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cc Mr. Mount
Mr. Vereker

MR. SCHOLAR

THE OUTLOOK FOR INDUSTRY: THE JENKINS PACKAGE

1. The leading indicators are good. The leading indicators have an excellent record - they forecast the pause in recovery and now they forecast the continuation of the recovery. If the indicators were forecasting a decline, then there may well be a case for considering some sort of package. But they are not. And the most sensitive of the indicators, housing starts, is showing a dramatic 40% rise. *on last year - but caution: there is some evidence that the upward trend is levelling out (see (tag A)). MCS*
2. This would be interpreted as a mini-Budget and would cause concern if not crisis in financial markets. It would be widely seen as a Government U-turn, a pre-election bonanza, just like all other previous governments have indulged in. Such increases in spending would be represented as the height of folly just after we have had all the expenses of the Falklands conflict. From January 1981 we have avoided interim budgets by introducing a consistency and stability in our budgetary and financial system - and this is much admired both by the City and by foreigners. Confidence has been hard to gain; it is, alas, easy to lose.
3. It would increase interest rates. Markets would rapidly revise their expectations of future inflation rates in the UK and interest rates would adjust upwards. Even quite modest increases in the borrowing requirement would be interpreted, as they are in America, as harbingers of larger deficits to come. Protestations that we were still sticking to our MTFPS would be greeted with scepticism or derision. As we saw in March 1981, the only thing that will convince markets are actions. One might well fear that we would drift into a situation similar to the disastrous financial conditions that obtain at present in the United States; high budget deficits, high interest rates and no confidence in the Government's fiscal and financial policy. Recent experience in OECD countries shows that the budget deficit has an amplified effect on interest rates which would more than negate any supposed expansionary effect of an increased deficit. So we should do nothing to jeopardise the progressive fall in interest rates which is the best way to emerge from the slump.

/4. Hire Purchase Controls

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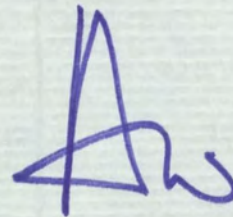
4. Hire Purchase Controls

Of all the recommendations which are made in the letter, the one we should accept immediately without reservation is to abolish hire purchase controls. This has been discussed between the Chancellor and the Governor and there is agreement on this issue.

) The Chancellor's letter to Lord Cockfield of 13 July refers.

attached

ms



ALAN WALTERS

14 July 1982

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