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17 June 1983

The Rt Hon Nigel Lawson MP
Chancellor of the Exchequer
Parliament Street
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(My Dear Nigel)

We covered, at our meeting on Wednesday, the ground which I would normally cover in writing to you after the monthly review of the monetary situation by officials.

Broadly, at that meeting, we agreed that recent and prospective monetary developments, with, in particular, the target monetary aggregates all growing substantially above the top of the target range, were now a cause for considerable concern. Other factors - the immediate prospect for inflation, positive real interest rates, and the strength of the exchange rate in the period up to the election - did not, however, indicate that policy was unduly relaxed, though the exchange rate has now, of course, come back quite sharply following the latest decline in the general level of short-term interest rates.

Among the monetary counterparts, you expressed particular concern, which I share, at the strength of government borrowing, and I understood that Treasury officials hope to arrive at a more confident assessment of where we are on that in the course of the next month. In the meantime we agreed that we should do everything we possibly can to advance the funding programme.

In our money market operations we will aim for the time being to consolidate the new level of rates established on Tuesday, and seek to discourage any substantial moves either up or down. That posture would be consistent with leaving the undisclosed band unchanged at 9-11%. In the exchange market the pound, although still a little fragile,appears for the time being to have steadied at an effective rate of around 84, and we would expect to confine our operations to the normal smoothing, being prepared to lean against the wind on a modest scale in either direction to moderate any unduly abrupt movement.

Should market conditions again become disturbed and require a more active management, we would, of course, be in touch in the normal way.

(Yours ever)

SGD: GORDON