to the conclusion that there should be more clear water between benefits out of work and wages in work. Since there was little scope for reducing benefits further, it was likely that this might lead to pressure for an increase in the rate of family credit. Lord Young was known to be particularly concerned about having a gap of at least £20 a week between in and out of work payments.

Housing benefit

8 The Chief Secretary explained his concern about the potential abuse of the housing benefit system where four young people could effectively have a house paid for by the DHSS although they were living within proximity of their parents. Miss Peirson pointed out however that imposing a locality constraint would simply drive even more young people to London. Miss Noble promised a paper on housing benefit in the context of Mr Major's recent letter. She noted that further work done by LG suggested that it might be possible to resurrect the reduction in housing benefit subsidy paid directly to local authorities originally proposed in the DHSS Green Paper, which had been dropped because of the unacceptable distributional implications.

Child benefit (Paragraph 34)

9 The Chief Secretary noted that this was an area where it was vital to avoid any manifesto pledge to maintain the real value.

The future

10 Mr F E R Butler asked if a note could be produced setting out the effect of increases in tax thresholds or reductions in tax rates on social security spending since the move to the calculation of benefit entitlement on a net income basis meant that tax reductions would feed through into benefit payments. Miss Noble agreed to ask ET to do the necessary work. This would obviously only apply from the introduction of the new benefit structure in April 1988.

Conclusions

11 The Chief Secretary noted that it would be important to block any new loopholes that the pressure groups could identify.

He would welcome a discussion with the Chancellor on the range of issues identified in the paper. Miss Noble has agreed to provide an agenda. 1X

Jill Rutter

JILL RUTTER

MR 9/24

CONFIDENTIAL

pup

FROM: A C S ALLAN
DATE: 26 January 1987

MR KERLEY

cc: Mr Culpin / Mr S J Davies
Miss O'Mara
Mr Hacche

INDEX OF OUTPUT OF THE PRODUCTION INDUSTRIES - NOVEMBER 1987

The Chancellor was grateful for your minute of 21 January.

ACSA

A C S ALLAN

CONFIDENTIAL

FROM: R D KERLEY
DATE: 21 JANUARY 1987

MOM 21/1

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

cc Mr Culpin
Mr S J Davies
Mr Hacche
HB/02

INDEX OF OUTPUT OF THE PRODUCTION INDUSTRIES - NOVEMBER 1987

You asked (Mr Allan's minute of 20 January) how the latest figure for the fall in manufacturing output since 1979H1 compares with the fall under Labour, and also when we expect manufacturing output to return to the 1979H1 level.

2. Under the period of the Labour Government (1974H1-1979H1) manufacturing output fell by 2.5 per cent (as against 3.9 per cent since 1979H1). On your second point, I understand from EA1 that we currently expect manufacturing output to return to the 1979H1 level during 1988H1.

R. Kerley

R D KERLEY

Ch

I have asked MOM to follow up Mr Hattersley's point yesterday about UK performance on manufacturing output relative to other countries.

AA

RA3.28

RESTRICTED

Rup

FROM: A C S ALLAN

DATE: 20 January 1987

MR KERLEY

cc Mr Culpin
Mr S J Davies
Miss O'Mara

INDEX OF OUTPUT OF THE PRODUCTION INDUSTRIES - NOVEMBER 1987

The Chancellor was grateful for your minute of 16 January.

2. He would be grateful for information about how the latest figures for manufacturing (a 3.9 per cent fall over the latest three months on 1979H1) compare with the fall under Labour. And when do we expect to return to the 1979H1 level?

ACSA

A C S ALLAN

8:2/4/3

PERSONAL AND CONFIDENTIAL
until 11.30am 19 January 1987
then RESTRICTED

FROM: R D KERLEY
DATE: 16 JANUARY 1987

1. **~~MISS~~ O'MARA**

2. **CHANCELLOR OF THE EXCHEQUER**

The latest figures give further confirmation of the pick-up in manufacturing output. They may be worth a passing reference in Thursday's debate.

MOM 16/1

Thanks. How does this compare with the fall we lost? 2. When do we expect to return to the 1979 H1 level?

cc Chief Secretary, Financial Secretary, Economic Secretary, Minister of State, Sir Peter Middleton, Sir Terence Burns, Mr Cassell, Mr Monck, Mr Burgner, Mr Scholar, Mr Sedgwick, Mr Gray, Mr Culpin, Mr Davies, Mr Pickford, Mr Naisbitt, Mr Dyer (+1 for No 10), Mr Cropper, Mr Ross Goobey, Mr Tyrie, Mr Stirling - CSO, Mr Kingaby - CSO, Mr Lang - CSO, HB/02

INDEX OF OUTPUT OF THE PRODUCTION INDUSTRIES - NOVEMBER 1987

This will be published at 11.30am on Monday, 19 January.

2. The index of production rose by 0.7 per cent in the three months to November compared with the previous three months, and by 0.9 per cent compared with the same period a year earlier.

3. Manufacturing output rose by 1.4 per cent in the three months to November compared with the previous three months, and by 1.9 per cent compared with the same period a year earlier.

4. **Recent movements**

percentage changes	Latest 3 months on previous 3 months	Latest 3 months on same period a year earlier	November on October	Latest 3 months on 1983Q2	Latest 3 months on 1981Q1 trough	Latest 3 months on 1979H1
Index of Production	+0.7	+0.9	+0.2	+9.8	+15.9	+3.1
within which:						
Manufacturing	+1.4	+1.9	+0.1	+10.8	+13.9	-3.9
Energy and Water	-0.9	-1.2	+0.2	+7.7	+21.1	+24.6

5. The CSO's assessment is that manufacturing output reached at least a temporary peak in 1985Q2 and then declined 1½ per cent by 1986Q1. Since then, however, output has more than recovered, and in the three months to November was 1 per cent higher than in 1985Q2. Whilst the figures for the three months to November of a 1½ per cent increase on the previous three months probably overstate the underlying rate of growth, it is clear that manufacturing is experiencing a period of healthy growth.

6. Energy sector trends are proving difficult to analyse, with short term movements in oil extraction caused by maintenance work, and a pipeline leak at the end of November. However, the underlying output of the energy sector appears, at best, to be flat.

7. The underlying output of all production industries in 1985H2 was 1 per cent below the level reached in the first half of that year, but partially recovered in the first half of 1986. Since then the output of production industries has continued to increase, reflecting the improvement in manufacturing output.

Lines to take

8.

(i) Total production up 1 per cent in three months to November compared with same period a year earlier.

(ii) Continued pick-up in manufacturing output. Up 1½ per cent in three months to November compared with previous 3 months and up 3 per cent since beginning of year.

R. Kerley

R D KERLEY

2

PERSONAL AND CONFIDENTIAL UNTIL 11.30 AM ON 19 JANUARY 1987

MR D NORGROVE
Prime Minister's Office

INDEX OF OUTPUT OF THE PRODUCTION INDUSTRIES - NOVEMBER 1986

The provisional index of the output of the production industries for November 1986 will be published at 11.30 am on Monday 19 January. A copy of the Press Notice is attached.

Latest figures

The November 1986 index of the output of the production industries - energy (including coal) and manufacturing - is provisionally estimated at 110.0 (1980=100, seasonally adjusted), little changed from October. For manufacturing the index was 105.7, little changed from October (see also paragraph on bias adjustment below).

In the three months to November 1986 the output of production industries was $^1/_2$ per cent higher than in the previous three months, with manufacturing output $1^1/_2$ per cent higher. Some industry detail is given in the attached Table A.

Assessment

Manufacturing output reached a temporary peak in the second quarter of 1985 and then declined $1^1/_2$ per cent by the first quarter of 1986. However, since the first quarter, output has more than recovered, and in the three months to November was 1 per cent higher than the second quarter of 1985. Also, in the three months to November, output was $1^1/_2$ per cent higher than in the previous three months, but this probably overstates the underlying rate of growth.

Trends in the energy sector are difficult to determine, particularly due to short-term movements in oil extraction caused by seasonal maintenance work and, at the end of November, by reduced production due to a pipeline leak. However the output of the energy sector appears, at best, to be flat.

The underlying output of all production industries in the second half of 1985 was 1 per cent below the level reached in the first half, but partially recovered in the first half of 1986. Since then, the output of production industries has continued to increase, reflecting the improvement in manufacturing output.

Bias adjustment for manufacturing output

In line with revised procedures introduced in January last year, figures of manufacturing output for the last six months include adjustments to try to allow for under-estimation in the provisional estimates (see Note 10 of Notes to Editors of Press Notice).

Figures for December 1986

Figures for December 1986 are scheduled for publication on Monday 16 February.

SK

S D Kingaby
16 January 1987

Central Statistical Office

Table A

Copy No.

++ PERSONAL AND CONFIDENTIAL until release of Press Notice at 11.30 am on January 19 1987 and thereafter unclassified ++

Index of output of the production industries 1980=100

SUMMARY		Total production industries	Energy and water supply	Total manufacturing industries	Metals	Other minerals and mineral products	Chemicals and man-made fibres	Engineering and allied industries	Food, drink and tobacco	Textiles, footwear, clothing and leather	Other manufacturing
1984		103.2	110.1	100.7	108.2	95.0	113.9	99.3	102.0	97.9	97.7
1985		108.2	120.1	103.9	115.0	94.3	119.1	104.1	101.1	101.7	98.8
1985	2	109.0	121.9	104.4	117.7	94.5	120.8	105.7	100.0	101.6	97.5
	3	108.3	120.9	103.8	116.2	94.2	118.7	103.5	100.8	102.9	100.0
	4	108.5	121.9	103.6	114.0	96.2	116.7	103.2	101.9	102.2	100.0
1986	1	109.4	127.6	102.8	111.3	92.7	118.3	101.9	101.2	103.2	99.8
	2	108.9	124.0	103.4	110.9	97.2	118.5	101.5	101.2	103.5	102.5
	3	110.6	126.7	104.9	107.5	97.7	121.0	103.0	104.3	101.9	104.8
1986	S	111.0	126.5	105.5	108	99	122	104	103	102	105
	U	109.8	121.6	105.6	115	98	122	104	103	101	105
	N	110.0	121.8	105.7	116	99	119	104	103	103	106
Percentage change latest 3 months on: previous 3 months		+0.7	-0.9	+1.4	+3.3	+1.0	+0.8	+2.3	-0.5	-0.4	+1.2
a year earlier		+0.9	-1.2	+1.9	-1.4	+2.8	+2.8	+0.9	+1.9	-0.7	+5.3
1st quarter 1981(a)		+15.9	+21.1	+13.9	+13.7	+10.7	+25.3	+16.0	+3.9	+11.9	+12.7
1st half 1979(b)		+3.1	+24.6	-3.9	-13.5	-8.5	+11.3	-5.1	+3.4	-14.9	-5.2

DETAILED ANALYSIS		Coal and coke	Extraction of mineral oil and natural gas	Mineral oil processing	Other energy and water supply	Metals	Other minerals and mineral products	Chemicals	Man-made fibres	Metal goods not elsewhere specified
1984		33.8	147.1	98.4	95.7	108.2	95.0	114.9	78.8	101.0
1985		67.2	150.3	98.7	105.9	115.0	94.3	120.4	74.2	99.1
1985	2	71.0	150.8	99.2	108.8	117.7	94.5	122.1	76.3	99.5
	3	80.3	146.1	98.6	107.8	116.2	94.2	120.0	75.5	99.9
	4	81.4	149.3	97.4	106.3	114.0	96.2	118.0	73.0	98.3
1986	1	79.5	155.6	95.3	115.9	111.3	92.7	119.6	74.7	95.6
	2	78.3	149.7	104.3	112.5	110.9	97.2	119.9	69.9	98.7
	3	77.0	159.3	101.4	108.2	107.5	97.7	122.6	66.2	96.3
1986	S	78	155	97	113	108	99	124	61	96
	O	79	151	95	105	115	98	123	64	97
	N	79	149	98	107	116	99	120	64	98
Percentage change latest 3 months on: previous 3 months		+2.1	-2.1	-5.8	+1.5	+3.3	+1.0	+1.0	-8.8	+1.9
a year earlier		-3.5	-2.2	-0.4	+1.7	-1.4	+2.8	+3.1	-14.9	-1.8
1st quarter 1981(a)		-19.1	+41.3	+0.3	+11.9	+13.7	+10.7	+26.8	-30.1	+9.6
1st half 1979(b)		-17.5	+60.8	-14.6	+3.3	-13.5	-8.5	+13.7	-54.2	-21.1

DETAILED ANALYSIS continued		Mechanical engineering	Electrical and instrument engineering	Motor vehicles and parts	Other transport equipment	Food	Drink and tobacco	Textiles	Clothing, footwear and leather	Paper, printing and publishing	All other manufacturing
1984		87.4	123.0	81.1	91.5	104.6	96.7	93.7	101.5	96.4	99.3
1985		92.9	130.9	86.3	94.6	104.1	95.0	98.3	104.7	98.1	99.7
1985	2	94.8	132.6	87.5	96.5	102.8	94.1	97.0	105.6	96.8	98.2
	3	91.7	129.1	88.6	93.5	104.4	93.6	99.7	105.6	98.5	101.6
	4	93.8	129.6	82.2	92.9	105.0	95.4	99.5	104.4	99.4	100.7
1986	1	93.3	127.0	80.8	94.3	104.3	94.6	98.7	107.1	99.2	100.6
	2	93.4	125.2	82.6	91.4	103.9	95.7	99.5	106.9	101.5	103.5
	3	93.7	130.6	80.8	93.1	108.2	96.2	97.7	105.6	102.9	107.0
1986	S	94	133	85	93	106	96	98	106	103	107
	O	93	133	85	92	107	97	98	104	102	108
	N	92	135	83	92	107	96	101	105	103	110
Percentage change latest 3 months on: previous 3 months		-0.5	+4.6	+5.5	-0.5	-0.5	-0.4	+0.4	-0.9	+0.2	+2.4
a year earlier		-0.1	+3.4	+1.0	-1.0	+2.5	+0.6	-1.0	-0.4	+3.7	+7.1
1st quarter 1981(a)		+6.3	+44.4	+9.9	-12.6	+8.4	-5.2	+9.3	+14.2	+8.2	+18.1
1st half 1979(b)		-15.7	+29.5	-31.4	-1.7	+7.2	-4.4	-20.7	-9.5	-3.9	-6.5

(a) Last trough for production industries (b) Last peak for production industries

Personal numbered copies of the minute and attachment to:

Treasury	(Principal Private Secretary (Sir Peter Middleton
Cabinet Office	(Mr Jack Hibbert
Department of Trade and Industry	(Private Secretary Secretary of State's Office
	(Private Secretary to Geoffrey Pattie
	(Private Secretary to Giles Shaw
	(Private Secretary to John Butcher
	(Sir Brian Hayes (Mr H H Liesner (Mr A Whiting (Mr N Harvey (Mr S W Treadgold
Bank of England	(Mr R Leigh-Pemberton

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CSO(87)6

19 January 1987

INDEX OF OUTPUT OF THE PRODUCTION INDUSTRIES - NOVEMBER 1986

Output of the production industries in the three months to November 1986 is provisionally estimated to have increased by ½ per cent from the level of the previous three months; manufacturing output rose by 1½ per cent.

Output of production industries (to November 1986)

The November index of the output of the production industries - energy (including coal) and manufacturing - is provisionally estimated at 110.0 (1980=100, seasonally adjusted). In the three months to November, production industries' output was ½ per cent higher than in the previous three months and 1 per cent higher than in the same period a year earlier.

Manufacturing output in the latest three months was 1½ per cent higher than in the previous three months and 2 per cent higher than in the same period a year earlier (see also note 10 of Notes to Editors). Within manufacturing, the output of the metals industry increased by 3 per cent and that of engineering and allied industries by 2 per cent between the two latest three-month periods; the output of other minerals, of chemicals and of the "other manufacturing" industries increased by 1 per cent. There was little change in the output of food, drink and tobacco, and of textiles and clothing.

Energy and water supply in the latest three months was 1 per cent lower than that in both the previous three months and in the same period a year earlier.

By market sector, the output of the investment goods industries increased by 1½ per cent between the two latest three-month periods, the output of the consumer goods industries by 1 per cent and the output of the intermediate goods industries by ½ per cent.

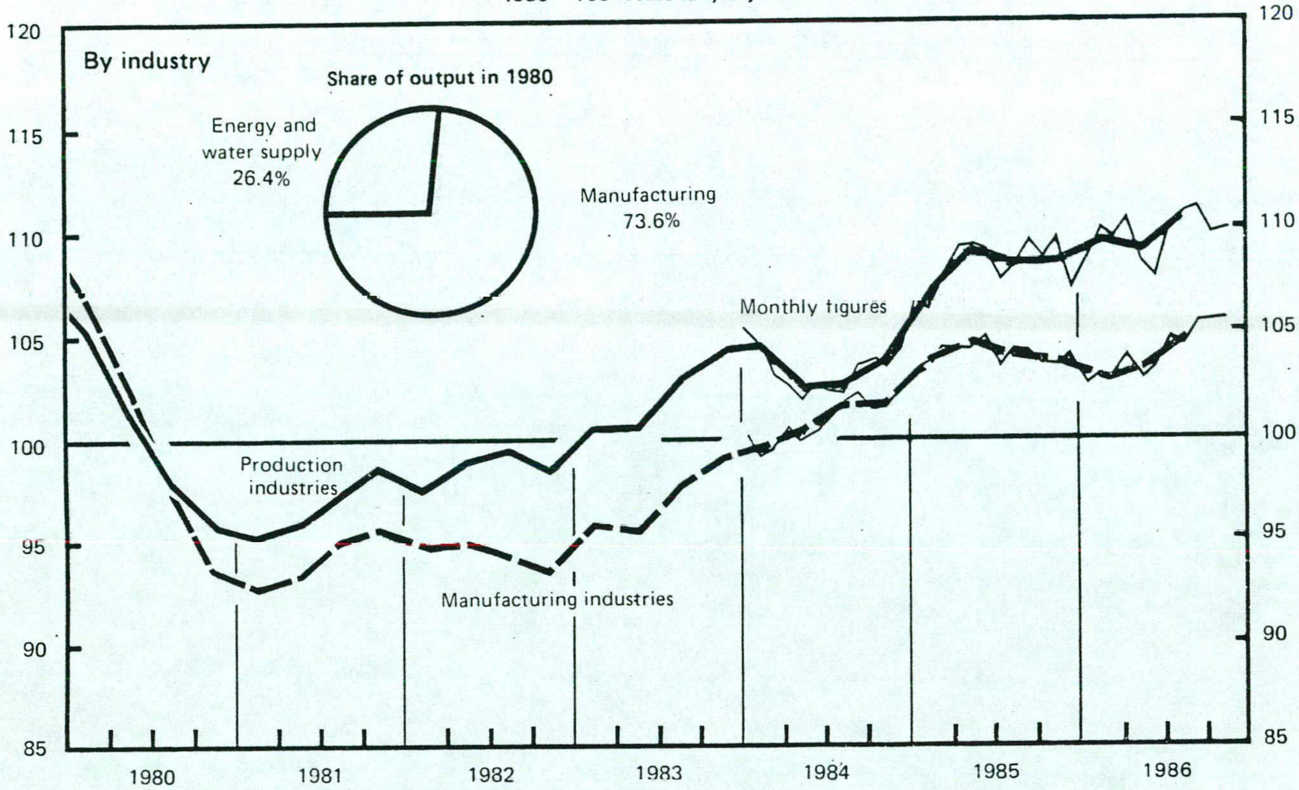
In the longer term, the output of the production industries in the three months to November was 16 per cent higher than at its trough in the first quarter of 1981; manufacturing output was 14 per cent higher.

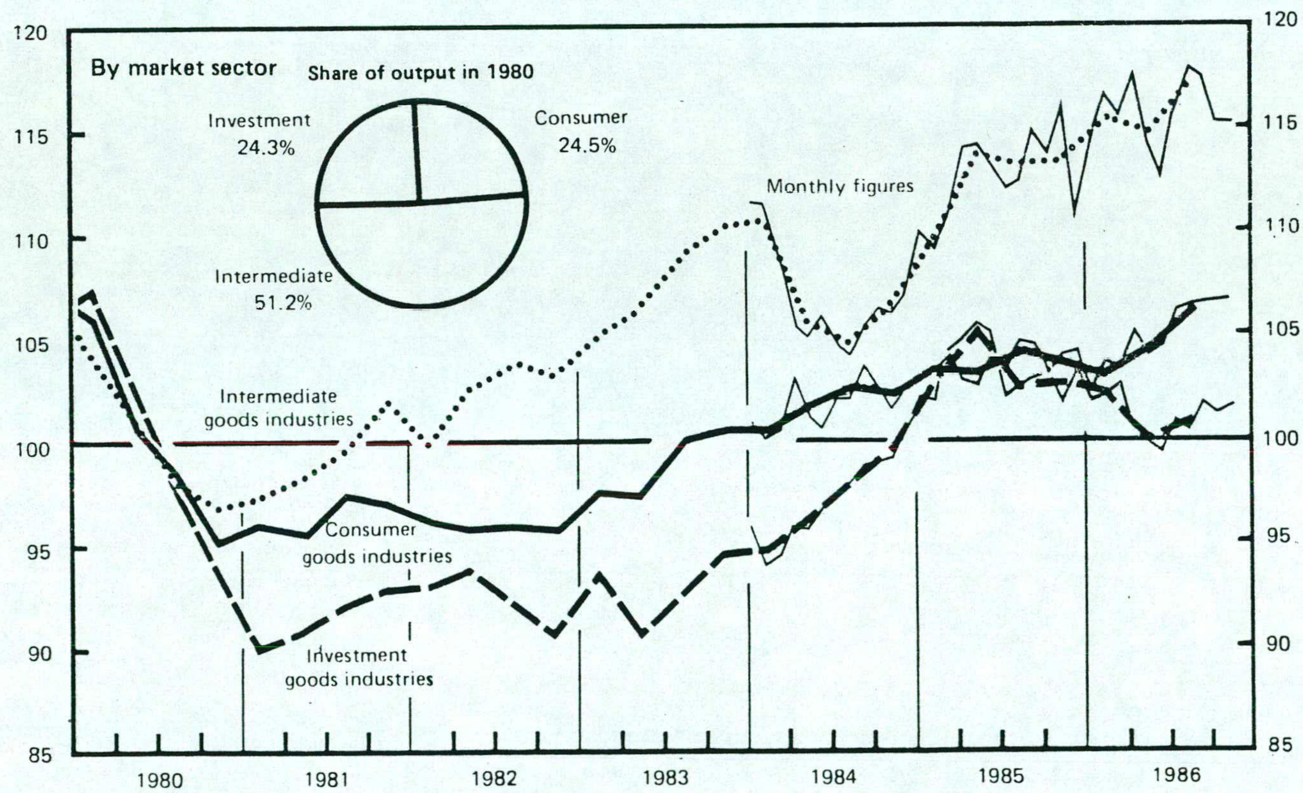
Output of production and construction industries (to Q3 1986)

Output of the construction industry in the third quarter of 1986 is estimated to have been nearly 3 per cent higher than in the previous quarter. Output of the production and construction industries in the third quarter was nearly 2 per cent higher than in the previous quarter, and nearly 16 per cent above the trough in the first quarter of 1981.

INDEX OF OUTPUT OF THE PRODUCTION INDUSTRIES

1980 = 100 Seasonally adjusted





OUTPUT OF THE PRODUCTION INDUSTRIES(1)

(1980=100)

TABLE 1

	Broad industry groups			Market sectors		
	Production industries Division 1-4	Energy Division 1	Manufacturing Division 2-4	Consumer goods	Investment goods	Intermediate goods
Weights	1000	264	736	245	243	512
1978	103.2	85.0	109.7	108.4	106.3	99.2
1979	107.1	100.5	109.5	108.3	104.7	107.9
1980	100.0	100.0	100.0	100.0	100.0	100.0
1981	96.6	103.8	94.0	96.4	91.3	99.2
1982	98.4	110.0	94.2	95.8	92.4	102.3
1983	101.9	115.9	96.9	98.8	92.9	107.6
1984	103.2	110.1	100.7	101.7	97.1	106.8
1985	108.2	120.1	103.9	103.6	103.3	112.6
Seasonally adjusted						
1980 1	105.2	100.5	106.8	105.9	107.2	104.1
2	101.3	98.4	102.3	100.6	101.9	101.3
3	97.8	98.8	97.5	98.5	97.4	97.8
4	95.7	102.2	93.4	94.9	93.4	96.8
1981 1	95.1	101.8	92.7	96.0	89.9	97.1
2	95.8	103.2	93.1	95.4	90.6	98.3
3	97.2	103.5	94.9	97.4	91.8	99.5
4	98.4	106.9	95.4	96.8	92.9	101.9
1982 1	97.2	104.3	94.7	96.1	92.9	99.8
2	98.8	109.7	94.9	95.7	93.7	102.8
3	99.2	113.2	94.1	95.9	92.2	103.7
4	98.4	112.9	93.2	95.6	90.8	103.0
1983 1	100.4	113.1	95.8	97.6	93.6	104.9
2	100.4	114.5	95.3	97.4	90.7	106.3
3	102.8	117.6	97.5	100.0	92.7	109.0
4	104.0	118.3	98.9	100.5	94.4	110.2
1984 1	104.2	117.3	99.5	100.5	94.7	110.4
2	102.3	108.1	100.2	101.6	96.2	105.6
3	102.5	105.4	101.5	102.5	97.9	104.8
4	103.8	109.6	101.7	102.1	99.5	106.5
1985 1	106.8	115.7	103.6	103.3	102.8	110.1
2	109.0	121.9	104.4	103.1	105.2	113.8
3	108.3	120.9	103.8	104.3	102.5	113.1
4	108.5	121.9	103.6	103.7	102.6	113.6
1986 1	109.4	127.6	102.8	103.2	102.2	115.6
2	108.9	124.0	103.4	104.5	99.9	114.9
3	110.6	126.7	104.9	106.4	100.9	117.2
1984 N	103.4	108.9	101.4	101.5	99.2	106.1
D	104.3	109.8	102.3	102.3	100.5	107.0
1985 J	106.6	115.9	103.2	103.0	102.2	110.1
F	106.1	114.0	103.3	103.1	102.0	109.2
M	107.7	117.3	104.2	103.9	104.2	111.0
A	109.0	122.2	104.3	102.8	104.8	114.0
M	109.2	123.0	104.2	102.6	105.6	114.1
J	108.9	120.5	104.8	103.9	105.3	113.3
J	107.5	118.8	103.4	103.4	102.0	112.0
A	108.1	119.2	104.1	104.8	102.5	112.4
S	109.4	124.6	104.0	104.6	102.9	114.8
O	108.6	122.7	103.5	103.0	103.1	113.8
N	109.7	127.0	103.5	104.0	101.6	116.3
D	107.1	116.1	103.9	104.2	103.1	110.6
1986 J	108.6	125.2	102.6	102.3	101.9	114.6
F	110.0	129.4	103.0	103.7	102.0	116.6
M	109.6	128.1	102.9	103.5	102.6	115.7
A	110.7	129.2	104.0	105.1	100.5	117.9
M	108.3	123.5	102.9	104.0	99.8	114.2
J	107.6	119.4	103.3	104.4	99.4	112.7
J	110.1	125.0	104.8	106.2	100.8	116.3
A	110.8	128.7	104.4	106.4	100.3	117.8
S	111.0	126.5	105.5	106.6	101.7	117.5
O	109.8	121.6	105.6	106.7	101.2	115.3
N	110.0	121.8	105.7	106.8	101.6	115.3
% 3-month on 3-month change (2)	+0.7	-0.9	+1.4	+1.0	+1.3	+0.4

(1) Output index numbers include adjustments, as necessary, to compensate for the use of sales indicators (see Notes to Editors).
(2) Average of September to November 1986 compared with the average of June to August 1986.

OUTPUT OF MANUFACTURING INDUSTRIES

(1980=100)

TABLE 2

	Metals	Other minerals and mineral products(1)	Chemicals and man-made fibres	Engineering and allied industries	Food, drink and tobacco	Textiles, clothing footwear and leather	Other manufacturing
	Class 21-22	Class 23-24	Class 25-26	Class 31-37	Class 41-42	Class 43-45	Class 46-49
Weights	25	41	68	325	99	52	126
1978	126.5	111.9	108.5	110.1	99.2	119.3	109.5
1979	131.8	111.0	111.3	107.6	100.7	117.9	111.9
1980	100.0	100.0	100.0	100.0	100.0	100.0	100.0
1981	106.0	89.0	99.6	91.8	98.3	92.7	93.2
1982	103.2	90.9	99.7	92.9	99.8	91.2	90.8
1983	104.7	93.9	107.4	94.9	100.9	94.7	93.7
1984	108.2	95.0	113.9	99.3	102.0	97.9	97.7
1985	115.0	94.3	119.1	104.1	101.1	101.7	98.8
Seasonally adjusted							
1980 1	81.6	109.9	111.6	108.0	101.4	108.9	108.8
2	116.3	104.4	101.7	102.4	99.9	103.0	100.6
3	104.8	95.7	93.2	97.5	99.5	97.2	97.1
4	97.3	89.9	93.5	92.0	99.3	90.8	93.6
1981 1	99.3	89.2	96.5	89.7	99.3	91.2	93.5
2	104.3	88.4	98.2	90.8	96.7	92.2	93.1
3	107.4	90.0	102.5	93.0	98.2	93.1	93.2
4	113.2	88.7	101.2	93.7	98.8	94.2	92.9
1982 1	110.3	89.8	99.9	93.7	98.9	92.0	91.0
2	108.3	91.7	99.7	93.6	100.1	91.3	91.3
3	100.3	91.2	99.6	92.6	100.7	91.4	90.8
4	93.8	91.0	99.5	91.8	100.6	90.3	90.2
1983 1	98.7	93.0	104.1	94.7	99.8	92.8	92.7
2	104.9	91.3	106.8	93.0	98.7	93.5	92.8
3	105.3	95.6	109.1	94.9	103.2	94.9	93.6
4	110.1	95.7	109.7	96.9	102.0	97.4	95.6
1984 1	112.1	94.1	111.4	97.3	101.9	96.8	97.1
2	105.0	95.1	112.2	98.3	102.5	97.5	98.2
3	108.5	96.2	116.1	100.5	102.3	98.4	97.4
4	107.2	94.8	115.9	101.0	101.4	98.9	98.2
1985 1	112.1	92.5	120.0	104.1	101.8	100.3	97.9
2	117.7	94.5	120.8	105.7	100.0	101.6	97.5
3	116.2	94.2	118.7	103.5	100.8	102.9	100.0
4	114.0	96.2	116.7	103.2	101.9	102.2	100.0
1986 1	111.3	92.7	118.3	101.9	101.2	103.2	99.8
2	110.9	97.2	118.5	101.5	101.2	103.5	102.5
3	107.5	97.7	121.0	103.0	104.3	101.9	104.8
1984 N	108	94	116	101	101	98	98
D	109	96	117	102	102	99	99
1985 J	110	92	120	104	102	99	98
F	110	91	120	104	102	100	98
M	116	94	120	105	102	102	98
A	116	94	122	105	100	101	97
M	118	94	119	106	100	101	97
J	119	95	122	106	100	103	98
J	116	94	119	103	101	102	100
A	118	93	118	104	101	104	100
S	114	95	119	104	101	103	100
O	114	97	117	103	102	101	100
N	116	96	117	102	101	104	101
D	113	96	116	104	103	101	100
1986 J	112	94	120	102	100	103	100
F	111	92	120	102	102	104	100
M	111	93	116	102	102	103	100
A	108	97	119	103	102	105	103
M	111	96	118	101	101	101	102
J	113	99	119	101	101	104	103
J	109	97	120	103	106	100	105
A	106	98	121	102	104	104	104
S	108	99	122	104	103	102	105
O	115	98	122	104	103	101	105
N	116	99	119	104	103	103	106
% 3-month on 3-month change (2)	+3.3	+1.0	+0.8	+2.3	-0.5	-0.4	+1.2

(1) Mainly building materials
(2) Average of September to November 1986 compared with the average of June to August 1986.

OUTPUT OF PRODUCTION AND CONSTRUCTION INDUSTRIES (1)

(1980=100)

TABLE 3

	Production and construction Division 1-5	Construction Division 5	Production industries Division 1-4	Energy Division 1	Manufacturing Division 2-4	Oil and gas extraction Class 13
Weights (parts per thousand of GDP(0))	424	63	361	95	266	44
1978	103.4	105.1	103.2	85.0	109.7	68.9
1979	106.9	105.8	107.1	100.5	109.5	98.7
1980	100.0	100.0	100.0	100.0	100.0	100.0
1981	95.6	89.9	96.6	103.8	94.0	110.3
1982	97.4	91.6	98.4	110.0	94.2	125.6
1983	100.9	95.3	101.9	115.9	96.9	137.6
1984	102.5	98.6	103.2	110.1	100.7	147.1
1985	106.9	99.8	108.2	120.1	103.9	150.3
Seasonally adjusted						
1979 1	104.1	101.0	104.6	97.0	107.4	89.6
2	108.9	107.2	109.3	101.0	112.3	99.3
3	107.3	107.7	107.2	104.0	108.3	106.0
4	107.5	107.2	107.4	100.0	110.1	99.9
1980 1	105.2	104.9	105.2	100.5	106.8	100.1
2	101.2	101.5	101.3	98.4	102.3	96.8
3	98.3	100.5	97.8	98.8	97.5	97.5
4	95.3	93.0	95.7	102.2	93.4	105.5
1981 1	94.8	92.4	95.1	101.8	92.7	107.4
2	94.8	89.5	95.8	103.2	93.1	107.8
3	96.3	90.9	97.2	103.5	94.9	110.7
4	96.7	86.9	98.4	106.9	95.4	115.3
1982 1	96.1	89.1	97.2	104.3	94.7	113.4
2	97.6	90.6	98.8	109.7	94.9	126.0
3	98.1	92.6	99.2	113.2	94.1	131.0
4	97.7	94.3	98.4	112.9	93.2	131.9
1983 1	99.4	93.7	100.4	113.1	95.8	131.7
2	99.2	92.1	100.4	114.5	95.3	131.5
3	102.0	97.7	102.8	117.6	97.5	142.0
4	103.1	97.8	104.0	118.3	98.9	145.2
1984 1	103.1	97.0	104.2	117.3	99.5	148.3
2	101.6	98.1	102.3	108.1	100.2	144.0
3	102.2	100.5	102.5	105.4	101.5	144.3
4	103.1	98.7	103.8	109.6	101.7	151.8
1985 1	105.7	99.5	106.8	115.7	103.6	154.9
2	107.7	100.0	109.0	121.9	104.4	150.8
3	106.9	99.1	108.3	120.9	103.8	146.1
4	107.4	100.8	108.5	121.9	103.6	149.3
1986 1	107.7	98.1	109.4	127.6	102.8	155.6
2	107.9	102.0	108.9	124.0	103.4	149.7
3	109.8	104.9	110.6	126.7	104.9	159.3

(1) The long run series in column 3-5 are consistent with table 1.

NOTES TO EDITORS

1. The index numbers of output of the production and construction industries in this Press Notice are on the base 1980 = 100 and classified to the 1980 revision to the Standard Industrial Classification (SIC). These industries account for 42 per cent of gross domestic product; production industries alone accounts for 36 per cent. The index numbers were first published in this form in September 1983. The monthly index for the production industries covers only the energy (and water supply) Division 1 of the SIC, and manufacturing industries, Divisions 2 to 4 of the SIC. An index of production and construction broadly equivalent to the previously published "all industries' index of production" is available only quarterly. These changes were described in advance in March 1983 Economic Trends. A further article describing the effects of rebasing appeared in October 1983 Economic Trends.

2. The purpose of the index numbers is to measure changes in net output or value added (that is total outputs less total inputs) at constant (1980) prices. Conceptually, this should be estimated as the difference between outputs and inputs, each valued at the appropriate prices of the base year. However, this approach, known as double deflation, is difficult to apply reliably since it requires a great deal of information. In practice, movements in net output at constant prices are generally estimated by movements in gross output at constant prices. This yields satisfactory estimates, provided the ratio of gross to net output remains largely unchanged, as will generally be the case in the short-term. Further discussion of the concepts of measurement may be found in "Sources and Methods, Studies in Official Statistics No 37" (HMSO, 1985).

3. The index of production is a weighted average of 330 separate indicators, each of which describes the activity of a small sector of industry. These indicators are obtained monthly where possible but for a number of sectors, representing 17 1/2 per cent of activity, only quarterly data are available. Two Occasional Papers, one describing the weights and indicators and the other the sources used in compiling the index, are available.

4. Many of the basic series used to construct the index of production measure either final production or deliveries. Neither type of series takes account of changes in work in progress and series based on deliveries do not take account of changes in stocks of finished goods. All of the index numbers in this Press Notice have been adjusted where necessary, for estimated changes in stocks. An Occasional Paper describing these calculations is available.

5. More detailed tables on the index of production are published regularly in "British Business" and the "Monthly Digest of Statistics".

6. Estimates of the output of the construction industry are compatible with those published by the Department of the Environment which are available only quarterly, one month in arrears of the corresponding quarters' estimates for the output of production industries. The aggregate index numbers no longer make use of preliminary estimates for the construction industry based, in advance of receipt of regular returns from the industry, on broad indicators of activity; they are thus delayed by one month but are better founded.

7. The index numbers in this Press Notice are all seasonally adjusted, to remove annually recurring month-to-month variations owing for example, to the incidence of holidays and other regular seasonal patterns of behaviour. The adjustments can only be derived from analysis of past data and may not be completely appropriate when holiday patterns change sharply. Unadjusted data may be obtained from CSO.

8. Estimates for the latest few months are always based on partial information and should be regarded as provisional and subject to revision as more complete data become available. During the lifetime of the 1975-based index, the average revision (regardless of sign) to the all-industries index for the latest month was one half of 1 per cent. It is recommended that, to obtain an assessment of short-term change, attention should be directed to the three-month-on-three month changes. The average revision to this latter measure was one quarter of a percentage point over the same period. An Occasional Paper is available from CSO describing the effects of revisions.

9. Occasional Papers (price £2.50 each) and off-prints of Economic Trends articles (price £1.50 each) are available from the Central Statistical Office.

10. Bias adjustments for the index of manufacturing output

In an attempt to allow for understatement in the provisional figures, an improved system of adjustments to manufacturing output was introduced in January last year. Some detail was included in note 12 of Notes to Editors in the January 1986 Press Notice and a fuller note on the methodology of the adjustment procedure is available on request from the CSO. The adjustment procedure makes use of smoothed monthly CBI figures on expectations of growth in output. The bias adjustment included in the manufacturing figures this month are:

1986

June	July	August	September	October	November
+0.1	+0.1	+0.1	+0.1	+0.1	+0.2

MR 9/30

pup-

FROM: A C S ALLAN
DATE: 27 January 1987

CHANCELLOR

PCC DISCUSSION ON THE FORECAST

PCC displayed their usual trait of looking for the bad news in anything. This reached an extreme when everyone began to act as if it was bad news if the fiscal adjustment got any bigger!

2. Terry was on the side of caution. There could be a cyclical element in the increase in revenues, and there was some evidence that errors in revenue forecasts were also cyclical. But it was nonetheless clear that money was coming out of our ears. He would hold to a £2 billion tax package. He thought that the prospects for 1987/88 were pressing against the margins of safety. He would not want to see any fall in the exchange rate, and indeed a rise could be a useful offset to the inflationary pressure.

3. Robin Butler was worried about inflation and the balance of payments etc - rather too influenced by press stories, I think. He recognised the likelihood of the planning total being exceeded in 1988/89 because of local authorities, social security etc. But he thought we might do better than assumed on MOD and on other central Government programmes (it was this remark which led to the "shock horror" about an even higher fiscal adjustment).

4. Frank made a mixture of good and bad points, in my view. He went on about how the current account deficit would be financed - the forecasters have it largely financed from increases in non-resident holding of sterling deposits, which worried him. This is plainly absurd: there cannot be any problems over financing a deficit of less than one per cent of GDP, and in any case the capital account forecasts are not worth the paper they are written

on (I speak from experience). But he made some good points about the problems we might face on the monetary side in April. He thought the very low PSBR must imply a fall in interest rates at the long end. And if the Budget was seen as good for confidence we could well find ourselves coming under very strong pressure for a cut in short-term interest rates, just at the time when MO, our only remaining targeted indicator, might be over the top of its band. He could also see the RPI/electoral attractions of a cut in the mortgage rate in April.

5. Peter was worried about money GDP. He thought we should stick to the £2 billion tax package and go for a £3 billion PSBR. He asked John Odling-Smee what PSBR would be needed to get money GDP back to its MTSF path. John replied that it would be about zero, and so Peter drew the conclusion that a £3 billion PSBR was a substantial relaxation in our fiscal stance!

6. Robin Butler noted that there were very substantial tactical difficulties over how to handle the likely increase in the planning total for 1988/89. We could hardly admit to anything in the Budget, and so would have to publish the PEWP numbers in the Red Book. At what stage would we then reveal our hand? We could not hope to spring another surprise in the Autumn Statement, but would not want to conduct the PES round against a background of a free-for-all. The timing of the election would be critical.

7. Terry noted that if we massaged down the public expenditure numbers we should also have to massage down the revenue numbers and commentators would be very alert for this sort of thing. Peter sensibly added that he hoped your meeting on Monday could concentrate on the policy implications, with a separate, smaller meeting on presentation and publication.

8. Among other comments: Peter Kemp thought the gently rising path for the RPI was a terrible background for the pay round, and was concerned about pay prospects generally. Frank asked about the

(for the public sector, I presume, since private sector settlements seem rather good) current account forecast in future years, and was told that the deficit started falling in 1989/90.

A C S ALLAN

Rus

A23/1 COPY NO 44

MONTHLY ECONOMIC BRIEF

Prepared by the CSO on 30 January 1987

Adult unemployment fell sharply again between November and December, the fifth consecutive monthly fall. It seems likely that even without Restart and other measures the previous upward trend would have been halted and possibly marginally reversed.

In December exports were little changed from November, while imports fell by 3½ per cent. Visible trade was in deficit by £0.8 billion, an improvement on the deficit of £1.0 billion in November. For 1986 as a whole, the current account was in broad balance - in line with the Autumn Statement forecast. The underlying levels of both non-oil export volume and non-oil import volume continue to rise.

The annual rate of inflation rose to 3.7 per cent in December from the 3.5 per cent recorded in November. In January a further small rise in the twelve-month rate may occur. During the first seven months of 1986 the price index for materials and fuel purchased by manufacturing industry continued the decline which began in March 1985. The index rose between August and November 1986 but has since fallen slightly, and is now some 4 per cent down on a year earlier and almost 13 per cent down on the 1985 peak.

Current projections suggest that GDP rose by 1 per cent between the third and fourth quarters of 1986 and continues to grow at a current underlying trend rate in the range 2-4 per cent per annum.

The PSBR is estimated to have been minus £1.4 billion in December, giving a cumulative total for the first nine months of 1986-87 of £4.4 billion. Outturns to date suggest that the PSBR is more likely to undershoot than overshoot the forecast of £7 billion for 1986-87 given in the Budget and the Autumn Statement.

Sterling has been around 69 in effective terms. It fell to 68.3 in the middle of the month but rose later, helped by the weakness in the US dollar.

RECENT RATES OF CHANGE AND ASSESSMENT OF CURRENT TREND FOR SOME KEY ECONOMIC INDICATORS

In the following notes, the figures for current trend represent our best assessment of the current underlying rate of increase after making allowance for temporary distorting factors such as strikes, unseasonal weather effects, etc. The figures show how the series are moving currently and may be different from the comparisons over the latest published twelve months.

GDP (average measure) in the third quarter of 1986 was 2 per cent higher than in the same period a year ago. This figure does not take account of past experience which shows that revisions to growth rates for the initial published estimates of GDP were on average, upwards, though not uniformly so. The assessment of current underlying trend for the fourth quarter of 1986 is that the rate of increase lies in the range 2-4 per cent per annum.

Industrial production in the three months to November 1986 was 1 per cent higher than in the same period a year ago; manufacturing output was 2 per cent higher. The assessment of underlying trend for industrial production is that the rate of change currently lies in the range $\frac{1}{2}$ to $2\frac{1}{2}$ per cent per annum. The trend in manufacturing output is in the range $1\frac{1}{2}$ to $3\frac{1}{2}$ per cent per annum.

Retail prices rose by a little over $3\frac{1}{2}$ per cent in the twelve months to December 1986. It is only possible to provide a useful indicator of trend for about 70 per cent of the RPI, mainly that covering private sector prices and excluding eg mortgage interest, rent, rates, products produced by nationalised industries, seasonal food and petrol. The current trend for this series is just under 4 per cent per annum. In the twelve months to December 1986 this series rose by 4 per cent (not published).

Producer input prices fell by $\frac{1}{2}$ per cent in seasonally adjusted terms in December after four months of increase, and will probably show some further decline in January. The index should be at least 4 per cent lower than in January 1986.

Average earnings (underlying) in the twelve months to November rose by $7\frac{1}{2}$ per cent. The current trend is estimated to be $7\frac{1}{2}$ per cent per annum.

Unit wage costs in manufacturing in the three months to November rose by 3 per cent compared with the same period a year ago. The current underlying trend is estimated to be in the range 2-4 per cent per annum.

Unemployment (excluding school leavers) in the twelve months to December has fallen on average by over 1,000 per month. The current trend continues downward at the rate of some 20,000 per month. There has been an average fall of over 17,000 per month in the past six months, and within this period, a fall of 25,000 per month in the past three months.

Movements over the latest published 12 months include any revisions that may have occurred since last publication (in general any such differences only occur in the GDP series).

CHART 1A

Gross domestic product (average measure)

1980 = 100, seasonally adjusted

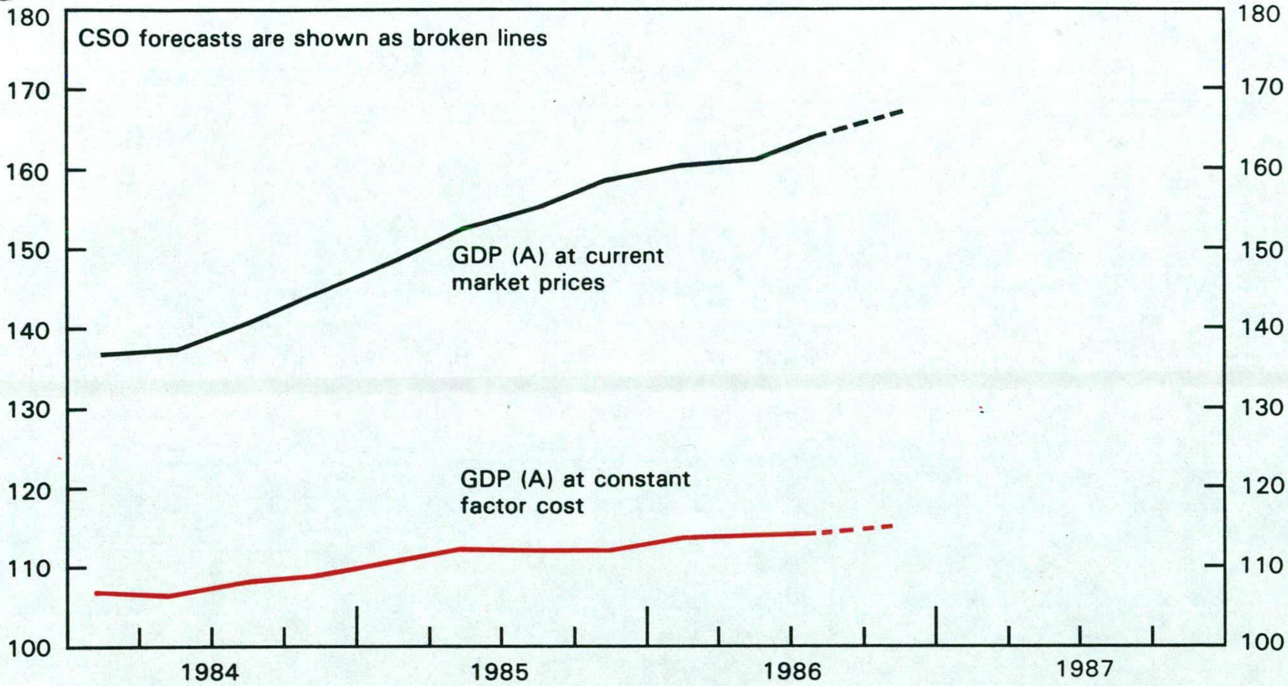


CHART 1B

Gross domestic product (average measure)

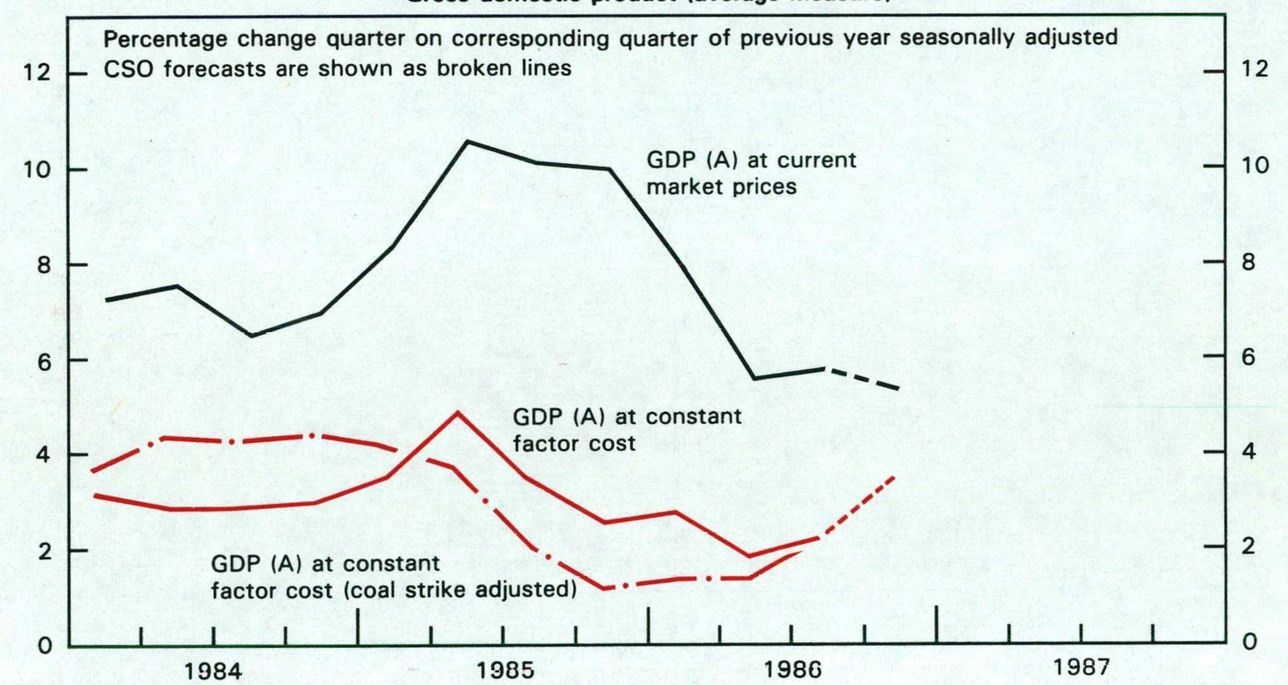
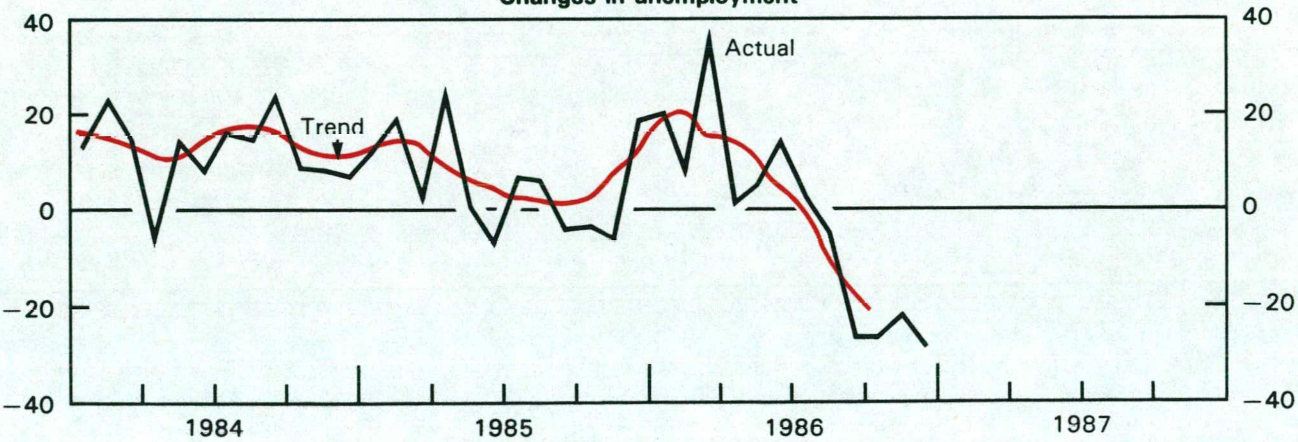


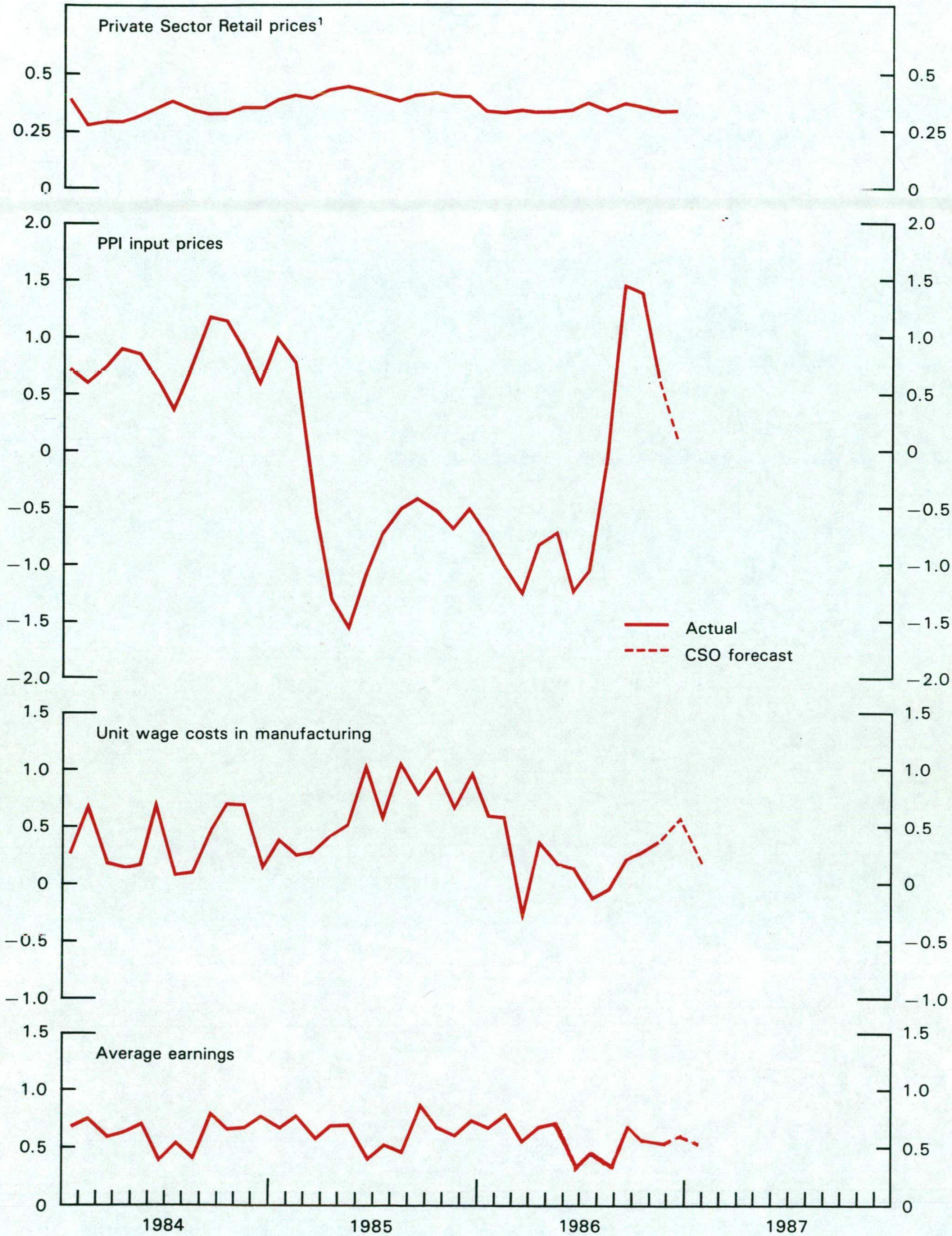
CHART 2

Changes in unemployment



Rate of increase in average earnings, unit wage cost in manufacturing PPI input prices and Private sector retail prices

Month to month percentage changes, smoothed and adjusted for distorting factors where appropriate



1. Excludes seasonal food, mortgage interest, rent, rates and water charges motor vehicle licences, products produced by Nationalised industries and petrol.

CHART 4

Movements in underlying average earnings and the tax and price index comparisons with 12 months previously

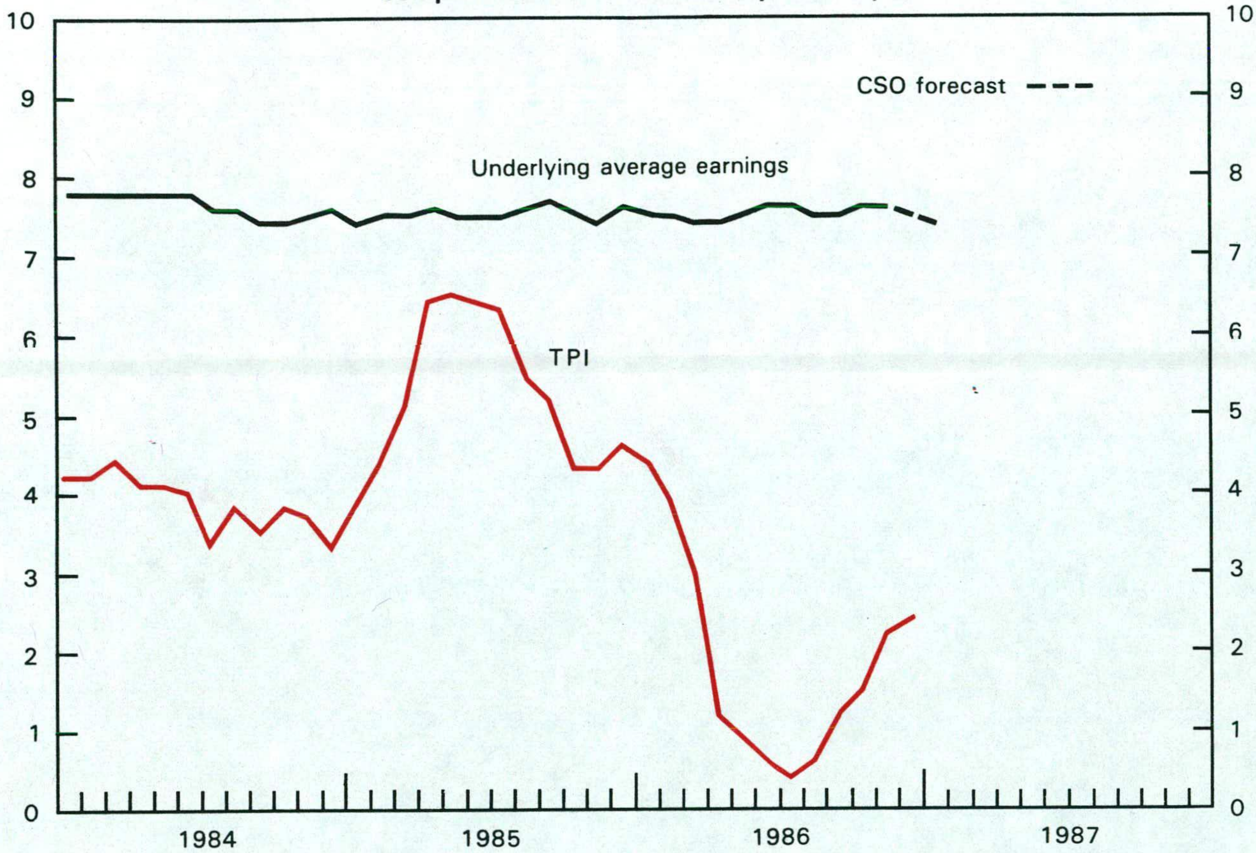


CHART 5

Interest rates

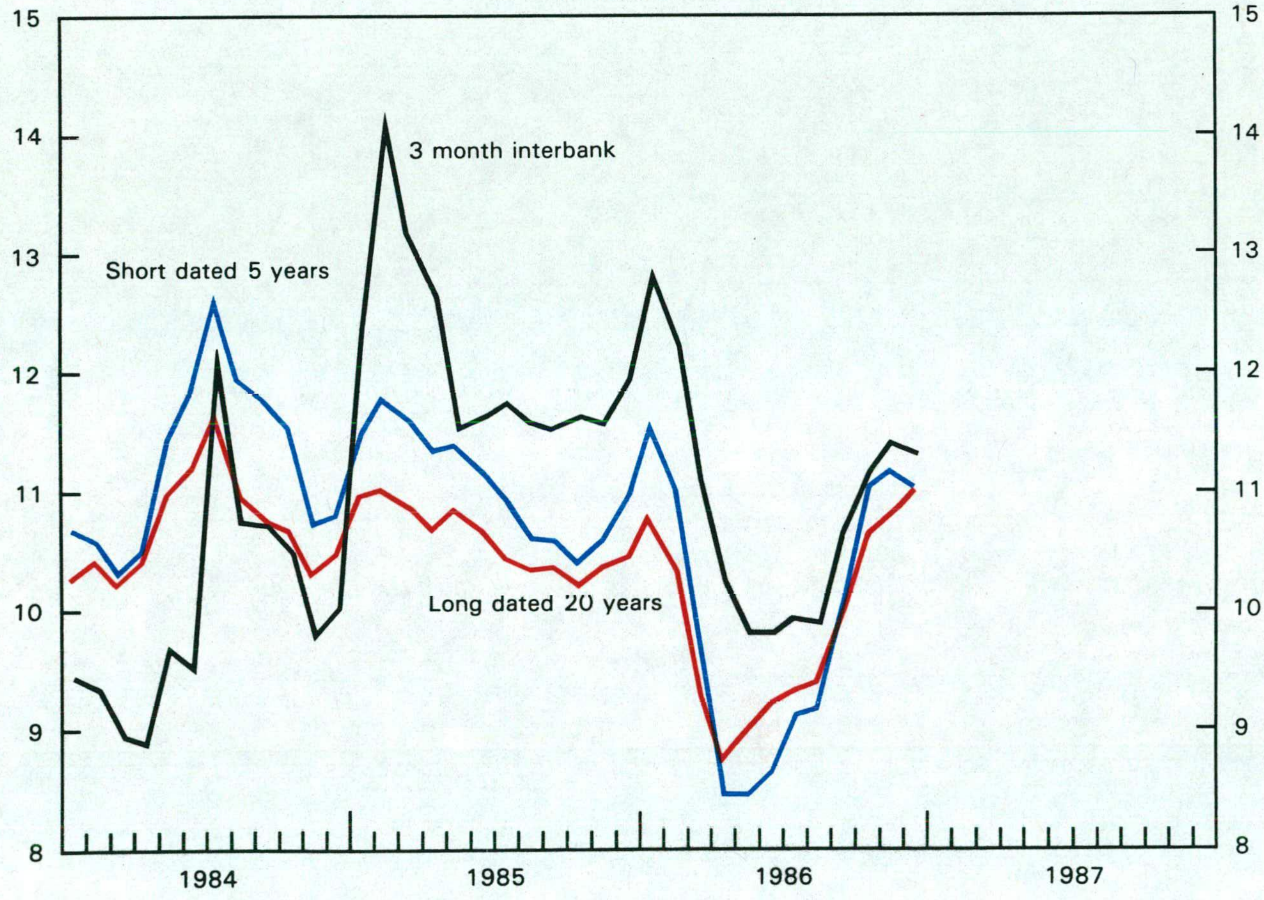
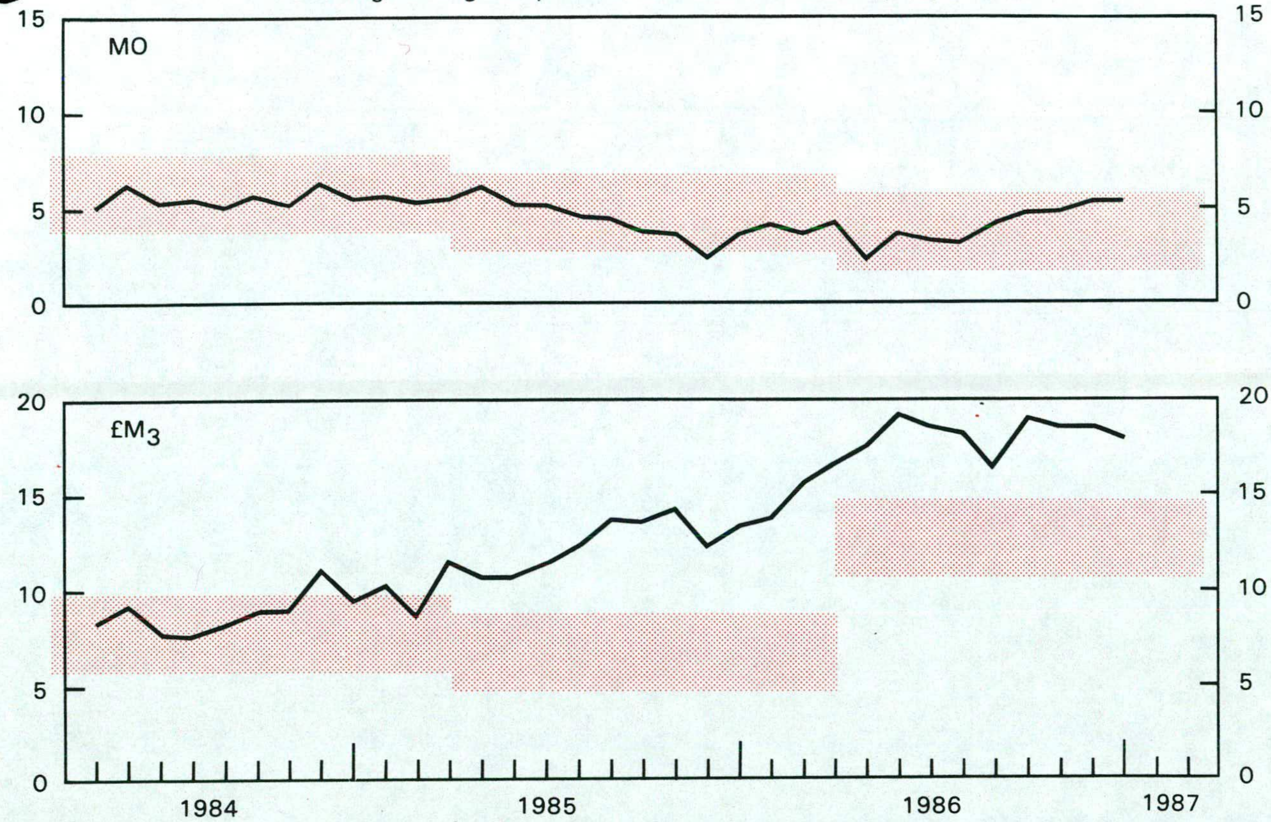


CHART 6

Monetary aggregates

not

Percentage Change on previous 12 months (seasonally adjusted)

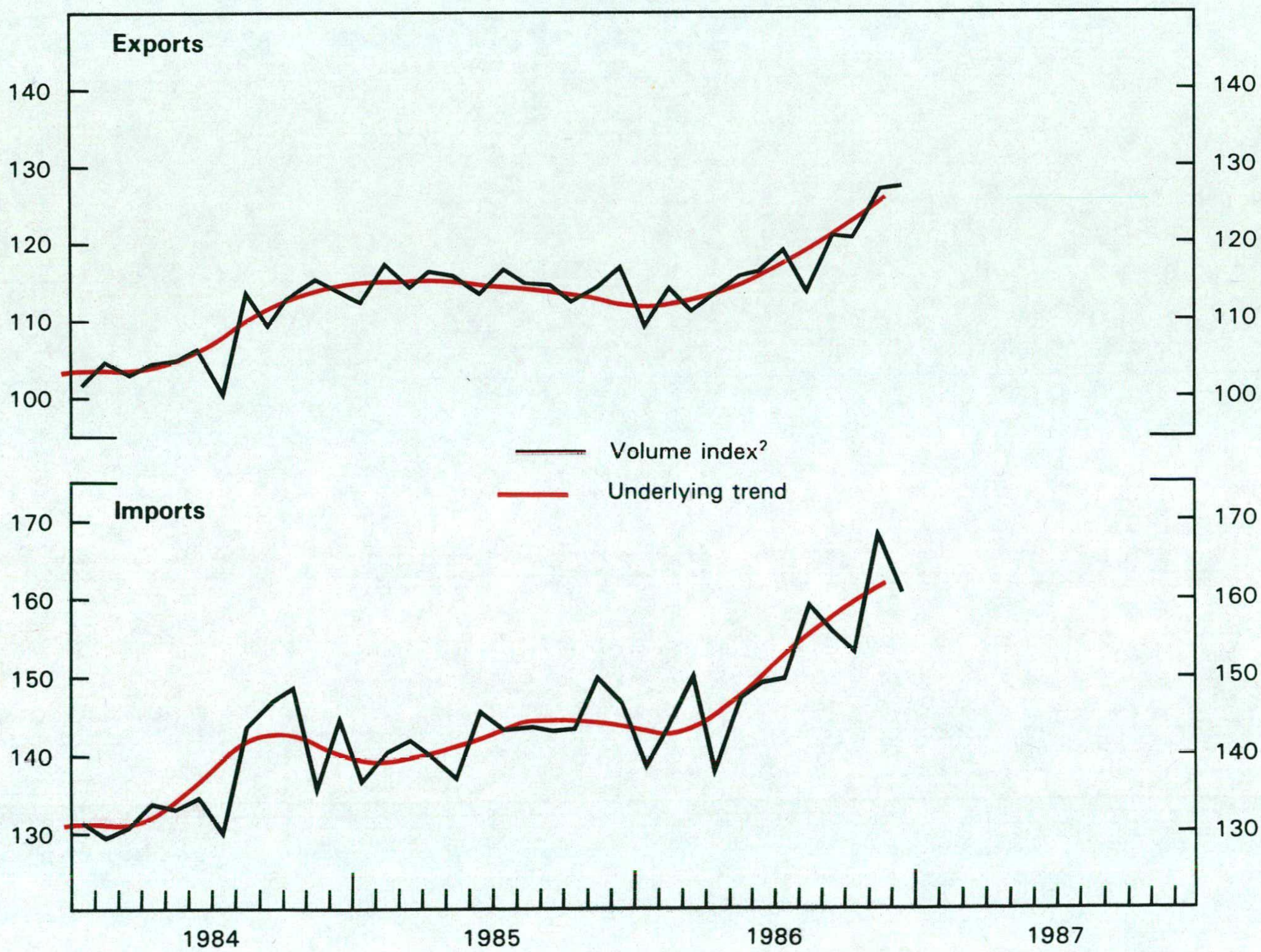


Shaded areas represent announced target ranges

CHART 7

Exports and Imports (excluding oil and erratics[1])

Index 1980 = 100



1. Ships, North Sea Installations, Aircraft, Precious Stones and Silver
2. Seasonally adjusted data, Balance of Payments basis

MONTHLY ECONOMIC BRIEF

DETAILED ASSESSMENTS SUPPLEMENT

A ECONOMIC ACTIVITY

A1 Total gross domestic product (in real terms)

A1.1 The current projection of the average measure of GDP, GDP(A), for the fourth quarter of 1986 suggests a rise in GDP of over 1 per cent compared with the previous quarter, and a growth of 3-3½ per cent compared with the fourth quarter of 1985, which is faster than the annual rate of growth in previous quarters (after allowing for the effects of the coal dispute).

A1.2 The three measures of GDP at constant factor cost show different profiles in 1986 with only GDP(O) exhibiting growth between the first three quarters of the year. The projections into the fourth quarter indicate GDP(O) is unchanged compared with the previous quarter, while the growth in both the other two measures is 1½-2 per cent.

A1.3 Despite the uneven quarterly profiles shown by the individual measures of GDP during 1986, the average measure indicates growth through the year and together with the fourth quarter projection implies growth in GDP(A) of about 2½ per cent between 1985 and 1986,or 2 per cent if allowance is made for the effect of the coal strike. Our best assessment of the current underlying trend in GDP(A) is that it now lies in the range of 2-4 per cent per annum.

A2 Money GDP

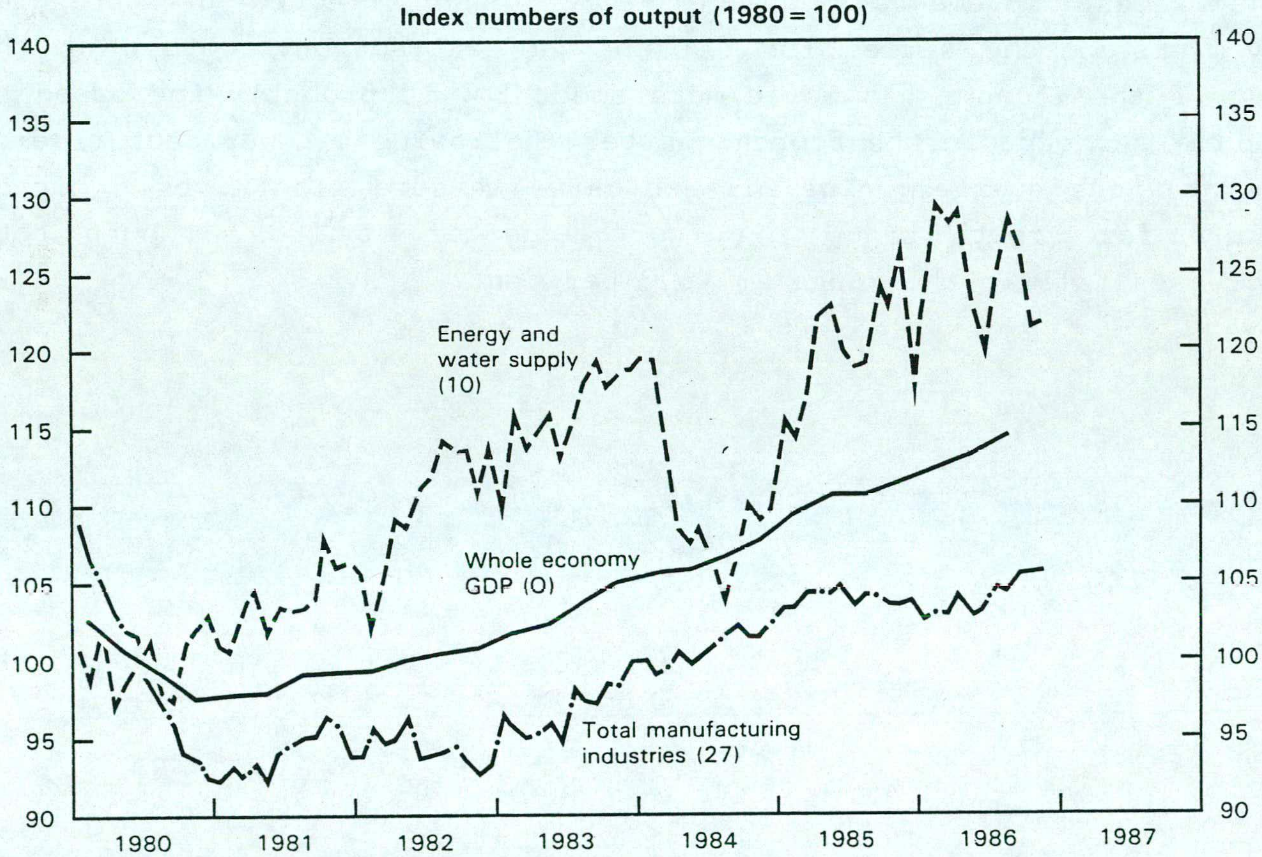
A2.1 The current projection of money GDP for the fourth quarter of 1986 suggests growth of nearly 2 per cent compared with the previous quarter and nearly 5½ per cent compared with the fourth quarter of 1985. The increase between 1985 and 1986 was about 6 per cent or 5½ per cent if broad allowance is made for the effect of the coal strike in 1985.

A3 Output measures

A3.1 Manufacturing output reached a temporary peak in the second quarter of 1985 and then declined 1½ per cent by the first quarter of 1986. However since the first quarter, output has more than recovered and in the three months to November was 1 per cent higher than the second quarter of 1985. Manufacturing output in the three months to November was 1½ per cent higher than in the previous three months, but this probably overstates the underlying rate of growth. The CBI Trends Survey of output expectations points to moderate growth.

A3.2 Sizeable monthly movements in oil extraction make trends in the energy sector difficult to assess, but it is probably at best flat.

Index numbers of output (1980 = 100)



Note: Figures in Brackets represent percentage of GDP (O) by weight in base year 1980.

A3.3 The underlying output of all production industries in the second half of 1985 was 1 per cent below the level reached in the first half, but partially recovered in the first half of 1986. Since then, the output of production industries has continued to increase, reflecting the improvement in manufacturing output. The index of production is expected to be about 108½ for December (November was 110.0), reflecting reduced oil extraction due to a pipeline leak. In January the index is expected to recover to about 110.

A3.4 The output measure of GDP is thought to have remained unchanged between the third and fourth quarters of 1986, following the high 1 1/4 per cent increase in the third quarter. In the fourth quarter, oil and gas extraction was well below its third quarter level but manufacturing output continued to grow. Although there was some slackening in the rate of growth of distribution output, overall growth in the service industries was similar to recent quarters.

A3.5 Recent movements in GDP(O) have been affected by irregular movements in the series for oil and gas extraction. Output of the rest of the economy has moved more smoothly; it probably increased by about ½ per cent in the fourth quarter, following a 1 per cent rise in the previous quarter. The oil-exclusive measure also gives a higher figure for growth since the fourth quarter of 1985, though both increases fall in the range 2½ to 3 per cent.

A4 Cyclical indicators

A4.1 The cyclical indicators continue to give no clear view of the direction of the business cycle during 1986 or of its likely development in coming months. The coincident index was broadly unchanged over the year while the two leading indices have been irregular.

A4.2 Since the trough in 1981, the main economic series which are used to "define" the business cycle (ie. the three measures of GDP, industrial production and retail sales) have not as a whole exhibited the sharp swings in growth rate seen in previous cycles. One interpretation of this is that the effect of the business cycle on the economy has been diminished. It would therefore be unsurprising that the indicator system has failed to reveal any clear cycle in recent years and a matter of some note that the major economic time series are now exhibiting non measurable cyclical behaviour.

B THE LABOUR MARKET

B1 Unemployment and Vacancies

B1.1 The seasonally adjusted level of unemployment (UK, excluding school leavers) fell sharply by 28,000 between November and December to 3.116 million, 11.3 per cent of the working population, now lower than a year ago.

B1.2 This fall continues the run of sharp falls over the previous three months and is the fifth consecutive monthly fall. Over the past six months on average the seasonally adjusted level has fallen by over 17,000 per month, the largest six month fall since the end of 1973.

B1.3 The current trend in the series appears to be a fall of the order of 20,000 per month. Restart and Employment measures have helped. Also, the new availability tests introduced at the beginning of November are likely to have begun to have some impact and may be responsible for some reduction in the inflow into unemployment when compared with December 1985. However the effects are uncertain and cannot be quantified. It seems likely that even without all these various influences on the count, the previous upward trend would have been halted and possibly marginally reversed.

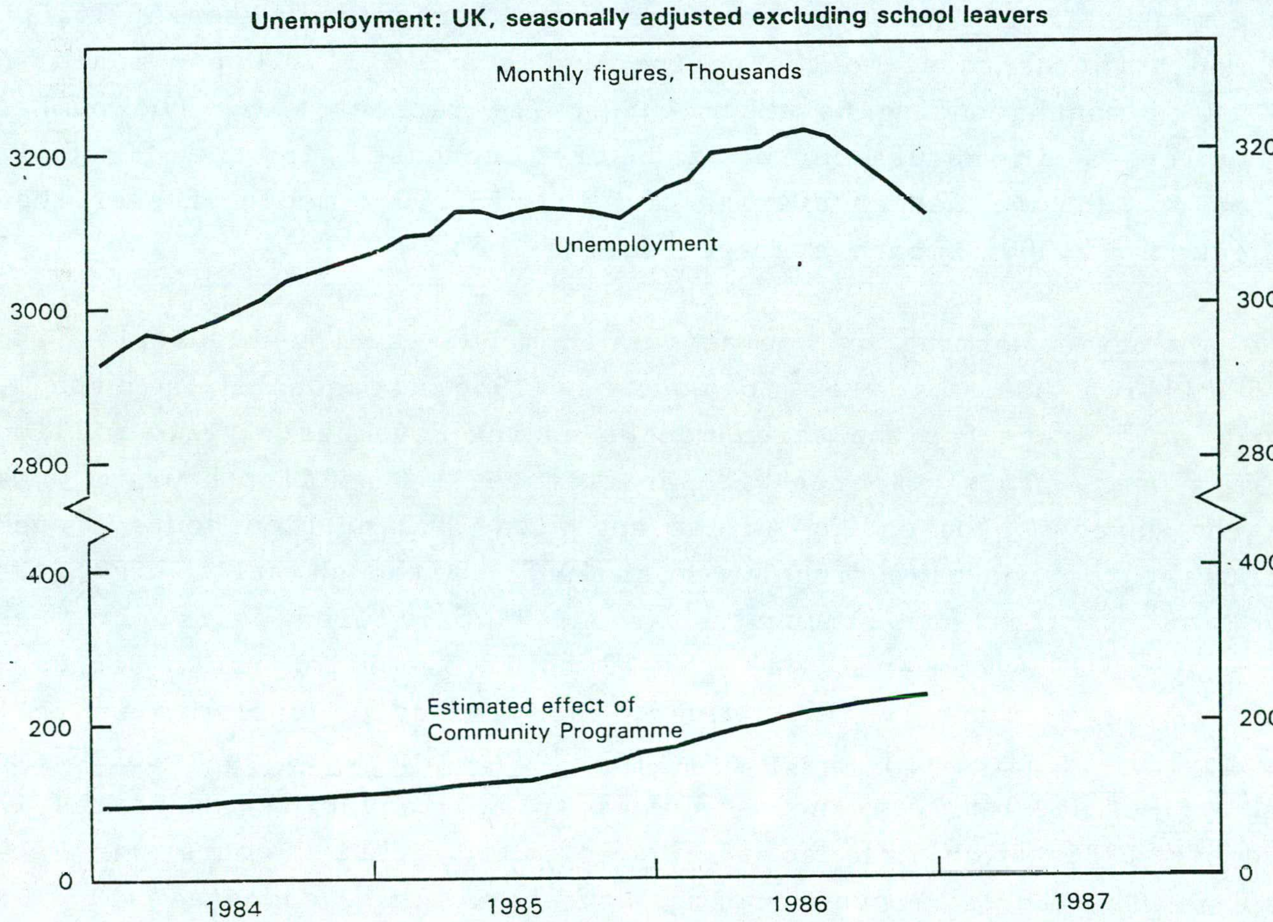
B1.4 Our best assessment is that Restart has so far reduced the claimant count by the order of 50,000, that is around 10,000 per month over the past five months. Employment measures, particularly the Community Programme (CP), have also continued to have a favourable impact and have been reducing unemployment by up to around 5,000 extra per month. Since rather more of the CP places may be going to the long term unemployed, there will be some overlap between the Restart and measures effect, so the two estimates cannot be added together.

B1.5 The falls in unemployment over the past few months have occurred among both men and women and have been spread across most regions with the exception of Scotland and, until recently, Northern Ireland where unemployment has now fallen for two months following previous sharp rises. Over the past year unemployment has fallen fastest in the North, Wales, the North West and West Midlands.

B1.6 The 'headline' claimant total (unadjusted, including school leavers) rose over 12,000 in December to 3.229 million, 11.7 per cent of the working population. There was an increase of 22,000 among adults while unemployed school leavers fell by over 9,000, little different from the fall a year ago. The December total of school leavers aged under 18 was 89,000, some 10,000 less than in December 1985.

B1.7 The stock of unfilled vacancies (seasonally adjusted and excluding Community Programme vacancies) fell by 5,000 in the month to December following rises in each of the previous ten months. The fall was mainly due to a reduction to the inflow of notified vacancies, while the outflows continued to rise. Placings remain at their highest level since the end of 1979.

Unemployment: UK, seasonally adjusted excluding school leavers



B2 Employment and hours

B2.1 The employed labour force in Great Britain is estimated to have increased by 71,000 in the third quarter of 1986 (seasonally adjusted). This follows the increase of 40,000 in the June quarter and compares with the increase of 64,000 in the September quarter a year ago. The total increase over the year ending September 1986 is estimated at 207,000. The increase of 71,000 in the September quarter is the net result of an increase of 40,000 in the number of employees in employment and an assumed increased of 30,000 in self-employment. Later figures are available for the number of employees in employment in manufacturing industries, which is estimated to have decreased by 8,000 in November 1986. The monthly figures can fluctuate erratically and some of this fluctuation is removed if averages over three months are considered. The average decrease of 7,000 per month over the three months ending November compares with average decreases of 16,000 per month in the three months ending August and of 1,000 per month in the three months ending November 1985. The rate at which the number of employees in manufacturing industry decreased in the first 11 months of 1986 was, at an average of about 13,000 a month, faster than the roughly 4,000 a month averaged during 1985.

B2.2 Overtime working by operatives in manufacturing industries was 11.5 million hours a week in November 1986 (seasonally adjusted), giving an average for the three months ending November of 11.5 million hours a week. This compares with an average 11.6 million hours a week for the three months ending August and with 12.2 million hours a week for the three months ending November 1985. Although still high, the level of overtime has fluctuated around 11.5 million hours per week since April 1986 compared with the 12 to 12.5 million hours per week observed in most of 1985. However, this reduction reflects in part the fall in manufacturing employment. Short-time working resulted in the loss of 0.40 million hours a week in manufacturing industries in November 1986 which made an average of 0.50 million hours per week lost in the three months ending November. This compares with an average 0.41 million hours per week for the three months ending August 1986 and 0.38 million hours per week for the three months ending November 1985.

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The Employed Labour Force in Great Britain   Thousand: Seasonally adjusted

		Employees in employment				Self-Employed Persons	Employed Labour Force
		Manufacturing Industries	Service Industries	Other Industries	All Industries and Services		
Levels							
1984	Sep	5,291	13,538	1,949	20,778	2,462	23,569
	Dec	5,298	13,647	1,941	20,886	2,489	23,703
1985	Mar	5,283	13,729	1,932	20,944	2,516	23,787
	Jun	5,275	13,793	1,909	20,977	2,543	23,846
	Sep	5,270	13,862	1,878	21,010	(2,574)	23,910
	Dec	5,254	13,935	1,855	21,044	(2,604)	23,972
1986	Mar	5,215	14,004	1,829	21,048	(2,635)	24,006
	Jun	5,162	14,077	1,810	21,059	(2,665)	24,046
	Sep	5,128	14,158	1,813	21,099	(2,696)	24,117
Changes							
1984	Q3	- 23	+ 75	- 2	+ 50	+ 27	+ 80
	Q4	+ 7	+109	- 8	+108	+ 27	+134
1985	Q1	- 15	+ 82	- 9	+ 58	+ 27	+ 84
	Q2	- 8	+ 64	- 23	+ 33	+ 27	+ 59
	Q3	- 5	+ 69	- 31	+ 33	(+ 31)	+ 64
	Q4	- 16	+ 73	- 23	+ 34	(+ 30)	+ 62
1986	Q1	- 39	+ 69	- 26	+ 4	(+ 31)	+ 34
	Q2	- 53	+ 73	- 9	+ 11	(+ 30)	+ 40
	Q3	- 34	+ 81	- 7	+ 40	(+ 31)	+ 71
1985	Jul	- 9					
	Aug	- 8					
	Sep	+ 12					
	Oct	- 1					
	Nov	- 14					
	Dec	- 1					
1986	Jan	- 7					
	Feb	- 25					
	Mar	- 7					
	Apr	- 8					
	May	- 30					
	Jun	- 15					
	Jul	- 19					
	Aug	- 15					
	Sep	-					
	Oct	- 14					
	Nov	- 8					

NB: Employed Labour Force also includes HM Forces
Brackets indicate projections based on the assumption that the average rate of increase between 1981 and 1985 is continuing.

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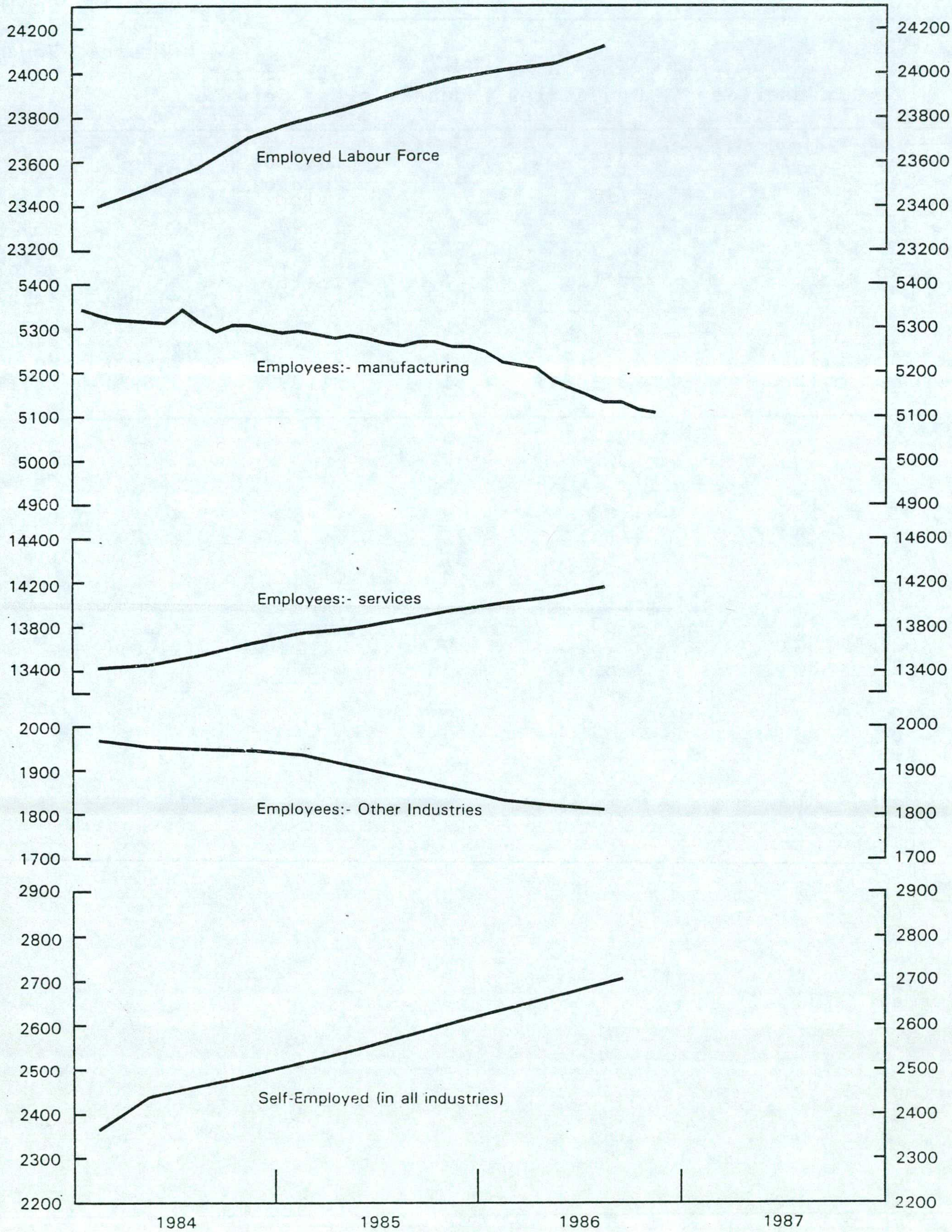
Employment

Thousands



B2.3 The index of average weekly hours worked by operatives in manufacturing industries (which takes account of hours of overtime and short-time as well as normal basic hours) was estimated at 103.6 in November 1986 (seasonally adjusted). This gave an average for the three months ending November of 103.5 which is the same as for the previous three months (ending August) and compares with 103.4 for the three months ending November 1985.

B3 Redundancies

B3.1 The downward trend in the number of redundancies confirmed as due to occur has accelerated. The reasons appear to be twofold; exceptionally high December 1985 figures have dropped out of the twelve month calculation and confirmed redundancies in the last three months have been lower than in recent years. The twelve month average, albeit with provisional estimates for the latest two months, is now at the lowest level since the twelve month period ended January 1980. However, these figures must be treated with caution. Changes in the operation of the Redundancy Fund introduced in August may have resulted in fewer redundancies being notified. The trend for confirmed redundancies in the manufacturing sector shows a similar pattern to total redundancies. The trend in redundancies in the energy and water sector has also fallen in recent months, but remains above the level in 1985 before the redundancies in the coal mining industry took effect. The upward trend of redundancies in the other industries and services sector appears to have halted and the trend has been broadly level since August. The trend in the numbers of advance notifications of redundancies has also been downward since June 1986.

B3.2 The number of confirmed redundancies in the three months ending December 1986 is expected to average about 16,500 a month, compared with 24,000 a month recorded during the corresponding period a year ago.

C PRICES AND REAL DISPOSABLE INCOME

C1 Average earnings

C1.1 The underlying increase in average weekly earnings in the year to November was 7½ per cent, the same as the increase in the year to October. The underlying annual increase has been broadly unchanged since the middle of 1984. There is little sign of a significant change in the annual increase, as the effect of some lower pay settlements may be offset by a rise in payments resulting from additional overtime working. Average earnings increases reflect not only normal pay settlements but also variations in overtime working, changes in productivity and bonus payments and changes in the composition of employment. The New Earnings Survey results for April 1986 showed that for full time adults, average earnings for non-manuals increased by considerably more than for manuals (increase of 9.0 and 6.8 per cent respectively on April 1985). The higher increase for non-manuals indicates that these employees received significant payments additional to the annual pay settlement.

C1.2 The actual increase in the year to November, of 8.1 per cent, was higher than the estimated underlying increase because of the net effect of the following temporary factors on the actual annual increase: (a) teachers had been paid two settlements in the twelve month period because of the delay in reaching the April 1985 settlement which inflated the increase and (b) changes in the timing of some bonus payments meant that the level of those payments in November 1986 was higher than in November 1985, inflating the increase. On the other hand, back pay in November 1986 was lower than in November 1985, depressing the increase.

C1.3 In December and January, the underlying increase for the whole economy may show little change. Although pay settlements in general are lower than the corresponding settlements a year ago they are relatively few in number at this time of year, so that the effect of these lower settlements on average earnings could be offset by other factors such as a rise in payments related to economic activity. The annual increases are expected to be similar to the underlying increases.

C2 Unit wage costs and competitiveness

C2.1 Unit wage costs in the whole economy rose by nearly 1½ per cent between the second and third quarters of 1986. In the fourth quarter the rise is likely to be about 2 per cent, with total wage costs rising by about 2 per cent and GDP(O) showing little change; this would give a rise in unit wage costs of over 5½ per cent since the fourth quarter of 1985.

C2.2 In the three months to November, manufacturing unit wage costs increased by ½ per cent compared with the previous three months. A rise in average earnings of 2½ per cent was largely offset by a 2 per cent increase in productivity. (However this rise in productivity is probably erratically high and consequently the calculated increase in unit wage costs is below the underlying trend). Compared with the same period a year ago, unit wage costs in the three months to November increased by 3 per cent, with an increase in average earnings of 7½ per cent being partially offset by a rise in productivity of 4½ per cent.

C2.3 UK competitiveness improved, at least in the short-term, between the fourth quarter of 1985 and the first quarter of 1986, when the fall in the exchange rate more than offset the rise in UK domestic labour costs. Despite the continued depreciation of sterling in the second quarter, UK competitiveness worsened slightly. With the sharper fall in the value of the pound more recently, however, there is likely to have been some further improvement again in the third quarter. Conversely relative unit wage costs and hence output in Japan and West Germany, in particular, have been adversely affected by exchange rate movements.

C3 Producer prices

C3.1 The seasonally adjusted price index for materials and fuel purchased by manufacturing industry fell by ½ per cent in December after 4 months of increase. It was 4 per cent lower than a year earlier. Most of the fall since the end of 1985 was due to lower fuel prices: raw material prices showed a relatively small decline. The seasonally adjusted index will probably show some further decline in January and be at least 4 per cent lower than in January 1986.

C3.2 The twelve-monthly rate of increase in the index for prices of output of manufactured products (home sales) fell to a little over 4 per cent in November, having shown a fairly steady decline from around 5 per cent at the beginning of 1986 and 6 per cent at the beginning of 1985. The underlying annual rate of growth in the index is thought to be 4-4½ per cent. Taking account of seasonal factors, this suggests that the index should rise by about ½ per cent in January and should remain a little over 4 per cent higher than a year ago.

C4 Retail prices

C4.1 The annual rate of inflation in December, as measured by the 12-month change in the retail prices index, rose to 3.7 per cent from the 3.5 per cent recorded in November.

C4.2 The overall level of prices increased by 0.3 per cent between November and December, larger than the increase of 0.1 per cent recorded between the corresponding months a year earlier. There were increased mortgage interest payments for owner occupiers as residual effects of the increases announced in October entered into the index. Food prices, some local authority rents and motor insurance premiums were higher than in November. There were Christmas discounts on the prices of wines and spirits.

C4.3 The average annual increase in prices over the last quarter of 1986 was 3.4 per cent which slightly exceeds the Chancellor's Autumn Statement forecast of 3 1/4 per cent.

C4.4 In January a further small rise in the 12-month rate may occur. Sale prices are expected for clothing, footwear and durable goods but the scale of the reduction is uncertain.

C4.5 Although oil companies have announced petrol price increases these are unlikely to be reflected in the index until February.

C5 Real personal disposable income (RPDI)

C5.1 Between the third and fourth quarters of 1986 total wages and salaries are estimated to have risen by about 1½ per cent to reach a level about 8 per cent higher than the fourth quarter of 1985.

C5.2 Personal disposable income is estimated to have risen by around 1½ per cent between the third and fourth quarters of 1986. With prices, as measured by the consumers' expenditure deflator, also rising by about 1½ per cent in the same period, RPDI is tentatatively estimated as remaining flat.

		RPDI 1980 prices £bn	Consumers' expenditure 1980 prices £bn	Saving ratio per cent
1984		41.6*	36.6*	12
1985		42.8*	38.0*	11½
1986		(44.5)*	39.8*	(10½)
1984	Q1	40.9	36.2	11½
	Q2	41.2	36.8	11
	Q3	41.2	36.5	11½
	Q4	43.0	37.0	14
1985	Q1	42.3	37.4	11½
	Q2	42.7	37.6	12
	Q3	42.8	38.3	10½
	Q4	43.6	38.6	11½
1986	Q1	43.8	39.0	11
	Q2	44.3	39.6	10½
	Q3	44.9	40.2	10½
	Q4	(45.0)	40.5	10

*Quarterly average

D COMPONENTS OF DOMESTIC EXPENDITURE

D1 Consumers' expenditure at constant prices

D1.1 Between the second and third quarters of 1986 consumers' expenditure rose by just over 1½ per cent to a level about 5 per cent above the previous year. This estimate reflects increases in all categories of goods and services except beer and tobacco.

D1.2 Preliminary estimates of consumers' expenditure in the fourth quarter of 1986 indicate a rise of about 3/4 per cent from the third quarter to a level about 5 per cent above the same period a year earlier. This estimate reflects the strong growth in retail sales but with falls in food and energy products and an expected small fall in car purchase.

D1.3 The provisional index of the volume of retail sales in December at 125.9 was a little below the record November figure but well above previous levels. The fourth quarter figure at 125.2 is 2½ per cent higher than that in the third quarter indicating that strong sales growth continues, although there must remain some slight doubt about the rate because of difficulties with the seasonal adjustment at this Christmas period (see Quality Section). Some fall-back from the high levels of the past two months is to be expected particularly in view of the bad weather. A value of 124 (at most) is forecast for January.

D1.4 The strong growth in sales volume over the last year has no doubt been helped by the low rate of price increases - around 1 per cent per annum for consumer goods apart from food, drink and tobacco. For some categories, notably brown goods (TVs, videos, hi-fi, etc), there have been falls in price of up to 10 per cent over the year.

D2 General government final consumption at constant prices

D2.1 General government consumption in the fourth quarter is estimated to be £13.0 billion which brings the total for the second half of 1986 to £26.0 billion, just below the forecast in the Autumn Statement.

D3 Gross domestic fixed capital formation at constant prices

D3.1 Total fixed investment is expected to be about £11.8 billion in the fourth quarter of 1986 which would imply an increase in fixed investment for 1986 as a whole of 1 per cent on the 1985 level.

D3.2 Fixed investment by manufacturing industries (including leased assets) fell by 2 per cent between the first three quarters of 1985 and the first three quarters of 1986 whilst fixed investment in the construction, distribution and financial industries (excluding assets leased to manufacturers) fell by 1 per cent. Over the same period fixed capital formation by the extraction of mineral oil and natural gas industry fell 13 per cent. On the other hand fixed investment in dwellings rose 6 per cent between the first three quarters of 1985 and 1986 after remaining on a flat trend during 1985.

D4 Stockbuilding at constant prices

D4.1 Stocks increased £0.3 billion in the first three quarters of 1986 following an increase of £0.7 billion during the whole of 1985. Stocks are expected to increase by about £0.1 billion in the fourth quarter of 1986.

E OVERSEAS TRADE AND CURRENT BALANCE

E1.1 Visible trade showed a deficit of £0.8 billion in December with exports little changed from November and imports 3½ per cent lower.

E1.2 In the fourth quarter of 1986 the visible trade deficit was £2.6 billion; an improvement of £0.4 billion on the third quarter. The surplus on oil increased by £0.1 billion and the deficit on non-oil trade was reduced by £0.3 billion.

E1.3 By value, total exports increased by 10 per cent in the fourth quarter while imports increased by 6½ per cent. Excluding oil and the erratic items, export volume increased by 6 per cent in the latest quarter and import volume increased by 3½ per cent.

E1.4 First estimates and projections show a broad balance in the current account for 1986 as a whole - a deficit in visible trade of £8½ billion being offset by a surplus in invisibles (both being in line with the Autumn Statement). This compares with a current account surplus of £3½ billion in 1985. The invisibles balance for the fourth quarter of 1986 (£2.4 billion) is a CSO projection.

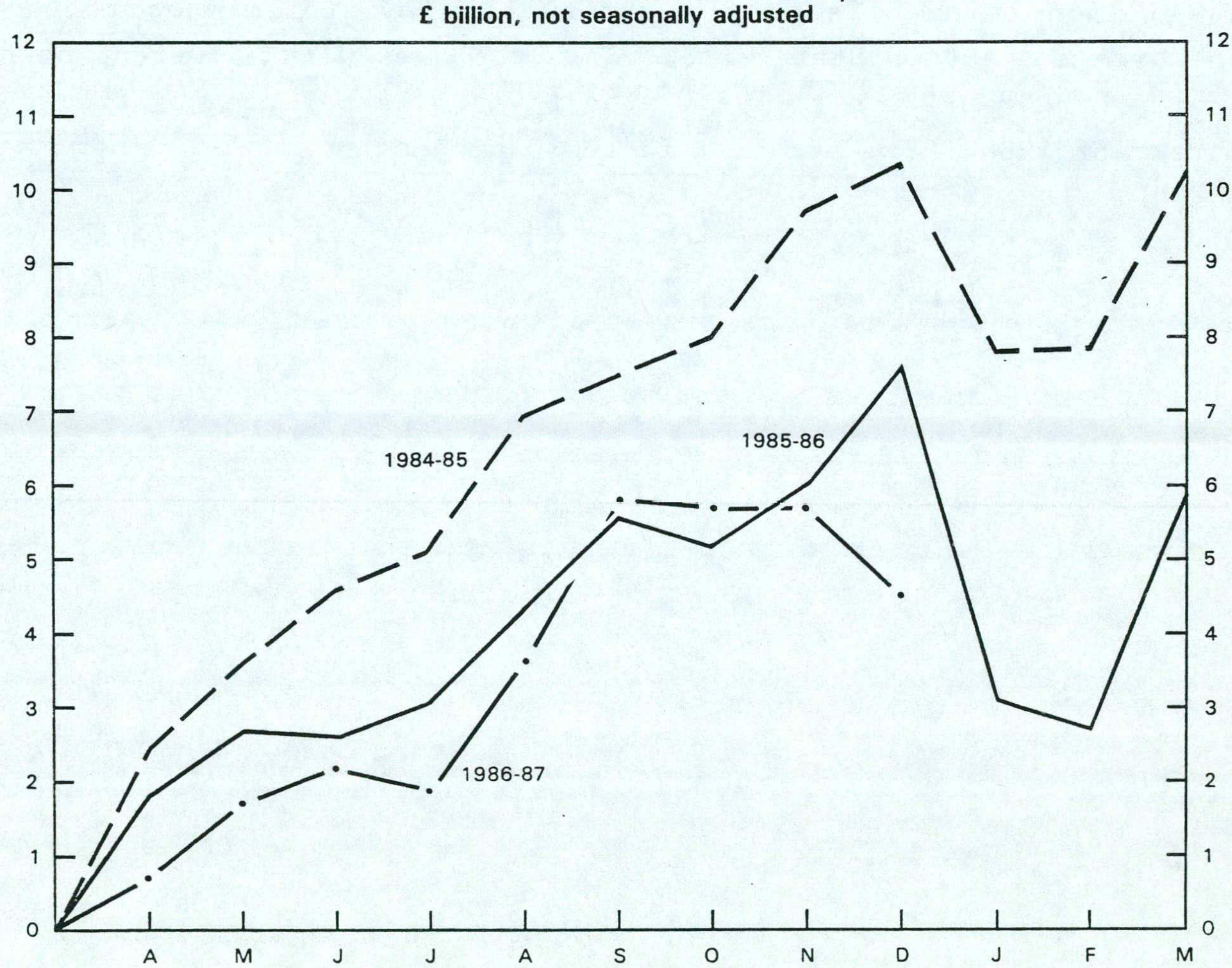
F FINANCIAL

F1 PSBR

F1.1 The PSBR is estimated to have been £0.1 billion in November and minus £1.4 billion in December, giving a cumulative total for the first nine months of 1986-87 of £4.4 billion. These figures are consistent with the final money supply figures published at the end of January. There were net receipts of £1.8 billion in December from the British Gas sale and earlier receipt of some £3/4 billion of Corporation Tax due on 1 January. In the first nine months of 1985-86, the PSBR stood at £7.6 billion.

F1.2 The forecast for 1986-87, announced in the Autumn Statement, is £7 billion. Outturns to date suggest that the PSBR is more likely to undershoot than overshoot this forecast.

Cumulative PSBR from start of financial year
£ billion, not seasonally adjusted



Note: The seasonal pattern can differ from year to year

F1.3 The components of the PSBR in December (consistent with the final money supply figures) were:

		(£ billion, not seasonally adjusted) Comprising		
	PSBR	CGBR(O)	LABR	PCBR
Outturns				
November	0.1	0.8	-0.3	-0.4
December	-1.4	-1.7	0.1	0.2
April to December	4.4	5.5	-0.4	-0.8

F2 Monetary growth

(All figures are unadjusted unless specified otherwise).

F2.1 In the 12 months to end-December, MO rose by 5.2 per cent and £M3 rose by 18.1 per cent. In December, MO rose by 7.6 per cent (1.4 per cent seasonally adjusted) and £M3 rose by 0.2 per cent (0.2 per cent seasonally adjusted).

F2.2 There is no underlying change in the twelve month growth rate of MO in December. MO remains within its target range of 2-6 per cent though towards the top end. The growth of £M3 remains high but difficult to interpret. The twelve month growth rate is below the average in recent months. The increase in December is the lowest monthly rise since January, although the figure is likely to have been lower than otherwise as, because of oversubscription to the British Gas Issue, about 60 per cent of the deposits built up in November were returned and unwound. (Estimates are uncertain but it may have reduced £M3 by 1/4 to ½ per cent).

F2.3 £M3 rose by £266 million in December. Counterparts to the change in £M3 are as follows:

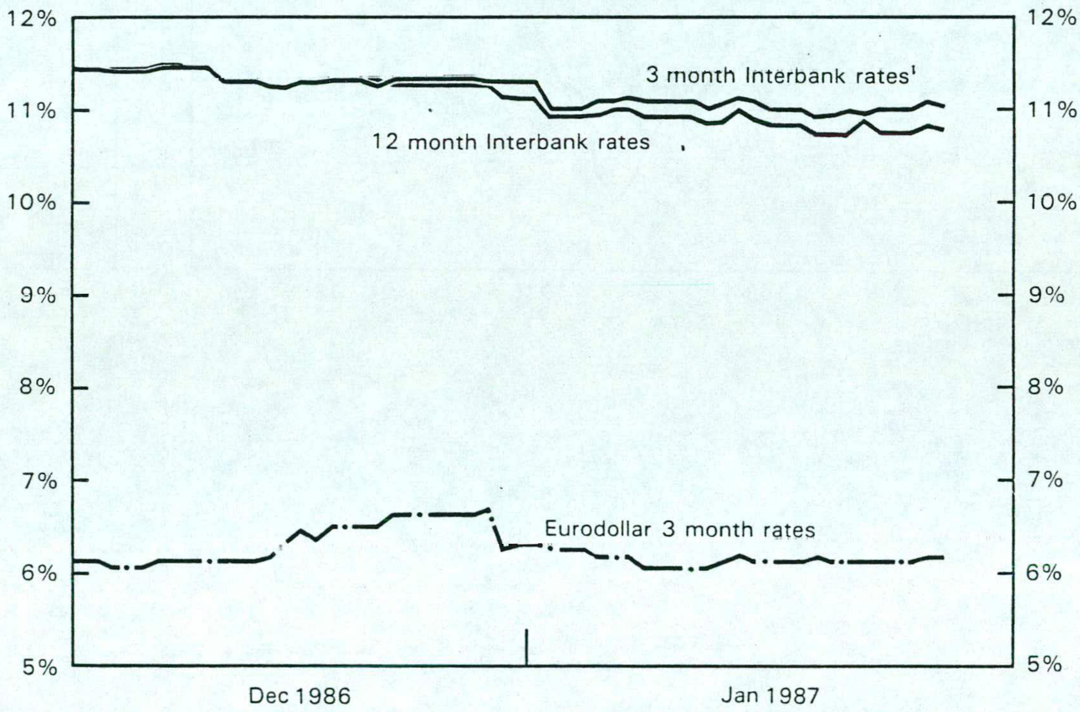
	£ million
PSBR	-1,394
Debt sales to the non-bank private sector and external flow to public sector	- 195
(of which debt sales to nbps)	(-125)
Sterling lending to private sector	+3533
Other counterparts	-1678
Change in £M3	+ 266

Sterling lending in December is not out of line with figures for recent months, but higher figures might have been expected given the surplus on the PSBR. More generally, financial developments make it increasingly difficult to read meaning into the behaviour of individual counterparts.

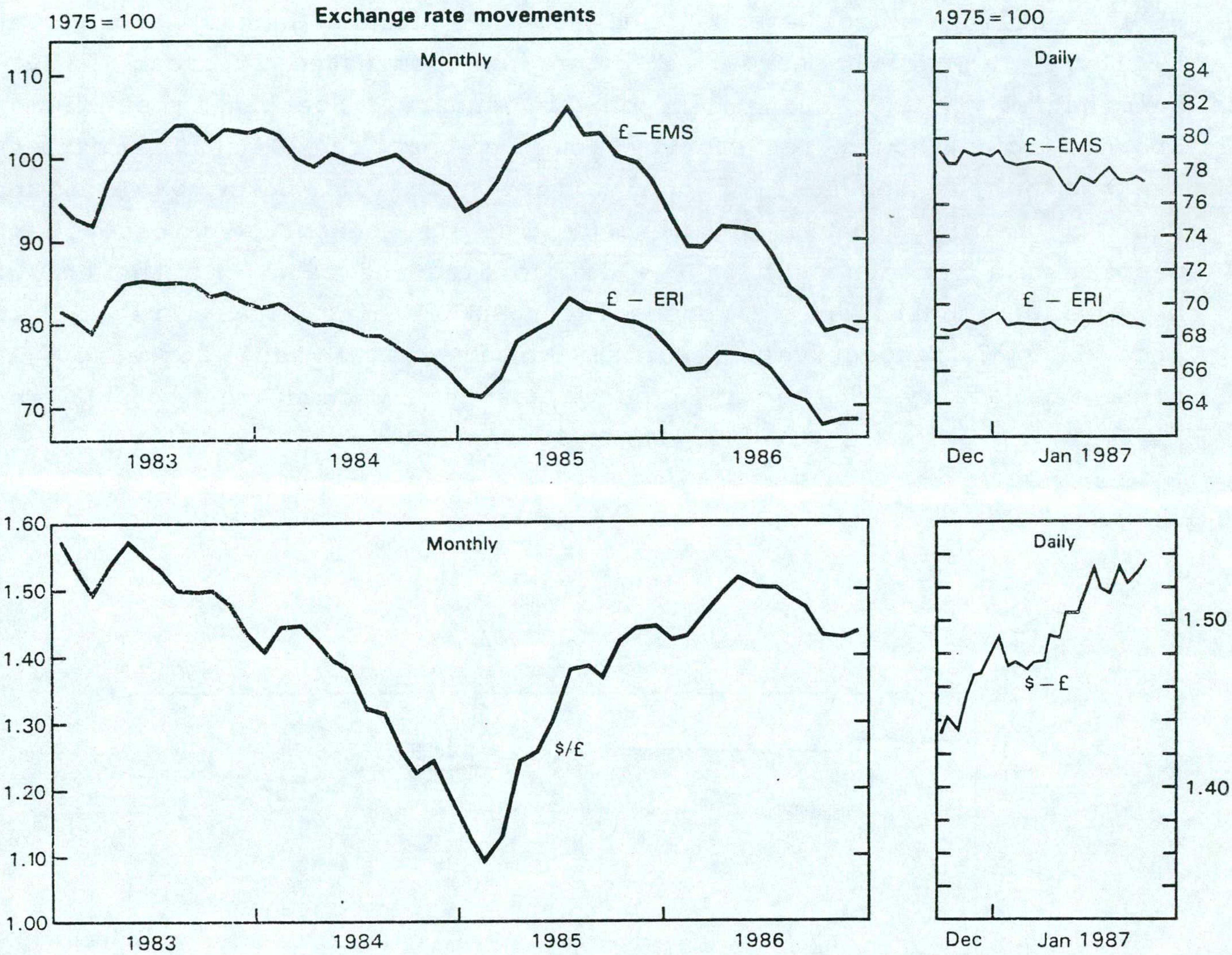
F3 Financial markets

F3.1 Sterling ended December and remained during January around the 69 level in effective terms. EMS tensions dominated European markets culminating in ERM realignment on 11 January. Sterling rose firmly above $1.50 (though registering lows against the DM). The markets centred on the weakness of the dollar which fell below DM 1.78 and Yen 150 mainly because of unencouraging US economic indicators and despite a ½ per cent cut in the German discount rate. At the end of December, 3 months and 12 months interbank lending rates were 11 9/32 and 11 5/32 respectively. During January rates have softened. At close on January 29 the yield curve was gently downward sloping from 11 1/16 at 3 months to 10 13/16 at 12 months.

Interest rate movements



1 For a long run of monthly data for this series and for 5 and 20 year gilts see Chart 5


1975=100
Exchange rate movements
Monthly
110
100
90
80
70
£—EMS
£ — ERI
1983
1984
1985
1986
1975=100
Daily
84
82
80
78
76
74
72
70
68
66
64
£—EMS
£ — ERI
Dec
Jan 1987
1.60
1.50
1.40
1.30
1.20
1.10
1.00
Monthly
$/£
1983
1984
1985
1986
Daily
1.50
1.40
$—£
Dec
Jan 1987

GROSS DOMESTIC PRODUCT: 1980 PRICES AND SEASONALLY ADJUSTED (figures in brackets are cso forecasts) (1)
TABLE 1

£bn, rounded to nearest £0.1 bn

	Consumers' expenditure	General government final consumption	Gross domestic fixed capital formation	Stock-building	Total domestic expenditure	Exports of goods and services	Imports of goods and services	Real resources for the balance of payments	Factor cost adjustment	Gross domestic product at factor cost
1985(2)	38.0	12.7	11.6	+ 0.2	62.5	18.3	17.7	+ 0.6	- 8.4	54.7
1986(2)	39.8	(13.0)	(11.7)	(+0.1)	(64.6)	(18.8)	(18.6)	(+0.2)	(-8.8)	(56.0)
1985 Q1	37.4	12.8	12.2	+ 0.1	62.5	18.2	17.7	+ 0.5	- 8.4	54.6
Q2	37.6	12.8	11.2	+ 0.4	61.9	18.6	17.5	+ 1.1	- 8.3	54.7
Q3	38.3	12.7	11.6	+ 0.1	62.7	18.0	17.4	+ 0.6	- 8.5	54.8
Q4	38.6	12.7	11.4	+ 0.1	62.9	18.4	18.0	+ 0.3	- 8.6	54.6
1986 Q1	39.0	12.8	11.8	+ 0.6	64.2	18.0	17.7	+ 0.2	- 8.5	55.9
Q2	39.6	13.0	11.4	- 0.1	63.9	18.7	18.1	+ 0.6	- 8.7	55.8
Q3	40.2	13.0	11.7	- 0.2	64.8	18.7	19.0	- 0.3	- 8.9	55.6
Q4	40.5	(13.0)	(11.8)	(+ 0.1)	(65.5)	(19.6)	(19.5)	(+0.1)	(-8.9)	(56.6)

Index numbers 1980=100

	GDP(E)	GDP(O)	GDP(I)	GDP(Average)	GDP(Average) coal strike adjusted (B)	% change same period on a year earlier (A)	(B)
1985	109.6	110.6	110.6	110.3	110.7	3.4	2.6
1986	(112.2)	(113.6)	(113.0)	(112.9)	(112.9)	(2.4)	(2.0)
1981 Q2(3)	98.6	98.0	97.9	98.2	98.2		
1985 Q1	109.4	109.6	109.3	109.4	110.7	3.3	4.0
Q2	109.7	110.7	111.6	110.7	111.0	4.7	3.5
Q3	109.8	110.7	111.1	110.5	110.5	3.3	1.8
Q4	109.5	111.6	110.6	110.6	110.6	2.4	1.0
1986 Q1	111.9	112.2	112.4	112.2	112.2	2.6	1.4
Q2	111.8	113.1	112.9	112.6	112.6	1.7	1.4
Q3	111.5	114.5	112.3	112.8	112.8	2.1	2.1
Q4*	(113.5)	(114.5)	(114.6)	(114.2)	(114.2)	(3.3)	(3.3)

(1) Entries in this table are latest estimates and are not necessarily the same as published figures.
(2) Quarterly averages
(3) Trough of cycle
***The forecasts for the GDP index measures are not intended to be more precise than the general statements in the text.**

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GROSS DOMESTIC PRODUCT: CURRENT PRICES AND SEASONALLY ADJUSTED (figures in brackets are CSO forecasts)(1)

TABLE 2

£bn, rounded to nearest £0.1 bn

	Income from employment: Total	Income from employment: Of which: wages and salaries and forces pay	North Sea oil profits	Other industrial and commercial company profits	Other factor incomes	GDP at factor cost (income-based)	Total final expenditure	GDP (expenditure based) at factor cost	GDP (expenditure based) at market prices
			(excluding stock appreciation)						
1985(2)	48.9	42.5	4.6	10.0	12.9	76.4	112.6	75.7	88.0
1986(2)	(52.7)	(45.9)	(2.1)	(11.3)	(14.1)	(80.2)	(118.6)	(79.6)	(93.4)
1985 Q1	47.4	41.1	5.3	9.2	12.0	73.8	111.6	73.9	85.5
Q2	48.5	42.1	4.9	9.9	12.9	76.1	111.9	74.8	87.0
Q3	49.4	42.9	4.0	10.5	13.2	77.1	112.4	76.3	88.8
Q4	50.3	43.7	4.2	10.6	13.4	78.5	114.6	77.7	90.6
1986 Q1	51.2	44.5	3.2	11.2	13.8	79.4	116.6	79.1	92.2
Q2	52.4	45.6	1.6	11.0	14.2	79.1	116.3	78.4	92.1
Q3	53.2	46.3	1.5	11.2	14.1	80.0	118.9	79.5	93.6
Q4	(54.2)	(47.2)	(2.0)	(11.9)	(14.2)	(82.2)	(122.5)	(81.5)	(95.8)

Index numbers 1980=100

	Money GDP (average GDP at market prices)	Implied index of total home costs
1985	153.6	138.4
1986	(163.1)	(142.2)
1985 Q1	148.5	135.4
Q2	152.3	136.8
Q3	155.1	139.2
Q4	158.7	142.2
1986 Q1	160.4	141.7
Q2	160.9	140.5
Q3	164.1	142.8
Q4	(167.2)	(143.9)

(1) Entries in this table are latest estimates and are not necessarily the same as published figures.

(2) Quarterly averages

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TABLE 3

SELECTED MONTHLY INDICATORS
(Figures in brackets are CSO forecasts)

	Average earnings		Prices				Industrial production				
			Producer								
	Whole economy	Manufacturing	Materials and fuel purchased	Home Sales (1)	Retail (1)	Retail sales volume	Total	Manufacturing	Unemployment(2) (Monthly changes)	Vacancies(3)	Employees in employment in manufacturing (Monthly changes)
	Jan 1980=100		1980=100	1980=100	Jan 1974=100	1980=100	1980=100		'000	'000	'000
1985	171.7	177.6	137.7	139.4	373.2	115.3	108.2	103.9	+ 6	162	- 3
1986	(185½)	(191)	126.5	(145.7)	385.9	121.3	(109½)	(104)	- 1	189	
1985 Oct	174.3	180.9	133.6	140.9	377.1	115.0	108.6	103.5	- 4	170	- 1
Nov	175.9	182.9	133.1	141.5	378.4	117.6	109.7	103.5	- 6	169	-14
Dec	178.1	184.7	132.2	141.9	378.9	117.4	107.1	103.9	+19	164	- 1
1986 Jan	179.1	185.5	131.5	142.7	379.7	117.3	108.6	102.6	+21	163	- 7
Feb	180.0	186.0	130.0	143.3	381.1	117.5	110.0	103.0	+ 3	167	-25
Mar	182.6	186.9	127.9	144.3	381.6	119.7	109.6	102.9	+33	170	- 7
Apr	185.3	191.1	126.4	145.4	385.3	119.3	110.7	104.0	+ 2	170	- 8
May	182.4	187.5	126.6	145.9	386.0	118.5	108.3	102.9	+ 5	172	-30
Jun	183.9	189.8	125.0	145.8	385.8	121.7	107.6	103.3	+14	184	-15
Jul	186.3	190.5	121.5	146.0	384.7	120.9	110.1	104.8	+ 4	193	-19
Aug	187.0	191.9	122.6	146.3	385.9	122.0	110.8	104.4	- 4	201	-15
Sep	187.1	194.0	124.7	146.7	387.8	123.2	111.0	105.5	-26	206	-
Oct	188.7	195.2	126.7	147.0	388.4	123.2	109.8	105.6	-26	213	-14
Nov	190.1	197.5	127.7	147.4	391.7	126.4	110.0	105.7	-21	215	- 8
Dec	(191)	(198½)	126.9	147.8	393.0	125.9	(108½)	(105½)	-28	210	
1987 Jan	(193)	(199½)	(126½)	(148½)	(394)	(124)	(110)	(106)			
Feb											
Mar											
Basis for assessing the present (ie the figures in brackets)	Effect of new pay settlements and short-term factors		Detailed assessment	Underlying trend	Detailed assessments	Continuing high level		Detailed assessments			

(1) Not seasonally adjusted

(2) New basis; excluding school leavers under 18 and adjusted for changes in coverage of the count.

(3) Unfilled vacancies at jobcentres, excluding Community Programme vacancies.

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TABLE 4

SELECTED MONTHLY INDICATORS
(Figures in brackets are CSO forecasts)(1)

	Volume 1980=100		Value			£ billion			MO (wide monetary base) £ billion (3)	Relative actual unit labour costs, including exchange rate movements (1980=100)
	Exports of goods (excluding oil and erratics)	Imports of goods (excluding oil and erratics)	Visible balance: Excl oil and erratics	Visible balance: Oil	Visible balance: Total inc erratics	Invisible balance(2)	Current balance total	Exchange rate Index (1975=100)		
1985	115	143	-11.0	+8.2	-2.1	+5.7	+3.5	78.2	14.4	87.7
1986	117	151	-14.4	+4.1	-8.7	+8.5	-0.2	72.8	(15.2)	
1985 Oct	112	144	-0.9	+0.8	–	+0.2	+0.2	80.4	14.1	)
Nov	114	150	-1.1	+0.6	-0.2	+0.2	–	80.0	14.2	) 91.1
Dec	117	146	-1.8	+0.5	-0.1	+0.4	+0.4	79.1	14.4	)
1986 Jan	109	138	-0.9	+0.9	+0.1	+1.0	+1.1	76.6	14.4	)
Feb	114	144	-1.1	+0.7	-0.4	+0.5	+0.2	74.2	14.4	) 86.7
Mar	111	150	-1.5	+0.4	-1.2	+0.5	-0.7	74.6	14.5	)
Apr	114	138	-0.9	+0.3	-0.3	+0.7	+0.4	76.2	14.4	)
May	116	147	-1.0	+0.2	-0.7	+0.7	-0.1	76.1	14.5	) 88.3
Jun	116	149	-1.1	+0.3	-0.6	+0.7	–	75.8	14.6	)
Jul	119	150	-1.1	+0.2	-0.6	+0.8	+0.1	74.0	14.6	
Aug	114	159	-1.7	+0.2	-1.5	+0.8	-0.8	71.4	14.7	
Sep	121	156	-1.2	+0.3	-0.9	+0.8	-0.1	70.4	14.8	
Oct	121	153	-1.1	+0.2	-0.8	(+0.8)	(–)	67.8	14.8	
Nov	127	168	-1.6	+0.3	-1.0	(+0.8)	(-0.2)	68.5	15.0	
Dec	127	161	-1.3	+0.3	-0.8	(+0.8)	(–)	68.5	(15.2)	
1987 Jan	(128)	(163)	(-1.4)	(+0.3)	(-1.0)	(+0.8)	(-0.2)	(68.9)		
Feb										
Mar										
Basis for assessing the present	Trend line					CSO projections		Actual data to 29 January		Recent trends in components

(1) Entries in this table are latest estimates and are not necessarily the same as published figures.
(2) Monthly figures are one-third of the quarterly total, except for EC budget refunds allocated to month of receipt.
(3) Average amount outstanding. Annual data relate to December.

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QUALITY NOTE

Retail Sales

To keep the trading year roughly in line with the calendar year, a 53 week trading year is necessary every 5 or 6 years, so the January 1986 trading month was exceptionally of 5 weeks. As mentioned previously this could lead to a somewhat more erratic series than usual because the 1986 trading periods are 6 calendar days later than the corresponding periods in 1985. A study of the seasonal adjustment of the retail sales index carried out in 1985 suggested no effect on the November 1986 index but an upward adjustment for December 1986 (which has been made).

A23/1 COPY NO 86

MONTHLY ECONOMIC BRIEF

Prepared by the CSO on 30 January 1987

Adult unemployment fell sharply again between November and December, the fifth consecutive monthly fall. It seems likely that even without Restart and other measures the previous upward trend would have been halted and possibly marginally reversed.

In December exports were little changed from November, while imports fell by 3½ per cent. Visible trade was in deficit by £0.8 billion, an improvement on the deficit of £1.0 billion in November. For 1986 as a whole, the current account was in broad balance - in line with the Autumn Statement forecast. The underlying levels of both non-oil export volume and non-oil import volume continue to rise.

The annual rate of inflation rose to 3.7 per cent in December from the 3.5 per cent recorded in November. In January a further small rise in the twelve-month rate may occur. During the first seven months of 1986 the price index for materials and fuel purchased by manufacturing industry continued the decline which began in March 1985. The index rose between August and November 1986 but has since fallen slightly, and is now some 4 per cent down on a year earlier and almost 13 per cent down on the 1985 peak.

Current projections suggest that GDP rose by 1 per cent between the third and fourth quarters of 1986 and continues to grow at a current underlying trend rate in the range 2-4 per cent per annum.

The PSBR is estimated to have been minus £1.4 billion in December, giving a cumulative total for the first nine months of 1986-87 of £4.4 billion. Outturns to date suggest that the PSBR is more likely to undershoot than overshoot the forecast of £7 billion for 1986-87 given in the Budget and the Autumn Statement.

Sterling has been around 69 in effective terms. It fell to 68.3 in the middle of the month but rose later, helped by the weakness in the US dollar.

RECENT RATES OF CHANGE AND ASSESSMENT OF CURRENT TREND FOR SOME KEY ECONOMIC INDICATORS

In the following notes, the figures for current trend represent our best assessment of the current underlying rate of increase after making allowance for temporary distorting factors such as strikes, unseasonal weather effects, etc. The figures show how the series are moving currently and may be different from the comparisons over the latest published twelve months.

GDP (average measure) in the third quarter of 1986 was 2 per cent higher than in the same period a year ago. This figure does not take account of past experience which shows that revisions to growth rates for the initial published estimates of GDP were on average, upwards, though not uniformly so. The assessment of current underlying trend for the fourth quarter of 1986 is that the rate of increase lies in the range 2-4 per cent per annum.

Industrial production in the three months to November 1986 was 1 per cent higher than in the same period a year ago; manufacturing output was 2 per cent higher. The assessment of underlying trend for industrial production is that the rate of change currently lies in the range ½ to 2½ per cent per annum. The trend in manufacturing output is in the range 1½ to 3½ per cent per annum.

Retail prices rose by a little over 3½ per cent in the twelve months to December 1986. It is only possible to provide a useful indicator of trend for about 70 per cent of the RPI, mainly that covering private sector prices and excluding eg mortgage interest, rent, rates, products produced by nationalised industries, seasonal food and petrol. The current trend for this series is just under 4 per cent per annum. In the twelve months to December 1986 this series rose by 4 per cent (not published).

Producer input prices fell by ½ per cent in seasonally adjusted terms in December after four months of increase, and will probably show some further decline in January. The index should be at least 4 per cent lower than in January 1986.

Average earnings (underlying) in the twelve months to November rose by 7½ per cent. The current trend is estimated to be 7½ per cent per annum.

Unit wage costs in manufacturing in the three months to November rose by 3 per cent compared with the same period a year ago. The current underlying trend is estimated to be in the range 2-4 per cent per annum.

Unemployment (excluding school leavers) in the twelve months to December has fallen on average by over 1,000 per month. The current trend continues downward at the rate of some 20,000 per month. There has been an average fall of over 17,000 per month in the past six months, and within this period, a fall of 25,000 per month in the past three months.

Movements over the latest published 12 months include any revisions that may have occurred since last publication (in general any such differences only occur in the GDP series).

CHART 1A

Gross domestic product (average measure)

1980 = 100, seasonally adjusted

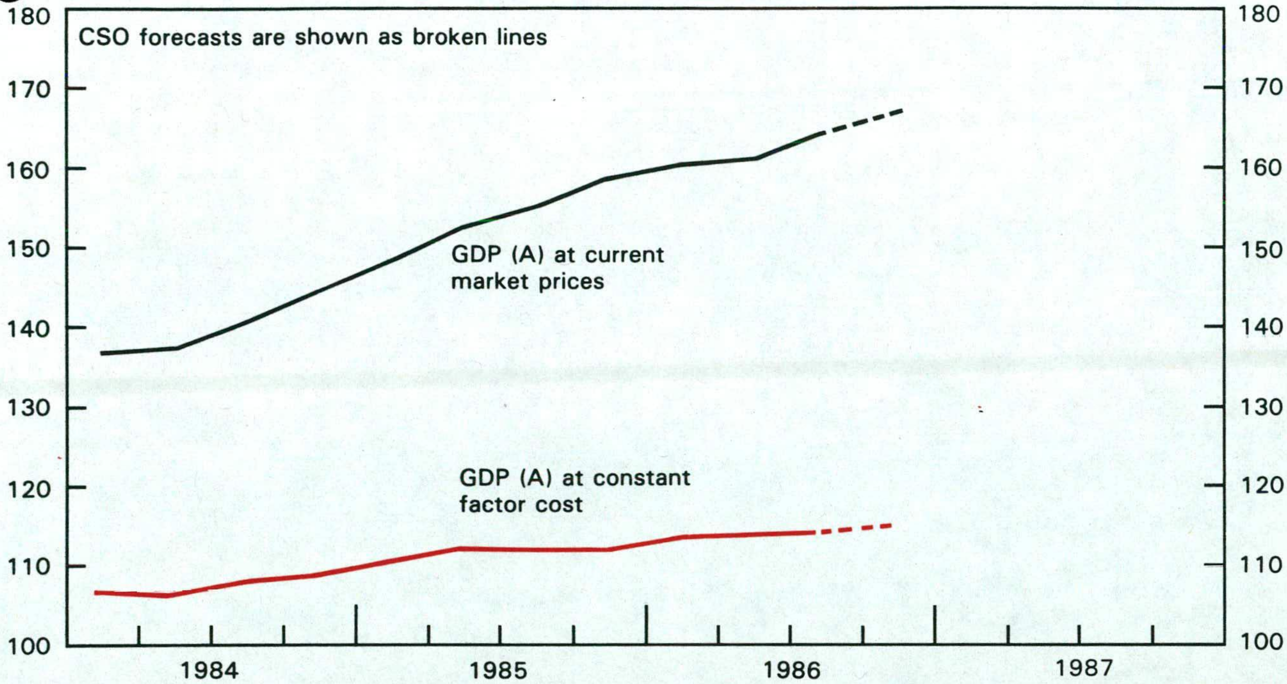


CHART 1B

Gross domestic product (average measure)

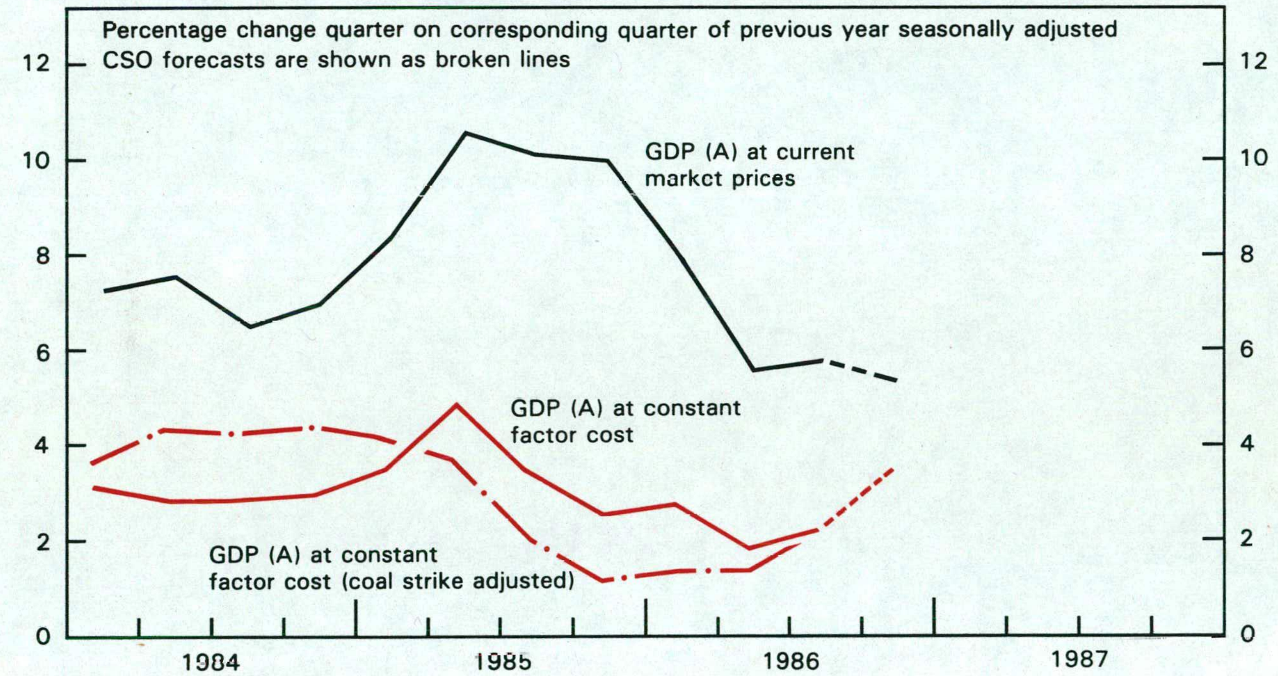
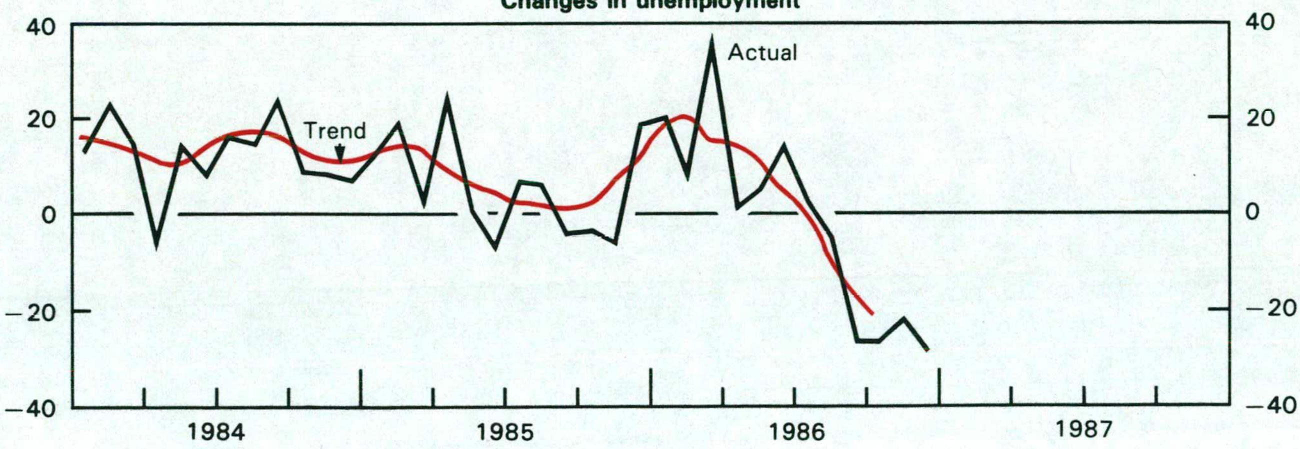


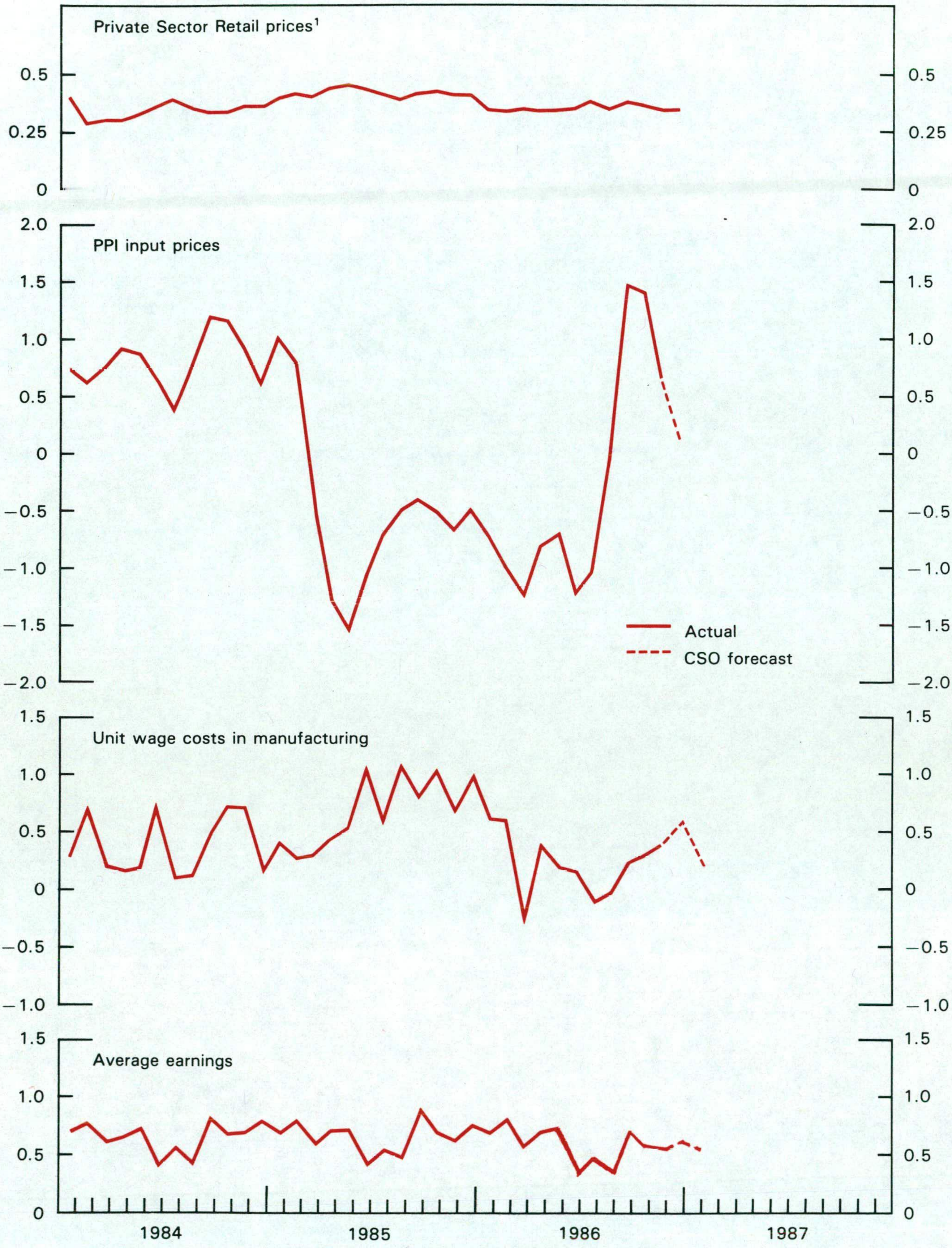
CHART 2

Changes in unemployment



Rate of increase in average earnings, unit wage cost in manufacturing PPI input prices and Private sector retail prices

Month to month percentage changes, smoothed and adjusted for distorting factors where appropriate



1. Excludes seasonal food, mortgage interest, rent, rates and water charges motor vehicle licences, products produced by Nationalised industries and petrol.

CHART 4

Movements in underlying average earnings and the tax and price index comparisons with 12 months previously

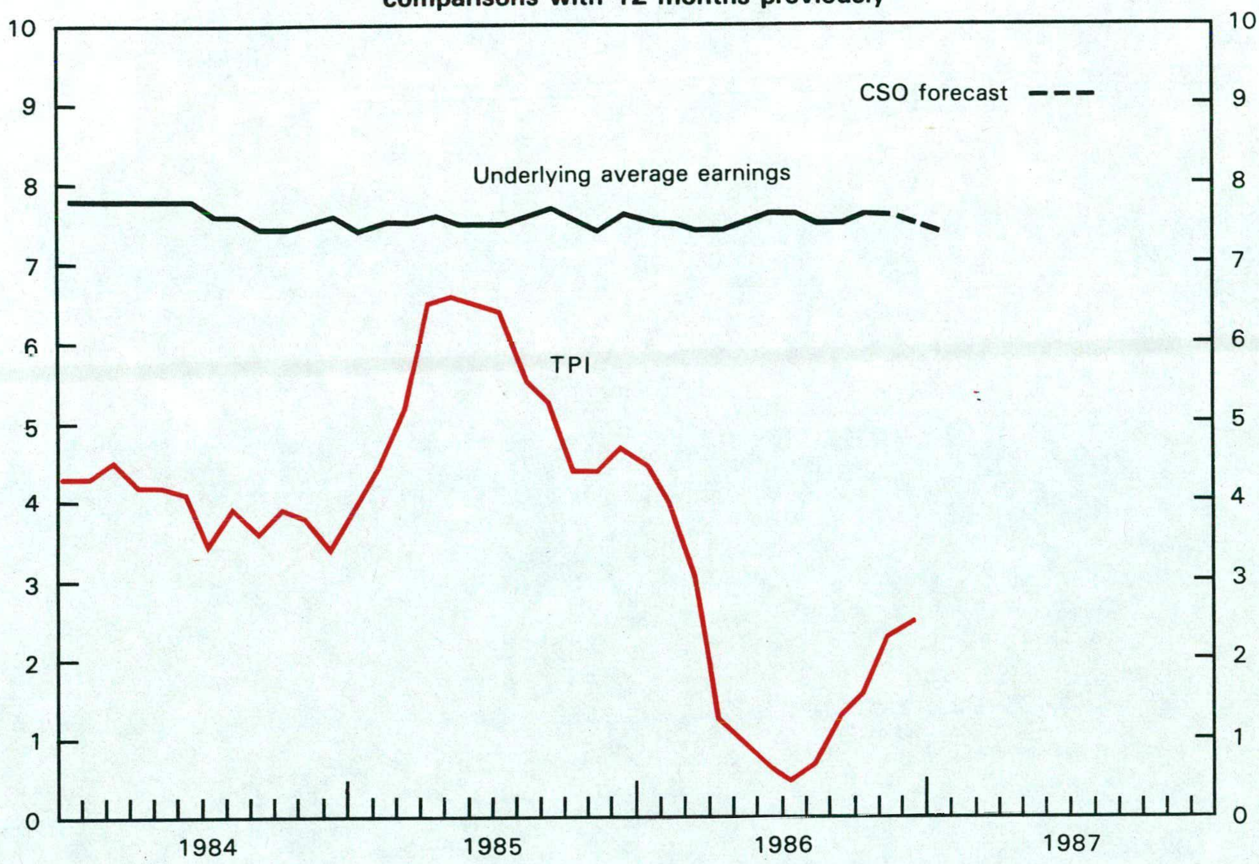


CHART 5

Interest rates

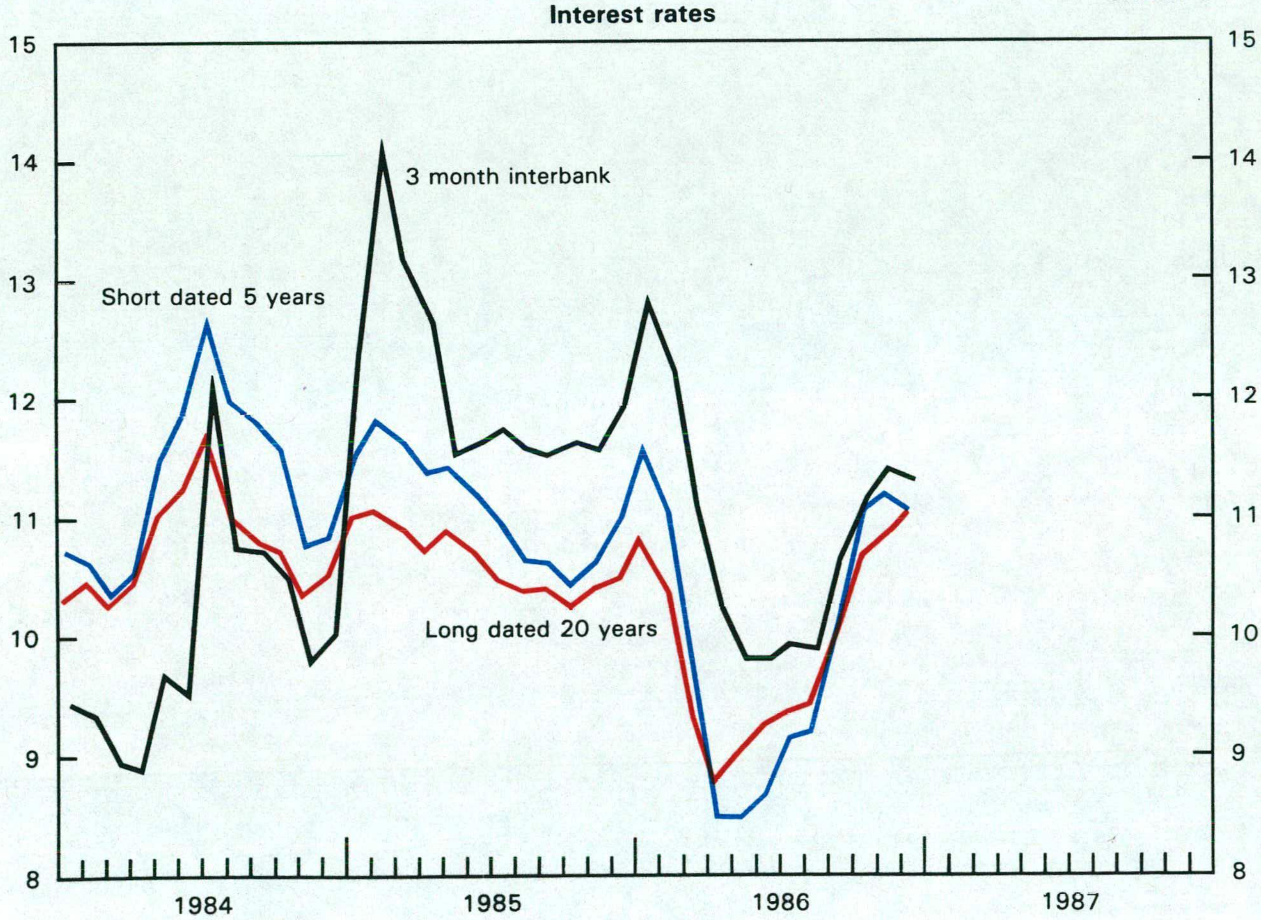
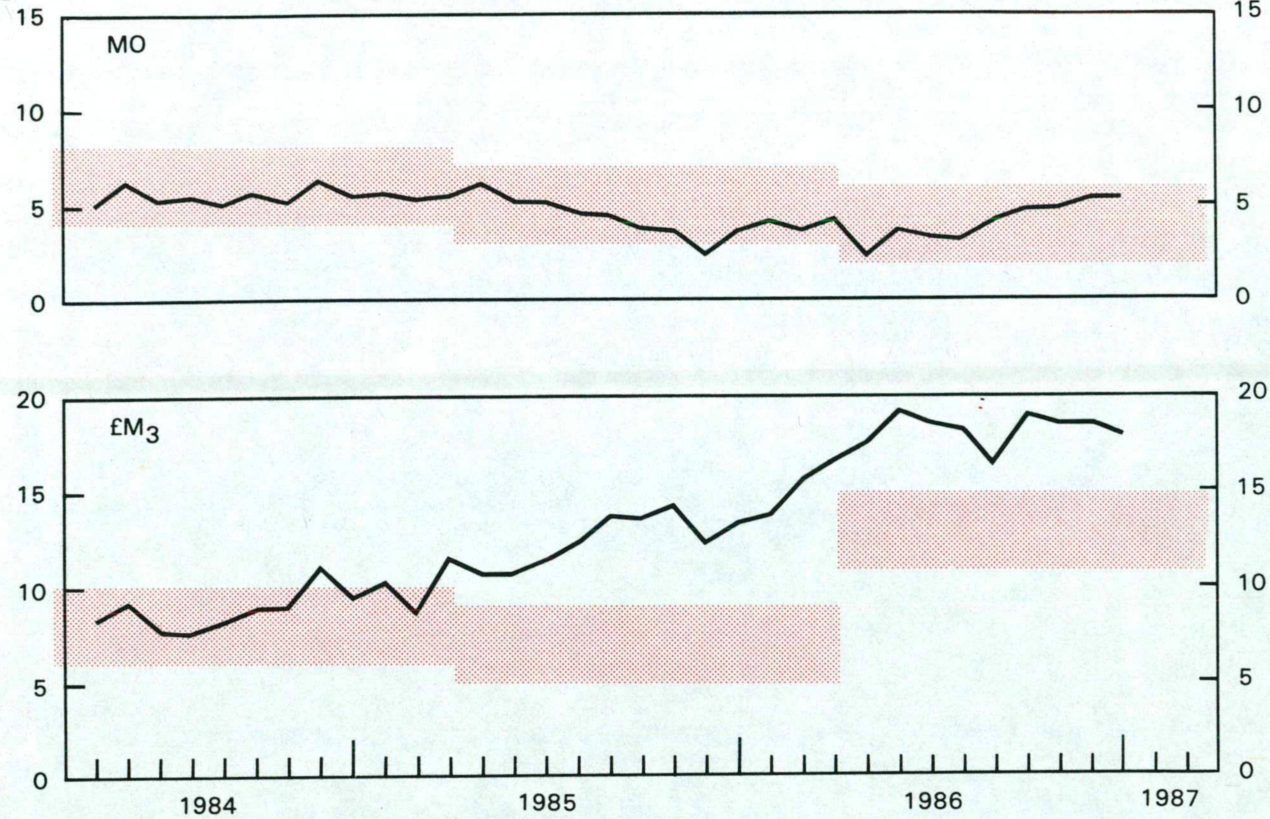


CHART 6

Monetary aggregates

Percentage Change on previous 12 months (not seasonally adjusted)

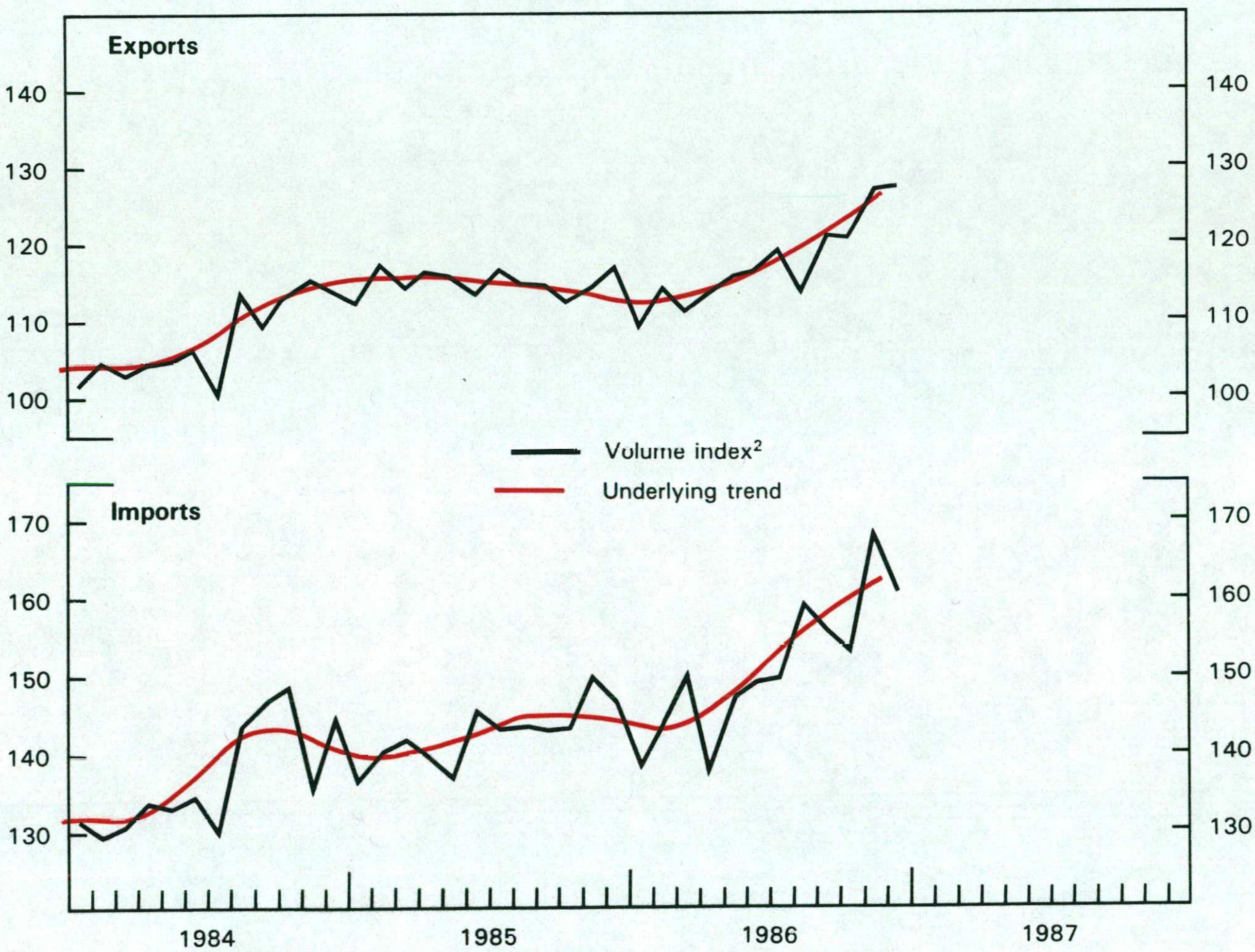


Shaded areas represent announced target ranges

CHART 7

Exports and Imports (excluding oil and erratics[1])

Index 1980 = 100



1. Ships, North Sea Installations, Aircraft, Precious Stones and Silver
2. Seasonally adjusted data, Balance of Payments basis

SECRET AND PERSONAL

FROM: A C S ALLAN
DATE: 30 January 1987

NOTE FOR THE RECORD: FORECAST

At the start of his bilateral at 5pm on 30 January, Sir P Middleton reported to the Chancellor his conversation with Brian Griffiths earlier that day about the forecast.

2. He reported that Griffiths had been worried about the growth in money GDP and inflation. He had also been concerned about the small balance of payments deficit. Sir P Middleton had made it clear that the MTFS would show a declining path money GDP, and had pointed out that it was very difficult for the Government to take any new initiatives to press down on inflation this year. He had asked Griffiths whether he would seriously suggest a PSBR of less than 1 per cent of GDP. He had pointed out that in market terms this would be seen to be a very prudent Budget, especially given the caution on tax revenues. Compared to the position we had been looking at 6 months ago, the policy stance was now very tight.

3. Sir P Middleton said he had suggested to Griffiths that the starting position should be a £4 billion PSBR and a £3 billion tax package. It might be possible to shade the tax package down a little, but certainly not below £2 billion. Griffiths seemed persuaded that a package of around £2½ billion might be appropriate, though it was difficult to know quite how he would brief the PM.

4. He had asked what reduction in the PSBR would be required to get 2 per cent off interest rates. Using Sir T Burns' rule of thumb, this would require a £4 billion PSBR <u>surplus</u>! And even a more modest cut could not produce any guarantee of lower interest rates, given the interaction with the exchange rate and with market confidence.

ACSA

A C S ALLAN

No distribution

ps2/25R

UNCLASSIFIED

FROM: CATHY RYDING

DATE: 28 January 1987

MR MOUNTFIELD

cc Chief Secretary
Economic Secretary
Sir P Middleton
Mr F E R Butler
Sir G Littler
Mr Lavelle
Mr Turnbull
Mr Scholar
Mrs Case
Mr Butler
Mr Culpin
Mr Bush
Mr Segal

ECGD: EXPORT FINANCE VEHICLES - FT, 28 JANUARY

The Chancellor was grateful for your minute of earlier today.

2. The Chancellor was not happy with the line for the press contained in your minute, and thinks he should have been consulted earlier. He thinks that the line should be:

> "There is no disagreement between the Treasury and the CSO. But the proposed reform of the UK's system of medium-term export credit finance raises a number of complex technical financial issues which have yet to be resolved."

3. The Chancellor also thinks that it would have been better not to tell the banks the reasons for the four months break in the margin negotiations.

CR

CATHY RYDING

1 Mrs Case - to see
2 PS/ Chancellor

I have passed on this revised formula to ECGD, CSO and Bank, who will use it if asked. I gather there have been no further questions.

RM
28 1

- Wells 6040
- Furrow 4667

2566/005

* Thanks. I do not approve this press line. Why wasn't I consulted? The line should be: "There is no disagreement between HMT & the CSO. Both sides agree the proposals upon the UK's system of export finance raise a number of complex technical issues which have yet to be resolved."

(PMP)

FROM: P MOUNTFIELD
DATE: 28 January 1987

CHANCELLOR

cc Chief Secretary
Economic Secretary
Sir P Middleton
Mr F E R Butler
Sir G Littler
Mr Lavelle
Mr Turnbull
Mr Scholar
Mrs Case o/r
Mr Butler
Mr Culpin
Mr Bush

Ch
I don't like the link between (b) & (c) below — what is holding things up now is not the statistical treatment, but the question whether we want new vehicles with liability side guarantees
AA

ECGD : EXPORT FINANCE VEHICLES - FT, 28 JANUARY

but presumably not that it had been settled!

We had been forewarned that this unhelpful piece would appear. The leak apparently came from one of the banks, who had been told in confidence of the reasons for the four month break in the margin negotiations. Shd not have been

Press Line

2. Before receiving Miss Ryding's note, there had already been press enquiries, and I had given Mr Segal a "line to take" as follows:

(a) confirm that there ~~[is a]~~ have been discussion[s] ~~[going on]~~ about the correct statistical treatment of these vehicles[;], which have now been resolved;

(b) ~~[almost resolved, and hope it willbe settled very shortly indeed;]~~

(c) discussions with the banks will resume ~~[quickly thereafter]~~ shortly.

Two of these vehicles have already been launched (?!), and we are considering the form in which future ones might be constructed;

I reported this to Sir P Middleton's office at the time.

3. I have suggested to the CSO, Bank of England and ECGD that they take the same line.

State of Play

4. The policy issue is, as you noted, now resolved. We have accepted the "CSO compromise" which Mr Hibbert worked out with Sir P Middleton. But there is one outstanding point - that raised by the Economic Secretary on 12 January. This concerned the need for "liability side guarantees" - the root of the problem. You agreed with Sir Peter Middleton that this should be sorted out before the question was finally resolved, and he commissioned a paper which Mr Bush has drafted and discussed with ECGD and the Bank of England. As soon as we have received their comments, this will be submitted - I hope, later this week. Provided you are satisfied with the explanations, discussions with the banks can then resume quite quickly; though we shall need to consult the Chief Secretary again on whether to make a revised offer in the hope of reaching a speedy settlement.

PM

P MOUNTFIELD

ps2/22R

UNCLASSIFIED

FROM: CATHY RYDING
DATE: 28 January 1987

MRS CASE

cc PS/Chief Secretary
PS/Economic Secretary
Sir P Middleton
Mr F E R Butler
Sir G Littler
Mr Lavelle
Mr Mountfield
Mr Turnbull
Mr Scholar
Mrs Butler
Mr Culpin
Mr Bush

ECGD: EXPORT FINANCE VEHICLES - FT, 28 JANUARY

I attach a cutting from today's FT.

2. The Chancellor would be grateful for an urgent note on this unhelpful piece. His understanding was that this had all been solved and agreed. Mr Culpin will also need a line to take.

CR

CATHY RYDING

FROM: MRS A F CASE
DATE: 29 January 1987

CHANCELLOR

Any views from CST?

cc Chief Secretary
Economic Secretary
Sir P Middleton
Sir G Littler
Mr Butler
Mr Lavelle
Mrs Lomax
Mr Mountfield
Mr Peretz
Mr Kelly
Mr Hall
Mr Bush

ECGD GUARANTEED VEHICLES

In the light of the Economic Secretary's suggestion that the benefits of securitisation were already available to the banks and that an extension of ECGD's guarantee was not therefore required (Mr Barnes' minute of 12 January), you asked for further advice on three issues:-

(i) why it is necessary to carry out capital market financing of export credit through specially constituted vehicles;

(ii) the need for such vehicles to have a liability side guarantee rather than simply an asset side one;

(ii) who benefits from the savings in interest payments.

2. The paper below (prepared in consultation with the Bank of England and ECGD) argues that

(i) the vehicles provide the most efficient means of accessing the capital markets since the banks would be unwilling to use their own balance sheets for this purpose and, even if they could be persuaded to do so, they would demand remuneration which would eliminate most of the interest savings;

(iii) a liability side guarantee is the only basis for possible exemption under the Banking Act. This was raised with the Economic Secretary 18 months ago in the Guangdong context when he asked whether such vehicles could take advantage of existing exemptions. The answer is that they cannot and, without an exemption, the frequency with which the vehicles could go to the market would be limited and their flexibility - and hence utility - would be seriously constrained. Again this would reduce the interest savings;

(iii) a liability side guarantee also improves the terms the vehicles will command in the market, and hence the interest savings. None of these savings would accrue to the banks. Except in the very limited case of "pure cover" (which improves the exporters' competitive position), all of the savings accrue to the Exchequer. Bodies with asset side government guarantees would trade at less fine terms and potentially compromise HMG's name in the market.

3. In considering these arguments it is worth bearing in mind that the capital market issues involved could be quite significant since they could encompass in addition to new fixed rate export finance (£200 million per annum assuming 30% were refinanced), the existing stock of fixed rate export finance (say £500 million plus a year) and Paris Club debt restructurings (possibly between £300-500 million a year but individual tranches could be higher - Nigerian refinancing alone could be in excess of £½ billion in 1987-88).

Conclusion

4. In the light of the arguments above, we judge that vehicles with a liability side guarantee and an exemption from the Banking Act provide the most efficient way of accessing the capital markets and securing the largest savings for the Exchequer, whilst, at the same time, protecting HMG's other interests.

AFC

MRS A F CASE

PR

SECRET

Mam. Rank. Most helpful. Keep them

FROM: F. E. R. BUTLER
29th January, 1987.

DS, Can you attach the other notes summary pegged up (after these). I will then deal with them this afternoon

SIR PETER MIDDLETON

c.c. Mr. Scholar (without enclosures)

POLICY PROPOSALS

I attach notes on all the policy proposals attached to Mr. Saunders' minute of 16th January except (vi) (a), (b), (c) which are being covered by Mr. Scholar. The notes refer to the Chief Secretary because my cover story was that the Chief Secretary had raised these ideas and had asked for my comments at our next bilateral. This seems to have been successful as a cover story, although I gather that the rumour went round that the Chief Secretary and I must be losing our grip! — see eg Gill N note below

2. Short summaries of the points are:-

(i) Removing entitlement to benefit from able-bodied people under 18 who are entitled to YTS This would be expensive because it would create extra demand for YTS, which is three times more expensive than supplementary benefit but DE will bring forward further proposals in 1987.

(ii)(a) Extending the concept of family credits to the single unemployed The family credits approach would mean giving a universal benefit to single people in work. It would therefore be very expensive and extend the benefit culture. It would be better from both points of view to cut out of work benefits.

(b) Making national insurance contribution levels help the poor not the rich We interpret this as making employees' contributions more progressive. At some level this must produce higher marginal rates, and that is why the Chancellor ruled it out in the 1985 Budget speech.

(iii) Study further the public expenditure trap whereby rent deregulation leads to increased payments of housing benefit Higher rents will always lead to more housing benefit, but I take it that this refers to the anomaly that for housing authorities in surplus the higher rent income is not offset against higher expenditure on housing benefit, with the result that raising rents increases public expenditure. This is mainly an accounting problem which does need looking at. Last summer we proposed solving it through setting up housing capital funds and now propose to pursue it in the review of controls of local authority capital expenditure and borrowing.

(iv) Regional development agencies for the English regions Without substantial machinery of government changes it would be difficult to reproduce in England the advantage of the SDA and WDA that all the statutory functions come under a single Minister. Without this, regional development authorities would be an extra layer of bureaucracy. Multiplying them would also make it difficult to get people of the necessary calibre and would certainly raise expenditure.

(v) Giving the MMC a specific remit to consider regional employment considerations The MMC is already required to have regard to the desirability "of maintaining and promoting the balanced distribution of industry and employment in the United Kingdom". The review of competition policy is considering whether the public interest criterion should be narrowed or made more precise but Mr. Monck's feeling is that regional factors are already given a sufficient place.

(vii) Regionally determined ceilings on housing benefit Since rents vary not only with regions but size and type of property, they would either have to be set on an individual basis, which would be a bureaucratic nightmare, or so high that they would have no effect. A better approach might be to put limits on the central government subsidy to local authorities in respect of benefit, which could be more by and large.

(viii) 30 per cent grants to housing associations for flat sharing schemes to deal with homelessness A scheme of this sort involving a 30 per cent grant through housing associations has been agreed between the Treasury and the DOE.

No

I think this is different — ie allowing losses on renting to be offset against other income

(ix) Sideways tax relief for the private rental sector This is covered in Mr. Ridley's housing policy review on which we will be commenting separately.

(x) Making local authorities responsible for paying part of housing benefit out of rent receipts There is much to be said for this but it would be fiercely resisted by housing authorities.

F.E.R.B.

F. E. R. BUTLER

Secretary of State for Trade and Industry

DEPARTMENT OF TRADE AND INDUSTRY
1-19 VICTORIA STREET
LONDON SW1H 0ET
Telephone (Direct dialling) 01-215) 5422
GTN 215) ....
(Switchboard) 01-215 7877

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30 January 1987

Rt Hon Nigel Lawson MP
Chancellor of the Exchequer
HM Treasury
Parliament Street
London SW1P 3AG

CH/EXCHEQUER
REC. 02 FEB 1987
ACTION CST 30/1
COPIES TO

Dear Nigel,

CONVERSION OF ANKARA TO NATURAL GAS : ATP SOFT LOAN

AMEC International Construction Ltd have for some time been pursuing a contract to convert Ankara to natural gas. This is an important contract, likely to involve some £60 million or so of UK exports and to serve as a reference for further conversion work both in Turkey and in other overseas markets. The prospects of obtaining this contract for the UK, however, depend upon our willingness to deploy an ATP soft loan to which, I understand, your officials are opposed.

This opportunity has been carefully cultivated for some time. British Gas undertook the feasibility and initial planning study for the project. They are now due to present a subsequent design implementation study to the Turkish client (the Ankara Gas Authority). A team from the Corporation is due in Turkey on 9 February. They will be accompanied by representatives from AMEC and the opportunity will be taken further to pursue a negotiated turnkey contract.

Given competitive financing, we believe AMEC to be well placed. I understand that a separate study of the project, undertaken by British Gas and funded by ODA, confirms its economic viability. But we must move very quickly if we are to capitalise upon our leading position. Our competitors - the Italians, Danes, Germans and French - are already offering soft loan support for gas or other projects. There are rumours that the Italians are prepared to offer highly concessional finance for this project (ECGD are checking whether an offer has been made).

JG4ALP

I am well aware of the tight ECGD cover position in Turkey and the fact that, if it proceeds, this contract will utilise more than half of that which is currently available. Nevertheless, I am convinced we should be prepared to offer support for the following reasons. First, the industrial and commercial case is very strong. I have referred above to the wider market opportunities which will arise from this important project. If we were to win this contract it would be breakthrough for the UK generally in major project work in Turkey.

Industrially, the contract will involve important business for UK suppliers of pipes, valve fittings, conversion kits etc, at a time of reduced demand in the domestic UK market.

Second, the case has very much wider political importance. This is summed up by Post's recent comment that:

> "if we mean to continue to take the market seriously and to demonstrate this intention to the Turkish Government we shall have, on occasions, to be ready to offer fully competitive financial support. The Ankara Gas Project with its high profile is of sufficient importance both for British industry and for the development of our commercial stake ... to continue to recommend that a soft loan be authorised."

To fail to give the necessary support to AMEC, therefore, would not only be a set-back to their and British Gas' long term efforts to gain a presence in the Turkish market, but would have much wider commercial implications. We can be sure that our competitors are ready to take full advantage if we falter.

Finally, I am convinced that we must offer ATP support in soft loan form. Although, when this case was considered by officials last year, there was agreement on a mixed credit (subject to the findings of the ODA funded study), it has become clear in the intervening months that we have to offer soft loan terms if we are serious about this business. The Turkish customer, central authorities, the Post, AMEC and British Gas have all indicated that it is the ATP route we need to follow. It is clearly a case where a soft loan would be more effective, on all the evidence, than a mixed credit, and we should not shrink from using the appropriate instrument available to us.

JG4ALP

For all these reasons, I propose that we should be prepared to support the AMEC bid for a negotiated contract for the Ankara Natural Gas Conversion project. The financing terms proposed (15 years maturity, 5 years grace period, 2 percent per annum interest) have been designed to minimise the call on ECGD cover and would, indeed, have a lower Departmental Maximum Liability than a mixed credit. They would also just conform with OECD minimum concessionality requirements and, Post believes, should be acceptable to the Turks.

We need to move quickly. The Turks are expecting an indication of HMG's position (although a formal notification is obviously subject to OECD prior notification requirements). Unless we can give this, to coincide with the British Gas/AMEC presentations, we shall have lost an important opportunity. I would ask therefore that we reach a decision by Friday 6 February.

I am copying this letter to EX colleagues and to the Secretary of State for Energy.

Yours,

Paul

PAUL CHANNON

JG4ALP