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FROM: P N SEDGWICK
DATE: 10 FEBRUARY 1984

SIR TERRY BURNS

cc Sir P Middleton
Mr Littler
Mr Cassell
Mr Unwin
Mr Evans
Mr Lankester
Mr Lavelle
Mr Odling Smee
Mr Folger
Mr Hall
Mrs Lomax
Mr Mowl
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Mr Lewis
Mr Matthews
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Mr Wynn-Owen
Mr Milne
Mr A Ridley

Sir J Boreham - CSO

Deputy Governor)
Mr George)
Mr Coleby)
Mr Fforde) Bank
Mr Goodhart) of
Mr Plenderleith) England
Mr W A Allen)
Mr Foot)

Professor A Walters No.10

INTERPRETATION OF MONETARY CONDITIONS : FEBRUARY

... I attach the note for this month which reflects the discussion at your meeting yesterday.

P.N.S

P N SEDGWICK

INTERPRETATION OF MONETARY CONDITIONS

(1) INTRODUCTION AND SUMMARY

The most recent monetary statistics confirm the trends that emerged in the second half of 1983. The six month growth rates of all the nominal monetary aggregates are now significantly lower than the high rates recorded in the middle of 1983 and have in most cases tended to level off in the last four months. The six month growth rates of the non interest bearing aggregates have fallen to very low levels (nib sight deposits and total NIBM1 only in the most recent month). Growth of interest bearing money has been higher. There is still, however, a significant difference between the six month growth rates of £M3 and both PSL2 and M3. For every aggregate there has been a sharp fall in the six month growth rate of real money.

2. While the other indicators of monetary conditions give somewhat conflicting messages they continue to give broadly the same picture as the monetary aggregates. Producer and retail price inflation remain stable (although producer input prices and the CBI survey could suggest some upward movement in the future). Nominal and real exchange rates and interest rates have been fairly steady in recent months. The behaviour of asset prices does not suggest an upward movement in the rate of inflation for the general price level. Indeed there are some signs that house price inflation may be falling.

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(2) THE BEHAVIOUR OF THE MONETARY AGGREGATES

3. Table 1 and Charts I and VI summarise the most recent information on the nominal monetary and financial aggregates as well as data for previous financial years.

TABLE 1 : % GROWTH RATES IN THE NOMINAL AND FINANCIAL AGGREGATES ϕ

	Composite monetary indicator	MO	Non- interest bearing M1	M2 ⁶⁶		narrow defin- ition (mone- tary sector)	broad defin- ition	£M3	M3	PSL2
				M1						
(a) financial years										
1980-81*	11.1	6.4	7.8	11.2				19.9	21.6	14.4
1981-82*	5.4	2.4	-0.3	3.9				12.0	15.3	10.8
1982-83*	10.9	5.7	11.3	14.9				11.5	12.8	11.4
(b) changes in 4 quarters to +										
1982(1)	7.7	3.1	3.5	8.0				13.2	15.5	11.7
(2)	6.0	2.7	1.3	6.4				12.0	13.1	10.3
(3)	6.3	2.0	3.9	8.8				10.3	10.3	8.5
(4)	8.9	4.3	8.8	11.5	6.4	4.3		10.4	12.0	8.8
1983(1)	10.5	5.7	10.9	13.3	8.0	6.3		10.2	13.3	10.2
(2)	11.3	7.3	10.5	15.9	8.9	8.0		11.7	13.1	11.7
(3)	10.4	6.0	9.1	12.4	7.9	7.9		9.6	11.2	11.8
(4)	11.2	5.9	9.2	12.4	7.5	8.0		10.8	12.7	13.1
(c) changes in 12 months to										
1983 Feb	9.2	3.8	8.9	11.8	6.3	14.9		10.2	13.1	9.5
March	10.5	5.7	10.9	13.3	8.0	6.3		10.2	13.3	10.1
April	11.3	5.7	11.3	14.9	8.5	7.1		11.5	12.8	11.3
May	11.6	6.2	11.5	16.0	9.1	7.9		11.0	12.2	11.5
June	11.3	7.3	10.5	15.9	8.9	8.0		11.7	13.1	11.9
July	11.9	6.0	10.7	15.0	8.5	7.9		12.4	13.1	13.0
Aug	11.5	6.4	10.3	13.9	8.6	8.0		11.4	12.3	13.0
Sept	10.4	6.0	9.1	12.4	7.9	7.9		10.6	11.9	12.2
Oct	10.8	6.3	9.4	13.7	7.8	7.9		9.6	11.2	12.0
Nov	10.1	6.9	8.2	11.9	7.1	7.4		10.6	11.3	12.2
Dec	11.2	5.9	9.2	12.4	6.9	9.0		10.0	11.3	12.1
1984 Jan	11.0	5.7	9.0	11.1	6.3	9.9		10.8	12.5	13.1
(d) changes (at an annual rate) in 6 months to										
1983 Feb	10.9	6.0	10	13.6	6.4	6.8		10.5	13.3	11.5
March	11.5	5.8	9.9	13.9	8.4	8.5		9.9	14.7	12.3
April	13.2	5.2	10.1	15.8	9.7	9.6		12.5	14.8	14.9
May	12.1	5.3	7.7	13.8	9.3	9.4		11.2	12.4	15.9
June	13.1	8.0	8.0	16.8	11.6	10.8		13.7	13.2	17.4
July	14.5	8.5	13.2	13.8	13.7	11.6		13.6	14.0	16.6
Aug	12.0	6.8	10.5	14.3	10.8	9.2		12.4	11.3	14.7
Sept	9.3	6.3	8.3	11.0	7.5	7.2		9.2	7.8	11.6
Oct	8.5	7.4	8.6	11.8	5.9	6.2		8.7	9.0	9.5
Nov	8.3	8.6	8.7	9.9	4.9	5.4		8.8	10.2	9.1
Dec	9.4	3.9	10.5	8.2	2.4	7.3		7.9	11.7	9.0
1984 Jan	7.5	4.9	4.9	8.6	-0.6	8.3		7.5	11.5	9.4

(See page 3 for footnotes)

Footnotes to Table 1

- Through the financial year (mid-April on mid-April)
- ∅ The growth rates for all monetary aggregates, except non-interest bearing M1, are adjusted for changes to the new monetary sector. The October 1982 figures were greatly distorted by the over-subscription of the STC share issue. The figures shown here are the Bank of England/Treasury best estimates of what would have happened in the absence of the distortion.
- + The quarterly figures are for the final banking month of the quarter.
- ∅∅ M2 is "seasonally adjusted" by using a seasonally adjusted series for the NIBM1 component and unadjusted series for the other components. When proper seasonal adjustment of M2 is eventually possible its within year movements will be different.

CHART I: ANNUAL GROWTH RATES OF NARROW MONEY

INCREASE OVER PREVIOUS 12 MONTHS

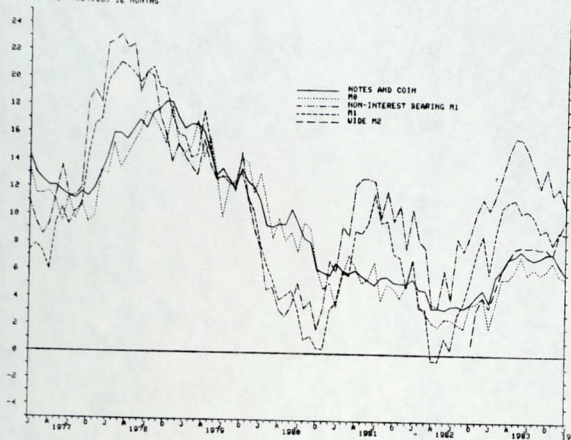
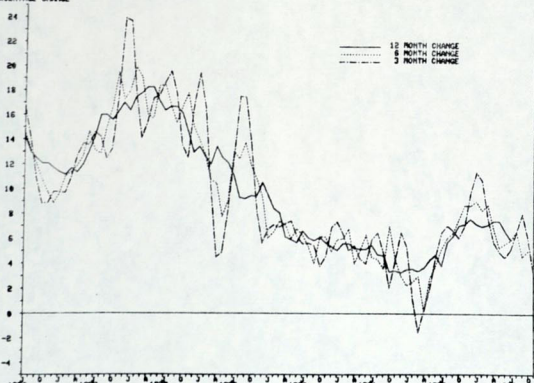


CHART II: GROWTH RATES OF NOTES AND COIN

ANNUALISED PERCENTAGE CHANGE



NOTE: THE GROWTH RATES IN CHART II ARE SHOWN AS THE RESPECTIVE PERIOD OVER WHICH THEY ARE MEASURED. THAT IS, THE GROWTH FROM SEPT. 1981 TO SEPT. 1982 IS SHOWN AS MARCH 1982 AND THE SIX MONTH ANNUALISED GROWTH RATE FROM MARCH 1982 TO SEPT. 1982 IS SHOWN AS JUNE 1982.

CHART III: GROWTH RATES IN M0

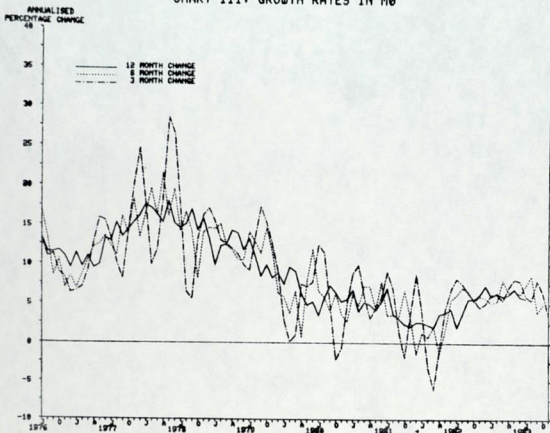


CHART IV: GROWTH RATES IN M1

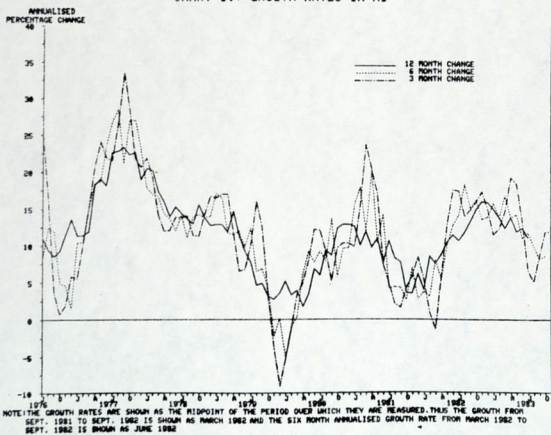


CHART U: GROWTH RATES IN STERLING M3

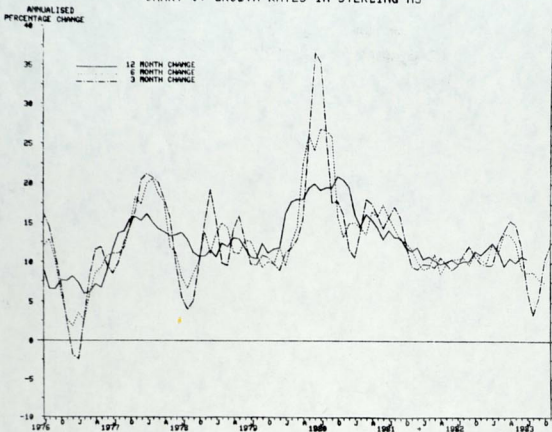
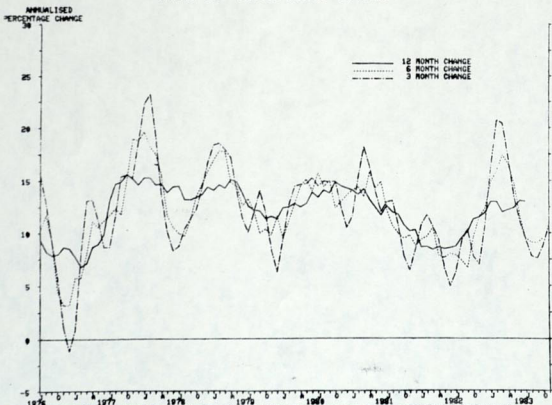


CHART VI: GROWTH RATES IN PSL2



NOTE: THE GROWTH RATES ARE SHOWN AS THE MIDPOINT OF THE PERIOD OVER WHICH THEY ARE MEASURED. THUS THE GROWTH FROM SEPT. 1981 TO SEPT. 1982 IS SHOWN AS MARCH 1982 AND THE SIX MONTH ANNUALISED GROWTH RATE FROM MARCH 1982 TO SEPT. 1982 IS SHOWN AS JUNE 1982

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4. There has been little change in the twelve month growth rate of any of the monetary aggregates over the past year, however the six month growth rates have been considerably lower in the past few months than earlier in 1983. The slow down in the six month growth rate is especially marked for narrow M2 (although this could reflect the inadequacies of the partial seasonal adjustments applied to the series). The growth rates in wide M2 in December and January have been increased by the change in the terms on accounts with two major building societies which switched about £1.6 bn from 3-month deposits (outside M2) to less than 1-month deposits (inside wide M2). The six month growth rates in the other aggregates, with the exception of M3 and PSL2, were about one half as fast in January as in the middle of 1983.

5. The aggregates in Table 1 overlap to a considerable extent and some components of money are in a number of aggregates. (Notes and coin is in all the aggregates, while NIBM1 appears in all except M0.) Table 1A shows the separate components of the widest reported aggregate, PSL2. The most marked changes have been a sharp drop in the six month growth of nib sight deposits and an acceleration in the volatile ib sight deposits series. The other interest bearing components of PSL2 expanded at a faster rate than notes and coin and nib sight deposits. The buoyant flow of funds into building society accounts, associated with the attractive interest rates on offer and the introduction of more liquid and transaction related types of deposits, appears to have continued; while it is likely that the effect of the earlier fall in interest rates on the non interest bearing aggregates is now coming to an end. Banks have continued to introduce new interest bearing chequable (retail) accounts which may have led to an additional move out of nib to ib sight deposits. The growth of the interest bearing component of M1 may, in addition, have been affected by a repatriation of money invested in offshore "roll up" funds. To the extent that money placed in offshore "roll up" funds was originally reinvested by the funds in banks or building societies in the United Kingdom, a repatriation of deposits would not affect the overall growth in PSL2, although the growth of the individual components within PSL2 may well be affected.

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TABLE 1A : GROWTH OF COMPONENTS OF FSL2 (%)

	Notes and coin	Non-interest bearing sight deposits with banks	Private sector interest bearing deposits with banks <u>Total</u>	(of which included in M1)	All other components of FSL2
(a) Financial years					
1980-81	6.2	11.0	29.1	34.5	8.0
1981-82	3.5	-2.9	21.1	27.1	5.3
1982-83	7.2	14.0	10.9	26.9	11.7
(b) Changes in 4 quarters to					
1982 (1)	4.7	2.5	18.0	32.8	9.2
(2)	3.4	-0.1	17.5	33.5	7.5
(3)	3.5	4.2	12.8	28.4	6.4
(4)	4.8	11.4	10.0	20.9	7.6
1983 (1)	6.3	13.8	9.7	21.3	10.3
(2)	7.7	12.3	11.6	33.2	12.8
(3)	7.2	10.3	10.0	23.2	15.4
(4)	6.7	10.7	11.7	22.3	16.3
(c) Changes in 12 months to					
1983 Feb	5.8	10.9	10.1	21.5	9.3
Mar	6.3	13.8	9.7	21.3	10.3
Apr	7.2	14.0	10.9	26.9	11.8
May	7.3	14.2	11.2	31.1	11.9
June	7.7	12.3	11.6	33.2	12.8
July	7.3	12.9	12.2	28.9	14.8
Aug	6.3	12.8	11.6	25.2	15.8
Sept	7.2	10.3	10.0	23.2	15.4
Oct	7.5	10.5	11.7	27.9	15.4
Nov	7.5	8.7	10.8	23.2	16.0
Dec	6.7	10.7	11.7	22.3	16.3
1984 Jan	6.0	10.8	11.2	17.3	16.7
(d) Changes (at an annual rate) in 6 months to					
1983 Feb	8.8	10.9	9.5	24.7	14.5
Mar	8.8	10.6	9.1	27.2	16.9
Apr	9.1	10.8	14.4	34.8	20.5
May	8.4	7.3	13.9	34.1	21.6
June	8.8	7.4	16.3	46.3	21.7
July	6.9	17.2	13.7	15.3	20.8
Aug	3.9	14.7	13.8	25.6	17.1
Sept	5.7	10.0	10.9	19.3	13.9
Oct	6.0	10.3	9.0	21.3	10.5
Nov	6.7	10.0	7.8	13.3	10.6
Dec	4.7	14.1	7.2	2.2	10.3
1984 Jan	5.1	4.8	8.6	19.2	12.7

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6. In anticipation of a switch to monitoring monthly average MO, Table 1B shows growth rates of banking monthly average and end banking month MO. The twelve month growth rate of the two series are very similar. Over 1983 the six month growth rate of monthly average MO has been a little smoother than that of end banking month MO rising to only 7.5 per cent in June instead of 8.0 per cent and falling to only 5.5 per cent in December instead of 3.9 per cent. The most recent growth rates (December 1983 and January 1984) of the averaged MO series are higher than those of the end-month series.

7. Table 2 and Charts VII & VIII show the latest data on the growth of real money. These series are deflated by the RPI less an adjustment for the mortgage component rather than the total RPI as in previous monthly notes. The six month growth in the RPI adjusted for mortgage rate effect was higher than the six month growth in the total RPI in the first half of 1983, reflecting the fall in mortgage rates in 1982, but lower in the second half of 1983 following the rise in the mortgage rate in the middle of the year. Consequently deflating by the adjusted RPI tends to smooth out somewhat the path for the growth of real money in 1983. The twelve month growth rates in real money are generally higher now than at the end of 1982 and beginning of 1983. The six month growth rates have fallen quite sharply and are now negative for M1 and MO. However, both of these aggregates have fairly strong velocity trends associated with innovations in financial markets. The six month growth rates of real money could also be distorted by the simple seasonal adjustment of the RPI. Charts IX-XII show the levels of real money and the real FT all share index. The rise in the real FT all share index, up until the last few days, has brought it to the levels approaching those experienced during the 1960s.

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TABLE 1B % GROWTH RATES OF MONTHLY AVERAGED
MO AND END BANKING MONTH MO

	Monthly average of weekly figures	End banking month MO
(a) Financial years		
1980-81	6.8	6.4
1981-82	2.0	2.4
1982-83	6.1	5.7
(b) Changes on same period in previous year		
1981 (1)	6.5	7.3
(2)	4.8	5.6
(3)	5.3	5.2
(4)	4.6	5.2
1982 (1)	2.7	3.1
(2)	2.8	2.7
(3)	2.3	2.0
(4)	4.0	4.3
1983 (1)	5.3	5.7
(2)	6.5	7.3
(3)	6.5	6.0
(4)	6.5	5.9
(c) Changes on same period in previous year		
1983 Feb	3.4	3.8
Mar	5.3	5.7
Apr	6.1	5.7
May	6.8	6.2
June	6.5	7.3
July	6.3	6.0
Aug	6.6	6.4
Sept	6.5	6.0
Oct	6.7	6.3
Nov	6.4	6.9
Dec	6.5	5.9
1984 Jan	6.0	5.7
(d) Changes (at an annual rate) in 6 months to		
1983 Feb	6.9	6.0
Mar	6.6	5.8
Apr	7.8	5.2
May	6.5	5.3
June	7.5	8.0
July	5.5	6.5
Aug	6.2	6.8
Sept	6.3	6.3
Oct	5.7	7.4
Nov	6.4	8.6
Dec	5.5	3.9
1984 Jan	6.6	4.9

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TABLE 2 : CHANGES IN THE REAL MONEY SUPPLY (%)

	Total RPI+	RPI ⁺ less mortgage element	Composite monetary indicator	MO	Non interest bearing M1	M1	£M3	PSL2
(a) Financial years*								
1980-81	12.0	12.4	-1.3	-5.3	-3.0	-0.02	7.5	2.2
1981-82	9.4	9.1	-3.4	-6.2	-8.7	-4.9	2.6	1.5
1982-83	4.0	4.8	6.2	0.8	6.2	9.6	6.4	6.2
(b) Changes on same quarter in previous year								
1982(1)	10.3	9.8	-1.9	-6.1	-5.8	-1.8	3.1	1.8
(2)	9.2	8.8	-2.6	-5.7	-7.0	-2.4	2.9	1.3
(3)	7.3	7.3	-1.0	-4.9	-3.2	0.3	2.8	1.0
(4)	5.4	6.6	2.0	-2.1	2.1	4.6	3.6	1.0
1983(1)	4.6	6.0	4.3	-0.3	4.6	6.9	4.0	3.9
(2)	3.7	4.5	6.5	2.7	5.8	10.9	6.9	7.1
(3)	5.1	5.2	4.9	0.8	3.7	6.8	4.1	6.4
(4)	5.1	4.8	6.1	1.1	4.2	7.3	5.7	7.9
(c) Changes in 12 months to								
1983 Feb	5.3	6.7	2.3	-2.8	2.0	4.7	3.2	2.6
Mar	4.6	4.3	4.3	-0.3	4.6	6.9	4.0	3.9
Apr	4.0	4.8	6.2	0.8	6.2	9.6	6.4	6.1
May	3.7	5.6	5.7	0.6	5.6	9.8	5.1	5.6
June	3.7	4.5	6.5	2.7	5.8	10.9	6.9	7.1
July	4.2	4.7	6.9	1.2	5.7	9.8	7.4	7.9
Aug	4.6	5.1	6.1	1.3	4.9	8.1	6.1	7.5
Sept	5.1	5.2	4.9	0.8	3.7	8.8	4.1	6.4
Oct	5.0	5.0	5.6	1.2	4.2	8.4	5.4	6.9
Nov	4.8	4.9	5.0	1.9	3.2	6.7	4.9	7.2
Dec	5.3	4.8	6.1	1.1	4.2	7.3	5.7	7.9
1984 Jan	5.1	4.6						
(d) Changes (at an annual rate) in 6 months to								
1983 Feb	3.5	5.4	5.3	0.6	4.5	7.8	4.9	5.8
Mar	3.5	4.5	6.7	1.2	5.1	9.0	5.2	7.4
Apr	2.8	3.8	9.1	1.4	6.1	11.6	8.4	10.7
May	2.2	3.3	8.5	1.9	4.2	10.1	7.6	12.2
June	3.0	3.1	9.7	4.8	4.7	13.3	10.3	13.9
July	4.7	3.9	10.2	2.5	8.9	9.5	9.3	12.2
Aug	5.6	4.7	6.9	2.0	5.4	9.0	7.4	9.5
Sept	6.7	5.8	3.3	0.4	2.9	4.9	3.3	5.5
Oct	7.2	6.2	2.2	1.1	2.3	5.3	2.4	3.1
Nov	7.5	6.5	1.5	1.9	2.1	3.2	2.1	2.4
Dec	7.6	6.6	2.5	-2.5	3.6	1.5	1.2	2.3
1984 Jan	5.6	5.2	2.2	-0.3	-0.3	3.2	2.2	4.1

+ The simple method of seasonal adjustment for the RPI less the mortgage component for use in calculation of the six monthly growth rates was described in the February 1982 Interpretation of Monetary Conditions.

* Through the financial year (mid-April on mid-April)

∅ The real money supply are deflated using the RPI less mortgage element.

CHART VII: GROWTH RATES IN REAL M1

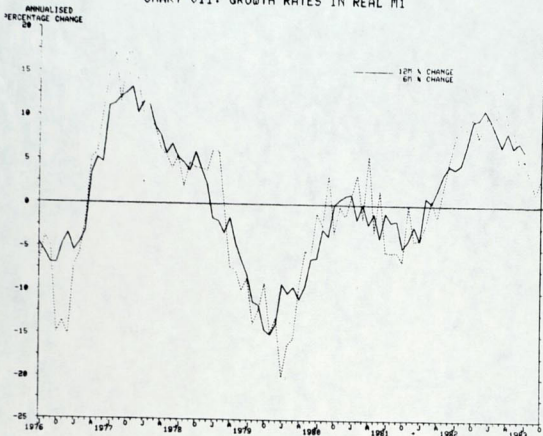
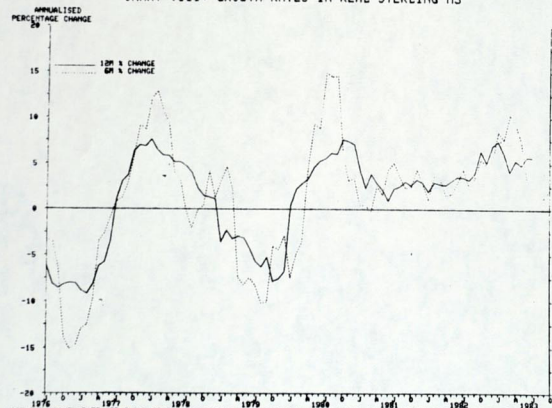


CHART VIII: GROWTH RATES IN REAL STERLING M3



NOTE: THE GROWTH RATE ARE SHOWN AS THE MIDPOINT OF THE PERIOD OVER WHICH THEY ARE MEASURED. THUS THE GROWTH FROM SEPT. 1981 TO SEPT. 1982 IS SHOWN AS MARCH 1982 AND THE SIX MONTH ANNUALISED GROWTH RATE FROM MARCH 1982 TO SEPT. 1982 IS SHOWN AS JUNE 1982

CHART IX: LEVEL OF REAL M1

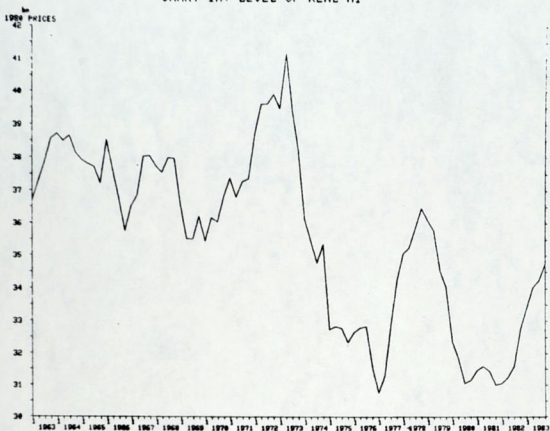
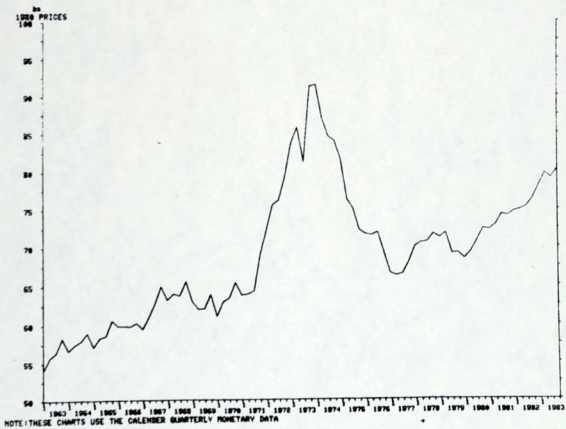


CHART X: LEVEL OF REAL STERLING M3



NOTE: THESE CHARTS USE THE CALENDAR QUARTERLY MONETARY DATA.

CHART XI: LEVEL OF REAL PSL2

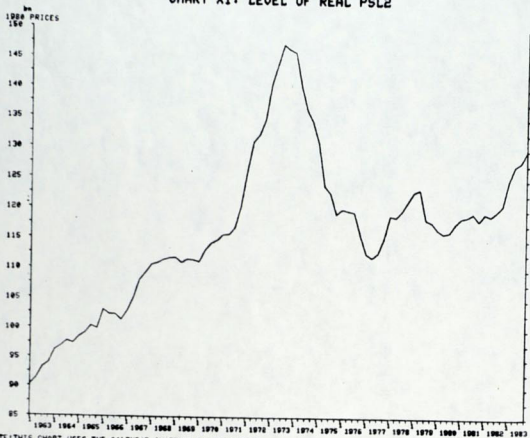
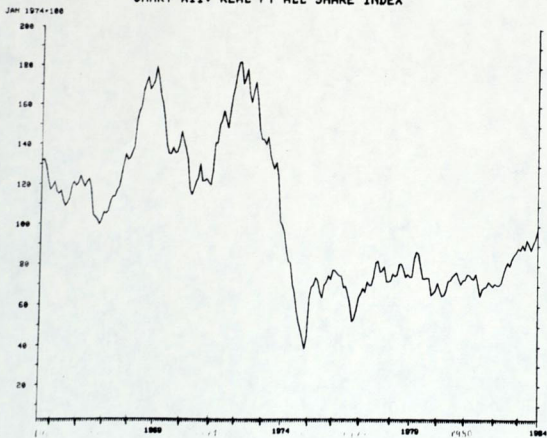


CHART XII: REAL FT ALL SHARE INDEX



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8. Table 3 shows the growth rates for total bank lending to the non-bank private sector. The rise in the six month growth rate continued in January, although there was some levelling off in the twelve month growth rate. The available sectoral breakdown for the calendar quarter data suggests that the upturn in lending that occurred in the second half of 1983 largely reflected a recovery in company borrowing and a small acceleration in borrowing for consumption. There is no clear evidence on the sectoral composition of the monthly total lending figures.

TABLE 3 : TOTAL STERLING BANK LENDING TO
THE NON BANK PRIVATE SECTOR (1)

	<u>Percentage change in stock of lending over</u> <u>12 months</u>	<u>6 months (at annual rate)</u>
1983 February	23.0	20.6
March	20.7	17.5
April	18.2	14.0
May	18.0	12.5
June	18.5	13.8
July	14.5	11.4
August	15.3	11.5
September	14.3	12.9
October	13.1	14.9
November	13.1	15.8
December	15.2	16.0
1984 January	14.8	18.2

(1) Lending by the monetary sector, banking months, seasonally adjusted.

(3) OTHER INDICATORS OF MONETARY CONDITIONS

9. Table 4 shows the growth of nominal and real GDP. The growth rate of nominal GDP rose slightly in the first quarter of 1983, and appears to have been a little lower in the second and third quarters. The twelve month growth rate of real GDP appears to have been in the range 2-3½ per cent in 1983. The CSO have revised up their projections for growth in real GDP in 1983 Q4.

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TABLE 4 : GROSS DOMESTIC PRODUCT (at market prices),
CSO's average estimate

	<u>Money GDF</u>		<u>Real GDF</u>
	<u>% change on a year earlier</u>	<u>% change over six months (annual rate)</u>	<u>% change on a year earlier</u>
1982 1	9.8	8.6	
2	10.3	8.2	1.5
3	8.9	9.2	2.5
4	8.2	8.1	1.8
			1.1
1983 1	9.3	9.5	3.4
2	7.4	7.4	2.3
3	8.5	7.0	2.9
4*	8-8½	9½-10½	(2½-3½)

*CSO projection

10. Table 5 shows the most recent data for the growth of retail prices, wholesale prices, average earnings and unit wage costs in manufacturing. Retail price inflation continues at around 5 per cent, while the rate of producer output price inflation has tended to edge up very slightly compared with earlier months in 1983. The six month growth of producer input prices has risen, but much of this is the result of seasonal influences. The growth of underlying average earnings, which remains just under eight per cent, is considerably greater than the growth of unit wage costs in manufacturing. The twelve month growth in unit wage costs has been erratic in 1983, making it difficult to isolate any distinct trend in the series. The available information, which is available only after a two month lag, does not indicate a significant upturn in unit wage costs.

TABLE 5 : PRICES AND EARNINGS
(% change on same period a year before)

	<u>Retail Prices</u>	<u>Producer Price Index</u> (All manufactured products)		<u>Underlying Average Earnings</u>	<u>Unit Wage Costs in Manufacturing</u>
		Output prices (home sales)	Input prices		
1982 1	10.4	8.7	11.8(11.5)*	10.8	4.0
2	9.2	7.2	5.7(-2.6)*	10.1	5.7
3	8.0	7.4	4.8(-4.4)*	8.9	5.5
4	6.2	6.5	6.3(6.3)*	8.4	5.8
1983 Feb	5.3	5.2	5.7(18.8)ø	8.0	4.3
Mar	4.6	5.1	5.8(15.6)ø	7.8	3.2
April	4.0	5.4	5.9(11.7)ø	7.5	3.6
May	3.7	5.6	6.8(8.2)ø	7.5	4.3
June	3.7	6.0	7.3(2.0)ø	7.5	2.1
July	4.2	5.5	6.4(-1.4)ø	7.5	1.5
Aug	4.6	5.3	8.3(-1.3)ø	7.8	3.1
Sept	5.1	5.4	9.6(3.7)ø	7.8	3.8
Oct	5.0	5.5	8.2(4.9)ø	7.8	3.7
Nov	4.8	5.7	7.2(6.2)ø	7.8	3.6
Dec	5.3	5.6	7.2(12.8)ø	7.8**	
Jan	(5.1)	5.7	7.3(16.9)ø	7.8**	

- * Increase over two quarters before at an annual rate
- ø Increase over past six months (at an annual rate)
- ** Department of Employment estimate.

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11. Both nominal and real interest rates have been remarkably stable in recent months (Tables 6 and 7). The main changes between the interest rates in January and those recorded in early February is a slight rise in yields on IGs and long conventional stocks.

TABLE 6 : NOMINAL INTEREST RATES
(period averages for calendar months
and quarters)

	<u>Three month Interbank</u>	<u>Three month Eurodollar</u>	<u>Base Rate</u>	<u>Long Rate (20 year gilts)</u>	<u>Yield Gap</u>
1982 1	14.3	15.1	14.1	14.7	0.4
2	13.4	15.1	12.8	13.7	0.3
3	11.5	12.6	11.4	12.2	1.3
4	9.9	9.9	9.7	10.8	0.9
1983 Jan	11.2	9.0	10.7	11.9	0.7
Feb	11.3	9.1	11.0	11.5	0.2
March	10.8	9.4	10.7	11.2	0.4
April	10.3	9.3	10.2	10.6	0.3
May	10.3	9.0	10.0	10.6	0.3
June	9.9	9.8	9.7	10.4	0.5
July	9.8	10.0	9.5	10.9	1.0
Aug	9.8	10.3	9.5	11.0	1.2
Sept	9.7	9.9	9.5	10.7	1.0
Oct	9.4	9.6	9.1	10.6	1.2
Nov	9.3	9.8	9.0	10.3	1.0
Dec	9.4	10.2	9.0	10.3	0.9
1984 Jan	9.4	9.8	9.0	10.3	0.9
Feb 9	9.3	9.8	9.0	10.5	1.2

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TABLE 7 : REAL INTEREST RATES

	Expected inflation over 12 months*	Real 3 month Interbank Rate**	Yield on 1988 indexed gilt***		Yield on 1996 indexed gilt***	
			Inflation assumption		Inflation assumption	
			<u>5%</u>	<u>7%</u>	<u>5%</u>	<u>7%</u>
1982 1	10.3	4.0	3.0	2.8	3.0	2.9
2	9.2	4.1	3.5	3.2	3.4	3.3
3	8.0	3.4	3.6	3.3	3.3	3.2
4	6.3	2.7	2.7	2.5	2.9	2.8
1983 Jan	6.1	5.1	2.4	2.1	2.6	2.5
Feb	6.4	4.9	2.7	2.4	2.7	2.6
March	6.5	4.3	2.9	2.6	2.6	2.5
April	6.5	3.8	3.2	2.9	2.9	2.8
May	5.9	4.4	3.8	3.5	3.3	3.2
June	6.2	3.7	4.2	3.9	3.5	3.4
July	6.4	3.4	4.6	4.3	3.8	3.7
Aug	6.2	3.6	4.2	3.9	3.6	3.5
Sept	6.2	3.5	3.8	3.5	3.4	3.3
Oct	6.4	3.0	3.6	3.4	3.4	3.3
Nov	5.8	3.5	3.9	3.7	3.5	3.4
Dec	5.8	3.6	3.7	3.4	3.5	3.4
1984 Feb 9	5.9	3.4	3.9	3.6	3.6	3.5

*Unweighted average of forecasts by Phillips & Drew, National Institute and the London Business School; the expected rate of inflation for a given month is the change in the price level between six months earlier and six months ahead. This is assumed to approximate roughly to average inflation expectations over the 3 months immediately ahead.

** average of working days for the month or quarter.

***Last working day for each month with first of month settlement assumed, or, for quarters, the average of the last working days of the three months.

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12. In the last few days there has been a weakening and subsequent recovery in the dollars' exchange rate and strengthening of the deutschemarks'. Sterlings effective exchange rate has eased slightly but remains around 82, the level it was at in January 1983.

TABLE 8 : EXCHANGE RATES (period averages)

	Effective rate	£/£ Rate	DM/£ Rate	uncovered differential*	
				£/£	£/DM
1982 1	91.1	1.85	4.34	-0.8	4.3
2	90.3	1.78	4.23	-1.7	4.2
3	91.4	1.72	4.28	-1.1	2.8
4	89.1	1.65	4.14	0.0	3.0
1983 Jan	82.0	1.57	3.76	0.1	4.5
Feb	80.8	1.53	3.72	2.2	5.8
March	79.1	1.49	3.59	1.4	5.8
April	82.1	1.53	3.76	1.0	5.3
May	85.0	1.58	3.88	1.3	5.3
June	85.2	1.55	3.95	0.1	4.5
July	84.7	1.53	3.95	-0.2	4.7
Aug	85.0	1.50	4.02	-0.5	4.4
Sept	84.7	1.50	4.00	-0.2	4.0
Oct	83.5	1.50	3.90	-0.6	3.6
Nov	83.6	1.48	3.96	-0.6	3.3
Dec	82.5	1.44	3.94	-0.8	3.2
1984 Jan	81.9	1.41	3.95	-0.4	3.5
Feb 9	81.7	1.42	3.89	-0.6	3.4

*Between 3 month UK interbank rate and 3 month Eurodollar rate and the 3 month Euro DM rate.

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(4) HOUSING FINANCE AND ASSET PRICES

13. The building societies again achieved record inflows in calendar December, with total shares and deposits outstanding increasing by £1.3 billion seasonally adjusted during the month. Weekly figures for the largest societies show that inflows have remained buoyant in January. Two of the top five societies have reduced the required withdrawal notice on their three month accounts to 28 days, thus giving M2 an artificial boost. The amounts involved were over £1½ billion. The interest rates on these accounts have not been reduced to compensate for the increased liquidity, so they have become very attractive investments. Recent inflow figures may also have been boosted by switching out of offshore roll-up funds. Inflows of wholesale money have fallen back considerably from the levels reached in the autumn.

TABLE 9 : BUILDING SOCIETY FINANCIAL FLOWS
(Calendar months and quarters,
seasonally adjusted at monthly rates)

	Liquidity ratio (end period)	Net increase in shares & deposits	Net inflows of whole- sale money (n.s.a.)	Net new commit- ments	Gross advances	Net advances
	%	£bn	£bn	£bn	£bn	£bn
1981 1	19.3	0.7	-	1.1	0.9	0.5
2	19.5	0.8	-	1.4	1.3	0.7
3	19.7	0.9	-	1.4	1.3	0.7
4	19.8	1.0	-	1.8	1.6	0.9
1983 1	18.2	0.2	-	5.1	5.2	3.0
2	17.4	0.2	0.4	4.6	4.8	2.8
3	17.8	0.3	0.5	4.5	4.5	2.4
4	19.0	0.4	0.7	5.2	4.8	2.9
1982 Dec	19.8	0.8	-	1.9	1.7	1.0
1983 Jan	19.3	0.7	-	1.8	1.7	0.9
Feb	18.8	0.7	-	1.7	1.7	1.0
Mar	18.2	0.8	-	1.6	1.8	1.0
Apr	18.0	0.7	-	1.6	1.6	0.9
May	17.6	0.6	-	1.5	1.6	0.9
June	17.4	0.8	0.3	1.4	1.6	0.8
July	17.7	1.0	0.2	1.5	1.5	0.8
Aug	17.8	0.9	0.2	1.4	1.5	0.8
Sept	17.8	1.0	-	1.6	1.5	0.8
Oct	18.8	1.1	0.3	1.7	1.5	0.8
Nov	18.8	1.2	0.2	1.8	1.6	0.9
Dec	19.0	1.3	0.1	1.7	1.7	1.0

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14. Mortgage commitments appear to have levelled off at just under £1.8bn a month and gross advances have now almost reached this level. The societies can finance this level of lending with their current inflows, but there is probably little upward pressure on liquidity ratios with mortgage demand as strong as it is. The present rough balance between the supply and demand for funds overall looks as though it could persist for some time, but it could lead to a deepening division between those societies which have differential mortgage rates (and are therefore probably not experiencing mortgage queues) and those which have a single rate and are facing mortgage queues. Both the Abbey National and Halifax, which have recently been pressing for a reduction in general building society rates are in the former camp. However, the deadlock on interest rates is unlikely to be resolved before competing interest rates move.

TABLE 10 : NET LENDING FOR HOUSE PURCHASE
(£bn. seasonally adjusted, calendar months)

	<u>Building Societies</u>	<u>Banks (Est)</u>	<u>Total Building Societies & banks</u>
1982 Dec	1.0	0.4	1.4
1983 Jan	0.9	0.3	1.2
Feb	1.0	0.3	1.3
Mar	1.1	0.3	1.4
Apr	0.9	0.3	1.2
May	0.9	0.3	1.3
June	0.9	0.3	1.2
July	0.8	0.3	1.2
Aug	0.8	0.4	1.2
Sept	0.8	0.3	1.1
Oct	0.8	0.3	1.1
Nov	0.9	0.3	1.3

Percentage change in stock of lending

	12 months	6 months	12 months	6 months	12 months	6 months
1982 Dec	16.6	18.9	89.0	76.7	24.1	26.0
1983 Jan	17.5	19.8	83.6	65.1	24.7	25.6
Feb	18.5	20.9	77.5	55.0	25.1	25.6
Mar	19.3	22.2	70.7	47.6	25.4	25.8
Apr	19.7	22.2	66.1	44.4	25.4	25.5
May	20.0	22.0	61.7	39.5	25.3	24.7
June	20.0	21.1	55.7	37.1	24.8	23.6
July	20.1	20.4	50.7	37.6	24.3	23.1
Aug	20.1	19.3	46.5	33.5	23.9	22.3
Sept	20.1	18.0	42.5	37.6	23.4	21.1
Oct	19.7	17.3	40.4	36.5	22.3	20.3
Nov	19.6	17.2	37.2	34.9	22.3	20.0
Dec	19.3	17.5	34.9	32.7	21.8	20.0

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15. The growth in house prices continued to decline in December at both the mortgage approval and completion stage, with a dramatic fall to 7.6 per cent based on mortgage approvals. Indeed on this basis, the level of house prices declined from a peak in August 1983 to the end of the year, and the December level was lower than at any time since last May. If this figure is not distorted by special factors, of which we are currently unaware, then the growth rate based on mortgage completion data should continue to decline over the next few months.

TABLE 11 : HOUSE PRICES
(% change on a year earlier)

	<u>Based on mortgage approvals</u>	<u>Based on mortgage completions</u>	<u>Mix-adjusted (based on completions)</u>	<u>Nationwide (based on approvals)</u>
1982 Q1	-4.0	-4.9	0	2
Q2	-0.7	-3.0	1	2
Q3	4.0	0.5	2	3
Q4	12.2	6.8	6	8
1983 Q1	13.0	11.3	11	9
Q2	12.8	10.4	9	11
Q3	14.6	12.3	10	13
Q4	9.6	11.9		12
1983 Jan	13.8	9.6		
Feb	13.7	10.8		
Mar	12.4	11.8		
Apr	12.6	10.9		
May	12.4	9.5		
June	13.3	10.9		
July	15.5	11.7		
Aug	14.7	12.4		
Sept	13.8	12.8		
Oct	10.8	12.7		
Nov	10.2	12.1		
Dec	7.6	11.0		

16. The fourth quarter figure for agricultural land prices shows a rapid deceleration over the previous year. Figures for tender prices and mix-adjusted house prices in the fourth quarter are not yet available, but the Nationwide and DOE unadjusted house price figures both suggest some deceleration. Taking the available evidence as a whole, it appears that the trend of asset price growth is now at worst flat and is almost certainly showing signs of declining from the peak growth rates of 10-12 per cent experienced during 1983.

CHART XIII: QUARTERLY HOUSE PRICES

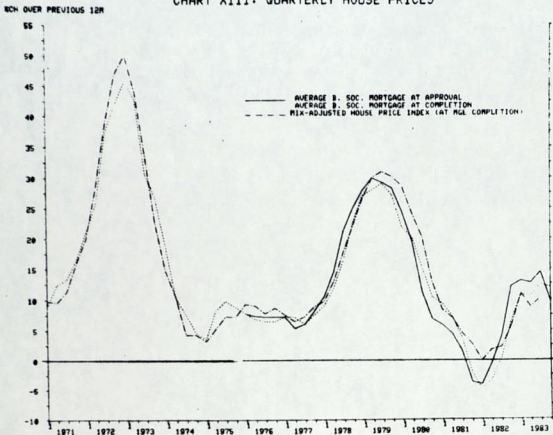
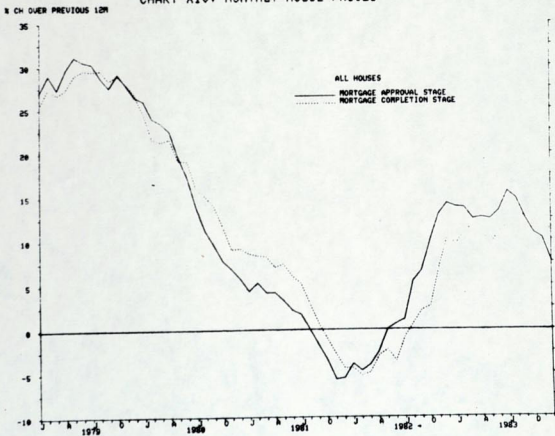
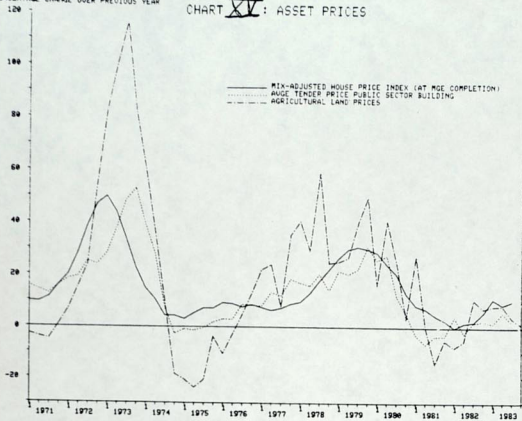


CHART XIV: MONTHLY HOUSE PRICES

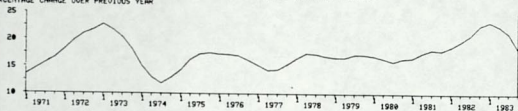


PERCENTAGE CHANGE OVER PREVIOUS YEAR

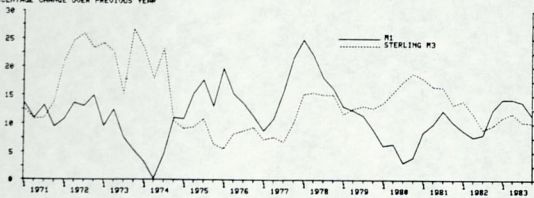
CHART XV: ASSET PRICES



PERCENTAGE CHANGE OVER PREVIOUS YEAR
STOCK OF MORTGAGES OUTSTANDING



PERCENTAGE CHANGE OVER PREVIOUS YEAR
GROWTH RATE OF M1 AND STERLING M3



ANNUAL PERCENTAGE CHANGE
RETAIL PRICE INDEX

