



Treasury Chambers, Parliament Street, SW1P 3AG
01-233 3000

1
Prime Minister
This is a rather disappointing response.
But the Treasury seem to have looked into this carefully.

PRIME MINISTER

ms.

Agree -

i) no action for the moment?

Yes

ii) future contingencies such as suggested in para 4 and at Page 4?

Yes

INFLOW CONTROLS

You expressed concern about the upward pressure on sterling which the current level of interest rates appears to be causing, and asked whether we should not be considering the imposition of controls on inflows. This is something which we ourselves have been looking at recently. Since your enquiry the rate has eased somewhat and I have also answered a number of questions about it in the House. But you may be interested to read the attached note which sets out the issues in some detail.

TL 3/3

2. The first question to consider is the factors which might lead us to introduce inflow controls. It is helpful to start by distinguishing between different causes of high exchange rate. A major influence is that of our domestic monetary policy. A high exchange rate is an important linkage in the transmission of a tight monetary policy to lower inflation and it would not be sensible to frustrate this by the use of inflow controls. Another influence is North Sea oil; a likely consequence of oil production is an exchange rate that is higher than it otherwise would be. It would not be appropriate to try to offset this essentially medium term effect by the use of short-term inflow controls - the experience of other countries has demonstrated time and again that inflow controls cannot be effective for more than a short period.

/Inflow



Inflow controls seem most appropriate for use in countering short-term speculative inflows stimulated by events outside the UK - a collapse of confidence in the dollar for example.

3. The effects on monetary policy must also be taken into account. The most obvious inflows to control - increases in non-resident holdings of sterling assets - are those which do least damage to monetary control. There is a danger that if we controlled only these flows we should simply divert inflows to other, more damaging, channels. As a result any successful scheme of inflow controls would have to extend rather wider: this would inevitably conflict with our desire to remove administrative burdens from the private sector. And inflow controls would in any case run counter to our philosophy of letting market adjust freely.

4. Sterling has indeed been very strong recently, but it appears that this is largely the result of our firm monetary policies and of North Sea oil rather than of any external events. I have thus concluded that no action should be taken on inflow controls for the present. I do however feel that we should have suitable contingency plans and I have asked officials to press ahead with work on them. This is closely related to work on the future of the exchange control legislation, which is discussed briefly at the end of the note. If you agree with the approach I suggest on that subject, I propose to send a minute to those Cabinet colleagues most directly concerned in this area, letting them know what our plans are.

Flay A

5. I am sending a copy of this minute to the Governor of the Bank of England.

Andigun

for (G.H.)

29 February, 1980

Approved by the Chancellor and signed in his absence