SECRET

TELEPHONE
01 - 601 4444

BANK OF ENGLAND
LONDON EC2R 8AH

10 October 1980

The Rt Hon Margaret Thatcher MP
10 Downing Street
London
SW1

My dear Prime Minister

In the hope that it would be useful ahead of the meeting you are holding on Monday afternoon, I enclose a memorandum prepared in the Bank. This begins by briefly reviewing recent experience with monetary policy and the money supply and indicates the lessons we feel can be drawn from this experience. It goes on to consider, in the light of an annex on the Bank's current forecast for the economy, the problems now facing us in the implementation of monetary policy in the coming months. The memorandum concludes with a discussion, drawing on our own analysis and the recent consultations, of the possibilities of changing our techniques of monetary control.

We have taken the questions in this order because, whatever may be the attractions of some form of monetary base control, its adoption would necessarily involve a long transitional period before we knew enough about the way in which the new system worked to be able to exert meaningful control.

On the other hand, I believe that the immediate situation faces us with policy dilemmas of a particularly acute and urgent kind which we shall need to resolve.

Yours sincerely

Gordon Richardson

MONETARY POLICY: THE MAIN ISSUES

1 Recent developments.

Both Bank and Treasury officials have carried the analysis of recent monetary statistics as far as is possible with the data at present available. They have reached broadly similar conclusions as follows:

(a) The corset seriously distorted the monetary statistics, both while it was in effect in the two years to June, and following its removal. One form of distortion - the commercial bill leak - could be directly observed and more or less precisely measured; other distortions could not be quantified at the time, nor can they be now. The Chancellor, of course, drew attention to the problem of these distortions in announcing the ending of the corset.

(b) But making such allowance as we can for corset effects, the "underlying" rate of growth of £M3 accelerated sharply in the late spring and summer to well outside the target range. (It will be recalled that this followed a period in which monetary growth had moderated for a time around the turn of the year, when the PSBR temporarily improved while heavy funding continued.)

(c) The acceleration in underlying monetary growth in the spring resulted largely from a resurgence in the PSBR. In the first half of the financial year this is thought to have been running at an annual rate of over £15 bn., which was not only much greater than had been expected but larger than could be financed outside the banking system from the capital market despite continuing heavy gilt sales to domestic non-banks (at an average annual rate of nearly £9 bn.). At the same time net external outflows from the private sector - which exercise a contractionary effect on monetary growth - tended to diminish as the current account went into surplus.

(d) These factors were superimposed upon persistently very strong demand for bank credit from the private sector. The vast bulk of private sector borrowing has been undertaken by industrial and commercial companies, reflecting the size of the continuing company sector deficit and the effective absence of alternative sources of finance. Increasingly, since the recession really began to bite in April, a proportion of this borrowing has been undertaken simply to maintain the substance of the business intact. Personal sector borrowing for consumption has been only just over 10% of total private sector borrowing over the year to mid-August, and - taking account of seasonal influences - showed no acceleration in the latest three months.

As a result of these developments the recorded increase in £M3 from mid-February (the beginning of the target period) to mid-September was some 13%. Our best estimate is that underlying £M3 during this period may have risen by about 10%. It should be remarked that this latter figure, taken together with the present forecast (which may of course be highly fallible) of monetary growth to next April, could mean an annual rate over the present target period as a whole of around 12% in underlying £M3, compared with the 7-11% target.

Most of the available evidence apart from £M3 - the performance of the exchange rate and the current account, the improvement in inflation, the stability in housing and other asset prices, the sharp decline in company profits, in output and in employment, and the fact that M1 has risen at a rate of only 8 1/2% since February or 6 1/2% since June last year - strongly suggests that policy has been and remains very restrictive. In particular, interest rates have now become substantially positive in real terms, because of the slow-down in the current and prospective rate of inflation, where, even with 17% MLR, they were negative earlier in the year. The current tax position of many companies will also add to the real burden of interest rates.

Taking all the evidence, we conclude that monetary policy has indeed been severe. The money supply target was originally chosen on the basis of assumptions that in certain crucial respects turned out to be wrong. The PSBR has persistently tended to exceed the forecasts. Wage increases last winter were much higher - in both public and private sectors - than was forecast. Despite the recent overshoot of £M3, the pressure on the company sector and the rise in unemployment indicate that these wage increases have not been validated by monetary policy. The exchange rate and interest rates have also been higher for longer than expected. The effect of these developments has been to put industry, and particularly that large part of manufacturing industry which is exposed to foreign competition, under disproportionate financial pressure. More generally, these developments have added to the financial imbalances within the economy, with large deficits in both public and corporate sectors matched by a massive personal sector surplus.

It was against these tensions, involving in particular the intermediation of the banking system between the corporate and personal sectors, that £M3 overshot during the spring and summer. Given the plight of the corporate sector, bank lending has been more than usually insensitive to the level of interest rates; and the recent size and volatility of the PSBR would have been difficult to handle in any circumstances.

One lesson from this might be that £M3 is not the appropriate target aggregate, and certainly in the light of the recent experience a number of outside commentators have re-raised this question. £M3 has its advantages: the ability to analyse it in terms of its credit counterparts is helpful to understanding the factors that underlie monetary growth; but £M3 is very difficult to control in the short run. However, all the alternative aggregates have their own drawbacks; and in any case we see no practical possibility of abandoning £M3 in the present circumstances. The real lessons - which both the outside commentators and we ourselves have repeatedly stressed in the past - are that we need to avoid focussing too narrowly on any single aggregate and that we cannot hope for precise control over £M3 - or any other aggregate - over short periods.

A further general lesson from the recent experience of the corset, and from our earlier experience with quantitative lending ceilings, is that we need to be deeply sceptical of the value of direct controls of any kind.

Against that background the questions we now need to concern ourselves with are:

(i) what steps need to be taken to manage the immediate situation; and

(ii) should our system of monetary control be changed?

2 Management of the immediate situation

(i) General considerations

The monetary figures for banking September, which suggest in particular that private sector loan demand may be beginning to ease, are reasonably encouraging, and there is a possibility that £M3 will grow more slowly for a time, especially after the turn of the year. The Bank's recent forecast suggests an annual rate of growth of 8% in the next six months. This however depends upon an expectation that the PSBR will be substantially lower than so far in this financial year (though it would still then be over £10 1/2 bn. for the financial year as a whole). But in the following year the PSBR rises in the forecast to £11 1/4 bn. so that the possibility of continuing moderate £M3 growth would depend upon sustaining a high level of debt sales and upon a further decline in the rate of bank lending to the private sector. At the same time the prospects for the economy are for a continuing decline in output, particularly manufacturing output, with unemployment rising close to 3 mn. by end 1982. Inflation falls to some 12 1/2% next year but only slowly thereafter. This forecast is described more fully in a separate paper.

All forecasts are hazardous and how much one should make of them is of course a matter of judgment. Nevertheless the general picture suggested for the development of the real economy may be realistic, bearing in mind the huge and continuing erosion of competitiveness in manufacturing, which will limit the extent to which we benefit from any upturn in the world economy. On the monetary side, provided the expected slowdown in the PSBR in the rest of this financial year occurs, and with the help of the new National Savings from November and of some falling off in the private sector's demand for bank credit, it seems possible that - as last year - £M3 growth will moderate into the spring. But we cannot be at all confident that we will be able to avoid a renewed acceleration as the PSBR picks up, just as there has been this year.

The problem for policy against this prospect is to preserve the effectiveness of the monetary strategy at a time when it is urgently necessary to ease the disproportionate pressure on manufacturing industry.

(ii) The roll-over

The dilemma crystallises first in the decision that must shortly be taken on the roll-over of the monetary target. There are three broad approaches:

(a) To attempt to claw back over the next 6-12 months the whole of the ground lost during the summer, including the effect of post-corset reintermediation. This would involve £M3 growth from now on at well below what is suggested by the forecasts and would certainly imply a sharp tightening of policy;

(b) The other extreme would be to start afresh with a new target for a 7-11% or perhaps 6-10% rate. This would impair credibility. At the same time some in the financial markets, and some economic commentators more generally, are impressed by the other evidence of monetary stringency and, although there would no doubt be criticism, the blow to credibility need not be fatal. Even this course would allow little scope for any significant easing of the pressures on manufacturing companies without a shift in the balance of policy within the monetary target.

(c) In between we might allow only that part of the base drift which can be attributed to the unwinding of distortions that occurred before February (ie outside the present target period) or before some earlier date eg last October. Such a calculation would be necessarily somewhat arbitrary because of the measurement problem referred to earlier; nevertheless, given the expectation among some commentators that we may adopt the approach in (b), it might be seen as a substantial effort to recover lost ground. This approach could allow £M3 growth of at most 8-9% a year over the coming 6-12 months

Public credibility of the strategy will depend only partly on the target chosen: it will depend at least as much on the conviction that the target can be achieved without imposing intolerable strains on the economy. This again poses a dilemma for policy. Avoidance of such strains would seem to require an early and substantial reduction in interest rates both to ease directly the pressures on the corporate sector and as probably the most effective means of moderating the strength of the exchange rate. We are not confident that there would be much room for a shift in this direction even with the most liberal of the options for the monetary target mentioned above.

(iii) The PSBR

Action to reduce the PSBR could help to square this circle if ways can be found of doing so that do not add too directly to the recession. At this stage it is more important to agree upon the outline of the strategy than its detail. But it is clearly important to hold down public expenditure which is not directly induced by the recession - and, within this, public sector wages in particular. Beyond this, the scope for raising revenue from those sectors of the economy that have been least affected by the squeeze (ie primarily the personal sector, but perhaps also from North Sea oil companies if ways could found which had a meaningful impact on monetary

growth) needs to be closely considered. The more that can be done in these areas the greater the scope for attaining a tight money target with lower nominal interest rates.

(iv) Corporate sector financing and the Bank's assistance to the banking system

The problems of monetary management are also being aggravated by the persistent strong demand from the company sector for bank credit. We cannot rely upon a sufficient decline in such credit demand - so long as the company sector deficit continues at its recent level and so long as there are no effective alternative sources of finance available to companies. If, in this situation, monetary policy were tightened and interest rates allowed to rise, this would add to the upward pressure on the exchange rate, and intensify company cutbacks and liquidations. Banks themselves could then become increasingly concerned over the security of their lending and its implications for their own position. The overall effect would be to steepen, perhaps abruptly, the fall in output and employment. At present levels of real interest rates borrowing by the corporate sector is in some large part borrowing to sustain the business. The pattern of financing of the public and corporate sectors has drained reserve assets from the banking system thereby generating upward pressure on interest rates. This the Bank has relieved by giving special assistance in various forms, including up to £1 1/4 bn.through its gilt purchase and resale operations - an amount that remains outstanding. If interest rates are to be prevented from rising we have no alternative but to continue to provide such relief - and we may well need to increase the amount outstanding during the revenue quarter early next year.

The difficulty could be eased if it were possible by fiscal means to reduce the company sector deficit. But the PSBR constraint clearly limits what can be done in this way. An alternative is to seek to divert some of the company sector borrowing from the banks into the capital market. It would also help to achieve this if

the demands on the gilt market can be reduced by containing the PSBR, and by financing more of it through National Savings, so that downward pressure can be brought on long-term interest rates. It may also help if the company debenture market could be stimulated by the temporary offer of an interest subsidy to the borrowers: the Bank have put detailed proposals to the Treasury for a scheme of this kind which we believe could be worth trying. A further possiblity is to encourage companies worried about a future fall in long-term rates to issue indexed debt. This would not suffer some of the drawbacks of the government itself issuing marketable indexed stock: for example, because of the difference in credit standing, and in size, company borrowing would not risk attracting a mass of OPEC funds which would push the exchange rate up further. A merchant bank has recently approached us about the possibility of issuing indexed corporate debt and we have indicated that we would have no objection in principle to such issues. A major deterrent at present, however, is the Corporation Tax treatment of the write-up in the nominal value of the debt: we would hope that this deterrent could be removed. Again, the more that could be achieved in these ways the easier it will become to combine a restrictive £M3 target with significantly lower short-term interest rates.

To sum up the Bank's views on immediate policy:

- We are acutely conscious of the present and prospective strains imposed on the manufacturing sector by monetary policy. To ease those strains would require a cut in short-term interest rates both for its own sake and as the most likely means of moderating the exchange rate. But the dilemma is how a meaningful move can be made unless the other constraints on policy can be eased through appropriate additional action on the PSBR and the adoption of a less rather than more restrictive monetary target within the limits described earlier.

- We think that greater attempts should be made to stimulate the private capital market by further initiatives on National Savings as soon as this can sensibly be done and by interest subsidies and tax changes to encourage long-term company borrowing.

3 The system of monetary control

The far-reaching changes that have been suggested in our system of monetary control could not be implemented sufficiently quickly to affect decisions on the immediate policy issues, but we need now to resolve the broad lines of approach to the system of control.

Both before and after publication of the Green Paper the monetary base debate has produced a welter of often diametrically opposed views, often obscured by complex points of detail. Cutting this tangled undergrowth aside some fairly clear conclusions have emerged.

Two general points are perhaps worth making at the outset. First, it was generally agreed in the consultations that any of the arrangements discussed below would involve moving away from £M3 to some other monetary target. Secondly, at least for an initial period - which might be prolonged - there would be much larger fluctuations in interest rates, which would be difficult to present and explain to the general public. It should be noted in passing also that the proposed arrangements would not be compatible with our membership of EMS, if that is to remain a policy option.

There are only two sets of monetary base proposals that have real coherence or substantial support.

(i) A non-mandatory monetary base system

The first is the pure, non-mandatory, system put forward by Brunner, Meltzer and Pierce at the recent seminar with foreign academics and supported in this country by Griffiths and Minford. It rests on the propositions that:

(a) the one thing a central bank can control with tolerable precision in the short run is the quantity of its own liabilities which form the base;

(b) if free to choose the amount of base money which they hold, banks will establish a desired relationship between their holdings of base and their total liabilities, which will be reasonably stable in the medium-term (say over 2-3 years).

They specifically do not argue that controlling the base will provide shorter-run control over any particular monetary aggregate and are not concerned that it should: their view is that by holding on to the base a central bank can be sure that none of the monetary aggregates - or inflation itself - can run seriously out of control (at least for any length of time).

This approach has intellectual attraction. Provided it is accepted that short-term interest rates should be allowed to fluctuate freely, without any restrictions, we would broadly accept the proposition at (a) - though in practice the degree of precision with which the base could be controlled is certainly rather less than some of the academics would allow. We simply do not know, however, whether the proposition in (b) is true, or would become true after the system had been allowed to evolve: it is untried in a financial system as complex as ours and in this sense it is a leap in the dark. But, if it were true then targetting and controlling the base would have advantages over targetting and controlling any particular monetary aggregate, given the real conceptual difficulty of selecting an appropriate single aggregate, and the practical difficulties of controlling it necessarily indirectly.

What did emerge fairly clearly from the consultations in relation to (b) is that, if a reasonably stable medium-term relationship between base asset holdings and the money supply (however defined) did emerge, it would not be because banks' behaviour would change dramatically so that they rationed their lending to the available base. Banks individually would be likely to take the view that they could obtain the base assets they required simply by bidding for deposits. In a sophisticated, competitive and necessarily decentralised banking system it is unrealistic to suppose that individual banks would be constrained in their lending activity by the prospect of a higher cost of funds which they would be able to pass on to their borrowers. If such a relationship emerged, therefore, it would be essentially because the banks - in bidding for deposits to finance their loans and to maintain their desired holding of base assets - would bid up interest

rates to the point where the demand for credit was curtailed. This clearly has implications for the degree of interest rate volatility that must be expected of the system.

A major difficulty with the proposal, acknowledged by most of the academic proponents, is that it would require a long transition before we could tell if a sufficiently stable demand for base or a sufficiently stable relationship between the base and either the money supply or nominal income had emerged. Initially we would know little about the banks' desired holdings of base assets or about how to interpret what evolved. We would not therefore know how to target the base. If meanwhile we sought to operate base control in these circumstances we should lose control over both interest rates and £M3.

If we wanted to move towards this kind of system, we should have to continue during the transition to rely essentially upon discretionary choice of short-term interest rates and debt sales designed to achieve a £M3 target, but providing steadily increasing scope for flexibility around the chosen general level of rates. This might allow the banks' voluntary demand for base assets gradually to be revealed, and, if it proved to be sufficiently stable, the base could then increasingly be used to guide the choice of the level of interest rates. Ultimately, then, one might hope to be in a position to leave interest rates to market forces.

From the outset, there would be substantial institutional change, involving the techniques for financing government, the clearing bank overdraft system, the rates charged by Building Societies and the role of the discount market.

Whatever the merits or demerits of such changes, they could not be carried through quickly, nor yield effective results for a number of years.

(ii) A mandatory monetary base system

The second main approach to monetary base control is that which has been advocated mainly by Pepper in the UK, and which would have some practical resemblance to present arrangements in the US. Under this proposal the Bank would again operate on the base which would however, in this case, be related by means of a mandatory minimum reserve requirement to certain categories of liabilities of the banking system. These liabilities, it was generally accepted in the consultations, would have to be those included in M1 (or possibly a different, retail deposit, aggregate M2), for which there would be a target as we now have for £M3.

The main disadvantage of such arrangements is that the mandatory reserve requirement would constrain the banks' freedom to manage their asset structure - with some inevitable earnings penalty. The banks would therefore have an incentive to avoid these constraints by channelling business outside the controlled aggregate. This would result in distortions of the kind we have experienced with the corset, and which the Americans have experienced in the growth of the euro-dollar market.

The main advantage claimed for the system is that it would leave short-term interest rates to be determined by market forces. In practice this would be more apparent

than real. With a system of mandatory reserves the Bank would in the final analysis have to provide the base that was required, and market interest rates would, as now, reflect the price at which the Bank chose to provide it - which could of course be allowed to vary more than at present in response to the movement in M1(M2) and the associated base requirement. Recent US experience, which is not yet decisive, suggests that there could be greater volatility not only of short-term interest rates but also of the money supply.

The institutional changes required would be similar to those under a non-mandatory base scheme.

The Bank would see little merit in arrangements of this sort as a final objective; nor would we see it - as some have argued - as a transitional step to a non-mandatory system since we would learn nothing in the meantime about the stability of demand for reserves under a non-mandatory system.

To sum up this section:

- we see the theoretical attraction attributed to a pure, non-mandatory, monetary base system as proposed by Brunner and other academics;

- there would be a long transitional period before we could operate it, during which we should have to continue much as now, although with increasing interest rate flexibility which would involve major institutional change;

- we remain sceptical as to whether even when it was fully in force it would work satisfactorily in practice.

SECRET

BANK OF ENGLAND

Annex

THE STATE OF THE ECONOMY

1. This note assesses developments in the real economy as background to discussion of monetary policy. Recession has hit manufacturing disproportionately hard, which sharpens complaints about the level of interest rates and the exchange rate. Prospects for manufacturing companies have to be assessed in the light of prospects for the economy as a whole.

Developments this year (Table 1)

2. Compared with other industrial countries, the decline in output this year has already been fairly steep. After a small fall in the first quarter, total output (GDP) fell a further 2% in the second quarter, taking it down to 2½% below the average for last year. Though there has been some decline in service sector output, most of the fall was concentrated on manufacturing which has fallen heavily this year and in July was over 7% below the 1979 average.

3. Adult unemployment, seasonally adjusted, was nearly 1,800,000 in September (7.4%), up 520,000 on a year ago. The brunt was borne by manufacturing (where employment by July had fallen by 6¼% since July last year.)

TABLE 1: DEVELOPMENTS IN 1980

	1980 so far			Bank forecast for 1980
OUTPUT				
% change from 1979 average	(Q1)	(Q2)		(Average 1980)
Total (GDP - output)	-0.7	-2.5		-2.5
	(March)	(June)	(July)	(Average 1980)
Manufacturing	-5.7	-6.6	-7.1	-7.5
UNEMPLOYMENT*				
	(March)	(June)	(Sept.)	(1980 Q4)
Thousands	1,413.9	1,535.1	1,784.0	1,867.0
%	5.9	6.4	7.4	7.8
RETAIL PRICES				
% change over 12 months	(March) 19.8	(June) 21.0	(August) 16.3	(1980 Q4) 16.5

*Excluding school leavers, seasonally adjusted

4.The whole of the fall in output this year is accounted for by the turnround in stockbuilding. The run-down in stocks appears far from completed: traders have probably been unable to reduce stocks of finished goods as quickly as they would have liked. Exports have been fairly steady: we have lost shares in export markets through growing uncompetitiveness, but this was masked because export markets continued to grow briskly in the early part of the year - but are now likely to turn down as recession abroad spreads. Imports (at any rate of manufactured goods) tend to be affected more rapidly by worsening competitiveness: in fact, however, this has been overlaid by the fall in demand at home. Foreign competition has also contributed to the squeeze of profit margins both on exports and probably in home markets; many firms appear to be faced with a question whether to abandon export markets in which they have so far managed to keep a footing.

5.Lower output and lower margins have reduced the already low level of industrial and commercial companies' profits. This in turn is forcing them to accentuate retrenchment - in stocks, investment, overheads and labour - which would probably anyhow have taken place; and this seems bound to continue. Because of the difficulty of and possible disadvantage of raising finance on the long-term capital market, and because of low profits, companies have been exceptionally dependent on finance from the banks.

6.Table 1 also shows the declining rate of price inflation. The year-on-year figures shown understate the fall-off in inflation: over the last four months the annual rate of rise in retail prices has been 9%. Prospects for inflation next year (and, to degree, for output), depend on wage settlements in the coming round.

7.Overall developments so far this year have been more or less in line with earlier Bank forecasts. Present Bank forecasts for 1980 - not greatly revised - are also shown in Table 1.

Prospects for 1981 and 1982

8.It seems more likely than not that output will fall further next year, and, quite possibly, again in 1982. The reasons for suggesting a pessimistic view - notwithstanding the uncertainty of forecasts - are broadly as follows.

9.Developments could be significantly affected, among other things, both by the course of wages and by the exchange rate. It is possible to be relatively optimistic about wages. Reports from the Bank's Agents suggest an increasingly widespread view in industry itself that settlements may be moderate -i.e.below the present year-on-year increases in the RPI (16%) and in many cases perhaps well under 10%. In services, the prospect is more difficult to guage, and much may depend on the level of settlements in the public sector. Even with considerable moderation, however, the increase in wages in this country is unlikely to be smaller than the average of our main competitors - which would not enable us to catch up lost ground.

10.The competitive position of industry undoubtedly suffered a large decline over the last two years. Thus, on the measure used by the IMF[1], it has declined by 35% since the second half of 1978. Half of that could be ascribed to wage costs here rising more rapidly than in other countries; half to the rise in the exchange rate over that period. The exchange rate might fall as and when interest rates can be reduced. But clearly no such adjustment is likely to reverse more than a part of the competitive deterioration that has occurred. The full effects of the latter have still to show up.

11.Thus, while the movement of exports and imports has not been a depressing factor on the economy this year, next year it could reduce output by 1 or 2%; and it could continue to operate in this direction in the next one or two years.

---

[1]The so-called normalised unit labour cost measure.

12. It is also likely that business expenditure will fall, but the pattern will change. Though stocks are likely to continue to be run down, this influence was already large this year and may not depress output further. But as a result of financial pressures, companies are likely to be forced to cut back on investment. That, also, might reduce output by 1 or 2% next year, and continue to be a factor on a smaller scale in 1982.

13. There could, then, be several factors operating together, all tending to pull output down, with nothing very powerful operating in the contrary direction. The sort of picture the present Bank forecasts suggest is shown in Table 2. This is somewhat worse than earlier Bank forecasts because wage increases have been higher than allowed for and the exchange rate has risen so much. The impact on manufacturing industry next year, though continuing, should be relatively less severe than it has been this year.

TABLE 2: MAIN FACTORS CONTRIBUTING TO FALL IN OUTPUT

	1980	1981	1982
Stockbuilding	-3%	0	(+)
Investment	-¼%	-1 or 2%	(-)
Exports and imports	+½%	-1 or 2%	(-)
All other factors	+¾%	-½%	
Total output (GDP)	-2%	-3 or 4%	-1%
Manufacturing output	-7½%	-5%	-2%

14. No mechanical forecast of price changes can have a high degree of validity or credibility. But unless expectational elements and general monetary and financial pressures induce extremely marked moderation in wage settlements this round and the next, it is difficult to see the rate of price inflation getting down below the 10% level over this period.

15. If the decline in output continues, unemployment could be expected to go on rising through the next two years. The exact rate of increase is difficult to predict, but could be as in the Bank forecast - 2½ million adult unemployed at end-1981 and nearly 3 million at end-1982.

Conclusion

16. Though no credence can be attached to the precise numbers, the forecasts strongly suggest the possibility that recession will continue through next year and, on a diminishing scale, into 1982. The outturn could be affected both by policy changes and by many unpredictable elements. Thus the forecast makes what could be over-pessimistic assumptions about wages, and assumes little change in the exchange rate. A somewhat lower exchange rate, in particular, could temper the recession and bring forward the date of the eventual upturn.

Bank of England
10th October 1980.