

Seen by PM

(PA)

MS 26/4

PRIME MINISTER

SECRET

Prime Minister *Econ BUZ*

The risk is that if we get forced to put interest rates up, we shall not get away with $\frac{1}{2}\%$ or even 1% . We ~~shall~~

EXCHANGE RATES

The upward market pressure on interest rates today is a consequence of the market expectation, promoted by the Bank, that we are on an exchange rate target. If we move interest rates upwards "to defend sterling", then we shall be validating the market's expectations and also the Bank's version of our monetary policy.

We shall then find that for the foreseeable future, it will be very difficult indeed to persuade markets that we are not on an exchange rate target. The increase in interest rates which the Bank would envisage may well give rise to a dramatic contraction in the recovery. But more important than the immediate prospects is the fact that, as the election approaches, we will be driven by the exchange rate target to impose interest rates which would severely damage our electoral chances.

As you know, I have been expecting some such confrontation with the Bank-generated market expectations for many months. But now is the time when we must force the revision. If we give way and increase interest rates, let's say by two or three percentage points, then we shall never recover the initiative. *I am afraid it is*

*would see the
consequences in the
output figures from
early 83
onwards.*

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25 November 1982

ALAN WALTERS

MS 25/11

SECRET

Sterling (Exchange Rate)

3.32 pm

Mr. Peter Shore (Stepney and Poplar) (*by private notice*) asked the Chancellor of the Exchequer if he will make a statement about the level of sterling and the Government's exchange rate policy.

The Chancellor of the Exchequer (Sir Geoffrey Howe): The movements of the sterling exchange rate in the markets this week have been fully reported. Successive Governments have made it their practice not to make statements about the level of the exchange rate. I do not intend to depart from that practice. There are, however, two points that should be made.

First, the right hon. Gentleman asked about exchange rate policy. Let me assure him and the House that there has been no change in the policy of this Government, which has continued to be that the exchange rate should reflect market forces.

Secondly, let me similarly assure the right hon. Gentleman that the Government are determined to maintain firm monetary conditions conducive to success in the fight against inflation. We back that up by determined control of public expenditure and by reducing public borrowing as a share of national output. As I made clear to the House in last week's debate, we shall maintain these policies.

Mr. Shore: I am grateful to the Chancellor for making that statement. I might call it in some places a non-statement. Does he agree that it is a wholly understandable, if delayed, reaction by the foreign exchange markets to the appalling and uncorrected loss of competitiveness of British industry and, indeed, to the prospective wiping out of our current account deficit next year as revealed in the autumn statement?

Does the Chancellor consider that the movement of the exchange rate is beneficial, or not, to Britain's hard-pressed industry? Will he make it plain that he does not intend to reverse the adjustment by raising interest rates once again?

Does the Chancellor agree that it is far better to have a coherent and industry-related exchange rate policy rather than one that is buffeted and will increasingly be buffeted by foreign exchange markets as they come to understand the appalling weakening of Britain's real economy—in jobs, industrial output and general growth?

Sir Geoffrey Howe: The right hon. Gentleman has asked several questions, all of which essentially relate to industrial strategy. It is true, as hon. Members have pointed out on several occasions, that a moderate movement of the exchange rate of this type may be of some help to some parts of manufacturing industry but only if they control their costs rigorously to retain that benefit.

It is extremely important on this occasion, as on previous ones, that one should underline the need for continued and increased success in moderation in pay bargaining. The United Kingdom cannot solve its basic problems of competitiveness by depreciation. No one in the market, therefore, should have any doubt about our

determination to hold fast to our strategy to beat inflation. Sound money remains at the heart of our economic strategy.

Several Hon. Members rose—

Mr. Speaker: Order. I remind the House that I have said previously that a private notice question is an extension of Question Time. I shall allow two questions from each side and then move on. That is what I have normally done.

Mr. J. Enoch Powell: Will the Chancellor of the Exchequer confirm, contrary to the implications of many press reports, that a fall in the exchange rate cannot of itself cause inflation, nor a rise in the exchange rate remedy inflation?

Sir Geoffrey Howe: As I have often made clear to the House and to the right hon. Gentleman, many factors may or may not be regarded as causative of inflation. That is why the Government's policy is founded on the maintenance of a well-disciplined and well-balanced monetary policy. With regard to inflationary impacts or effects in industry, I repeat that it is for industry and those who work in it or manage it to take their own steps, in the light of their own competitive conditions, to maintain and improve their competitiveness.

Mr. Higgins: Does my right hon. and learned Friend agree that, although there were various interpretations of the CBI conference debate on the exchange rate, it was clear that British industry did not want a soft option? Does he also agree that if we are to restore our competitiveness, it must be achieved by a policy of restraining excessive wage settlements and cutting industrial costs, not by a downward spiral of devaluation, higher prices and higher wage settlements of the type envisaged by the Opposition?

Sir Geoffrey Howe: I am happy to endorse every one of my hon. Friend's propositions.

Mr. Joel Barnett: I was interested to hear what the Chancellor said about exchange rates policy being related only to market forces. Bearing in mind the enormous advantage to manufacturing industry and jobs of the present decline in the exchange rate, may we take it from what the Chancellor said that he will not intervene in any way to ensure that the exchange rate will go up again?

Sir Geoffrey Howe: I shall not depart from my policy on the exchange rate as I outlined it. I shall allow it to be regulated by market forces. The right hon. Gentleman must appreciate that, although a lower exchange rate may bring some advantages to some companies and some industries, it also means higher costs to some industries and the consumer. No one can welcome that.

Mr. Forman: As there is no such thing as the perfect exchange rate for the pound against all currencies, and as the real problem is one of exchange rate volatility, is my right hon. and learned Friend prepared to reconsider the possibility of full British participation in the European monetary fund?

Sir Geoffrey Howe: The factors that have so far led successive Governments not to join the exchange rate mechanism do not seem to me to have changed significantly in the past few days.

That is another reason for not negotiating in any way with the Argentine Government over the sovereignty of the Falkland Islands.

Miss Joan Leston: Will the Prime Minister find time today to do what I did this morning—[*Interruption.*] When the public hear the guffaws from male Members of Parliament they may be able to reach a judgment about a very serious matter. Will the Prime Minister do what I did this morning and visit the breast cancer unit at the Royal Marsden hospital, where she will learn that 1 in 17 women in Britain is likely to suffer from breast cancer at any one time? If that unit closes some of the women who would have saved will die. Is the right hon. Lady prepared to tell the House now that she will find the money to save that unit?

The Prime Minister: The Royal Marsden is a postgraduate teaching hospital, managed by a special health authority, which is directly accountable to the Secretary of State. The allocation to that authority has not been cut and the authority is undertaking a review of all its activities so that it can decide its priorities.

Mr. J. Enoch Powell: When the right hon. Lady has occasion to count the cost—as I am sure that she does—in terms of casualties and suffering, of the constitutional arrangements recently imposed on Northern Ireland, will she consider how she can best use her personal authority to restore confidence in the Government's commitment to Northern Ireland as a part of the United Kingdom?

The Prime Minister: As the right hon. Gentleman knows, the commitment to Northern Ireland is enshrined in legislation. There will be no change without the consent of the people of Northern Ireland. I agree that terrorism is grave, but we shall continue to wage an unrelenting war on it. We have great confidence in the Royal Ulster Constabulary, the Ulster Defence Regiment and our Armed Forces. I pay tribute to the excellent way in which they continue to discharge their duties.

Mr. Fairbairn: Will the Prime Minister use her influence today to ask Opposition Members to place in the Library a list of the goods that they have bought from British manufacturers out of concern for unemployment, and a list of the goods that they have bought from foreign manufacturers? In that way, we shall know the depth of their emotional concern for Linwood and Ravenscraig.

The Prime Minister: I am sure that the Opposition will have heard my hon. and learned Friend's comments. It is important to try to buy as many British goods as possible, always assuming that their quality, design and price can compete with those from abroad. We are in business not to try to protect inefficient companies but to persuade people to buy British when there is a proper and effective choice.

Q3. Mr. Christopher Price asked the Prime Minister if she will list her official engagements for Thursday 18 November.

The Prime Minister: I refer the hon. Gentleman to the reply that I gave some moments ago.

Mr. Price: Will the right hon. Lady find time today to consider the issue of science policy? Is she aware that the Select Committee on Education, Science and Arts sent to discover which Minister was in charge of it and received the reply that she was? Given the absolute pledges made by two Leaders of the House that responsible Ministers will attend Select Committees, will she come and tell the Select Committee about science policy? It is an important issue, upon which the regeneration of British industry depends.

The Prime Minister: Responsibility for the research aspect of science policy lies with the Department of Education and Science. There is a Minister and a very well known organisation for it. The research and technological grants given by other Departments are a matter for them. I stress that science policy is not a thing apart and separate from Departments. It should be a part of each and every Department. It would be wrong to try to sever it and to make it into a separate Department.

Q4. Mr. Timothy Smith asked the Prime Minister if she will list her official engagements for Thursday 18 November.

The Prime Minister: I refer my hon. Friend to the reply that I gave some moments ago.

Mr. Smith: Has my right hon. Friend seen today's reports that the Treasury is apparently considering the abolition of tax relief on mortgage interest? Will she reaffirm the Government's commitment to home ownership and their determination to maintain tax relief on mortgage interest?

The Prime Minister: I saw those reports. I have no idea where they came from. There is no truth in them and there will not be so long as I remain First Lord of the Treasury.

Mr. James Lamond: When the Prime Minister addressed the NATO assembly in Westminster Hall yesterday and reached the passage in her speech that referred to the pledge of member States to safeguard the freedom, common heritage and civilisation of their peoples, based on human liberty, democracy and the rule of law, did she notice any uneasy stirrings among the representatives of the Turkish Government? Does she agree that that military Government have broken every one of those points by placing many trade unionists and leading people in the peace movement on trial simply for trying to exercise the freedoms of which she was boasting yesterday?

The Prime Minister: As the hon. Gentleman knows, the Turkish Government are committed to restoring democracy, which is a jolly sight more than the Soviet Union is.