

*See Mr Ingham
Mr Duguid*



*pl copy to A Walters o/R 2.
Prime Minister Econ Sec*

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

FOREIGN AND COMMONWEALTH SECRETARY

IMF: 1981 ARTICLE IV CONSULTATIONS

The UK annual consultations with the IMF were completed last week. This was a routine 10-day visit but colleagues may like to have a brief account of the Mission's concluding assessment. This foreshadows the report that will be made to the Fund Board next February.

2. The Mission's central recommendation was that we should persevere with our efforts to bring down the rate of inflation. In their words:

"From a peak of 22 per cent in the second quarter of 1980, the rate of price increase has dropped to about 11 per cent where it appears to have stabilised. At that level it is still somewhat above the average for your major trading partners. It seems important to us, from an international as well as a domestic perspective, that you should persevere in your efforts to bring it down further."

3. They judged that the limitation of claims in the public sector would also continue to be of central importance. To leave room for the private sector, and to make overall restraint credible in the market, it would again be necessary to reduce the public sector borrowing requirement in relation to GDP: they see the spending plans announced for 1982-83 as a first step.

4. They had no special wisdom to offer on monetary policy but saw advantage in monitoring the performance of several aggregates:

"It is important meanwhile that monetary policy should seek to prevent excessive downward pressure on the pound."



Movements in sterling M3 are likely to remain difficult to interpret for this purpose. Institutional changes in progress may similarly limit the usefulness of the narrower aggregates alone as guides to policy. Both should nevertheless continue to be closely monitored to forestall excessive accumulations of liquidity before they spill out into the exchanges."

5. The Mission thought that much of the cost of adjustment had now come through and some recovery of output now seemed to be on its way. They judged that a forced expansion of demand would put downwards pressure on the exchange rate and so jeopardise anti-inflationary objectives. They suggested that "a measure of patience is therefore required to permit growth to resume on a sustainable basis". To the extent that wage costs can be reduced, and competition improved in that way, a higher level of activity would become possible.

6. In short we were given no blinding new insights - but a solid endorsement of our basic strategy, and one which may influence the climate of opinion for international discussion of other countries as well.

7. I am copying this minute to the Prime Minister, to other members of Cabinet and to Sir Robert Armstrong.

A handwritten signature in dark ink, appearing to be "G.H.", written in a cursive style.

(G.H.)

24 December, 1981

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