



Treasury Chambers, Parliament Street, SW1P 3AG
071-270 3000

10 May 1990

Barry Potter Esq
Private Secretary to
Prime Minister
10 Downing Street
LONDON
SW1

Dear Barry

Your letter of May 8 commissioned further briefing on the RPI figures to be published tomorrow.

... I attach a copy of the main Treasury brief (which has a one page summary of our briefing line) plus free standing notes, together with lines to take, on

- Alternative measures of inflation, including the GDP and consumers' expenditure deflators
- International Measurement of Inflation: the treatment of owner occupiers' housing costs and local government charges and taxes
- Interest rates and inflation
- A "German" measure of inflation
- The effects of the switch in 1987 from net to gross treatment of rent and rates rebates.

In addition the Prime Minister will be interested in the extra material in the main Treasury brief that covers the following points:

- The community charge and the RPI
- Budget excise duty changes and the RPI
- Administered prices and the RPI



- International comparisons of inflation
- Inter-Government comparisons of inflation
- General defensive points.

The Chancellor thinks the key points to make are:

- The inflation rate measured by the RPI is so high this month because it includes mortgage interest payments and the community charge. Leaving these aside the rate is 6½ per cent.
- The RPI is seriously out of line with consumer price indices in most other countries. On a more comparable basis our inflation rate would be almost 3 per cent lower than the RPI. It has risen in recent months, is still above the G7 and European averages and the government is determined to reduce it. But it is essential to get the problem in perspective.

In putting across this line we will be accused of replacing one measure of underlying inflation with another as soon as the first ceases to suit us. Our answer to this must be that we are not producing a new measure of underlying inflation. But in the unique circumstances of the introduction of the community charge in England and Wales it is perfectly natural to calculate a measure of inflation without this effect, and that to do so produces a measure that is closer to consumer price inflation as measured abroad.

The Prime Minister and Chancellor have already agreed on the need to reform the RPIAC in due course and we need to be careful not to pre-empt this process by provoking questions at this point, especially since the current RPIAC is still in session. The Government has given various undertakings that any reforms of the RPI will be put before the Committee. We should give no hint of any such reform, therefore, until the current RPIAC has completed its work programme and been stood down. For the same reason the Chancellor does not think we should advocate a new definition of the RPI at this stage. [And as you know, the Government explicitly accepted the inclusion of mortgage interest payments in the RPI in 1986 and the inclusion of community charge in 1989.]

Yours

Kate Gaseltine

MISS K GASELTINE
Assistant Private Secretary

CONFIDENTIAL

Prime Minister

No sign yet of deceleration
in MO growth. Recent numbers

MAMC: C9

FROM: MS J E C HEALEY (MG2) my wife
DATE: 3 MAY 1990 reflect continued
EXT: 4604 buoyancy of retail sales.

BHP

3/5

- 1. MR GRICE
- 2. ECONOMIC SECRETARY

- cc PS/Chancellor
- PS/Financial Secretary
- PS/Paymaster General
- Sir P Middleton
- Sir T Burns
- Mr Wicks
- Mr Scholar
- Mr Peretz
- Mr Riley
- Mr Sedgwick
- Mr Owen (EA2)
- Mr O'Donnell
- Mr McIntyre
- Mr Brooks o/r
- Ms Simpson
- Mr Pike
- Mrs Williams

Coming after the sharp rise
in notes and coin in April,
this week's further significant
increase in notes and coin has
to be regarded as disappointing.

JWG

3.5.90

Mr Gray - No 10

MO FIGURES

The latest weekly figures, covering the first week in May, are attached. In the latest four week period, MO was 7.3 per cent higher than a year earlier in seasonally adjusted terms (and 8.7 per cent higher before seasonal adjustment). Notes and coin increased by 7.4 per cent over the same period after seasonal adjustment (8.8 per cent nsa).

2. The annualised six month growth rate of notes and coin was 6.5 per cent in the latest four week period compared to 6.8 per cent in April.

Juliette Healey
JULIETTE HEALEY