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CONFIDENTIAL

FROM: S BROOKS
DATE: 21 March 1989

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PROVISIONAL MONEY FIGURES - FEBRUARY 1989

You asked whether declining NIBM1 just reflects the introduction of the new interest bearing current accounts (Mr Sparkes minute of 20 March).

2. The twelve month growth rate of NIBM1 declined to 7.3 per cent in January and 5.3 per cent in February after being in the 10-15 per cent range (with little sign of any trend within this range) for the previous eleven months. Over the longer term NIBM1's growth has been erratic, as the chart below shows; we believe it to be very interest rate sensitive. NIBM1 fell sharply in January, by £1.6 billion, seasonally adjusted. Half this fall was accounted for by lower holdings of notes and coin - presumably a run down after the Christmas build up. The other half reflected an unusually large fall in NIB sight deposits. While we cannot be sure of the reasons for this, it seems likely that four factors played a part:

- a correction following an unusually large rise in NIB sight deposits in December;

- a reduction of deposits to pay taxes;

- switching out of non-interest bearing deposits following the rise in banks' retail deposit rates at the turn of the year (the banks delayed their reaction to November's base rate rise);

- switching into the interest bearing current account already operated by Lloyds.

3. In February, banks' NIB sight deposits fell slightly after seasonal adjustment. As they had risen strongly in February last year, this was reflected in a decline in NIBM1's twelve month growth rate. An increase in banks' total retail deposits in February was to be expected as deposits were rebuilt following the payment of taxes in January. In the event retail deposits increased by £1.6 billion, after seasonal adjustment, one of the largest increases of the past year. But with non interest bearing deposits falling the increase was more than accounted for by rises in interest bearing deposits. This could suggest that the rebuilding of deposits was combined with switching into the new interest bearing current accounts (operated by three of the big four clearing banks in February). The Bank of England reckon that the new accounts increased by around £1 billion in February (FIGURE NOT FOR USE) as a result of switching out of other M4 accounts.

<u>Conclusion</u>

4. The slowdown in NIBM1 growth in the last two months may be explicable in terms of a number of special factors, though no doubt the higher interest rates have played a part. The effect of switching into the new accounts may well persist for several months yet, leading to low figures for NIBM1 growth. But if, as we believe, there is little wider macroeconomic significance in these developments and that the growth rate may rise again when the special factors cease to operate, then our advice would be not to highlight the slower NIBM1 growth in the briefing.

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CHART : NIBM1's 12 MONTH GROWTH RATE