



# H. M. TREASURY

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Statement by Nigel Lawson, MP, Financial Secretary to the Treasury during his meeting with Regional City Editors on Monday 9 June 1980.

## THE MEDIUM-TERM FINANCIAL STRATEGY IN PERSPECTIVE

Any committee which contains within its ranks two former Financial Secretaries to the Treasury is a force to be reckoned with. And I am sure that the new parliamentary select committee on the Treasury, thus endowed, has an important and distinguished role ahead of it in reinforcing parliamentary scrutiny of economic policy and contributing to an informed public debate on these matters.

But it has to be said that in some respects the Committee has made a disappointing start. Its recent report on the Budget and the Government's expenditure plans to 1983-84 fails to grasp what the Government's underlying financial strategy for the medium term is about. It may be that the fault lies, at least in part, with the Government - and more particularly with Treasury Ministers - for failing to make the true nature of the strategy clear. If so, it is not too late to repair the omission.

The medium term financial strategy is essentially a monetary - or, if you like, monetarist - strategy. We believe that in order to reduce the inflation rate on anything more than a strictly ephemeral basis it is necessary to reduce the rate of monetary growth. For this reason the centrepiece of the strategy is a medium term monetary target, to which we are committed. Nowhere in the Committee's report is it suggested that that target cannot or will not be met: indeed, our record since taking office is evidence that we do meet our monetary targets, however unpopular the short term measures needed to do so.

The Government also believes that in order to make sure of achieving this monetary strategy - and in particular in order to do so without putting excessive weight on interest rates - it is necessary to have a consistent fiscal policy. This implies a reduction in the Public Sector Borrowing Requirement as a proportion of national output. It is in this sense, as I have said before, that our policy is fiscalist as well as monetarist. And it is for this reason that we have included in the strategy an illustrative fiscal framework.

But there is no PSBR target. We believe that the numbers published in the Red Book are consistent with the achievement of the monetary target at acceptable rates of interest, but inevitably there is much that is uncertain. We cannot be sure how much banks will lend or what will be the preferences of bondholders. The appropriate PSBR in any given year will vary with the state of the business cycle. We have therefore served notice of the broad fiscal balance we consider to be both possible and desirable; but the precise details will have to be determined year by year, in the normal way.

Finally, we have published tax and expenditure figures which, on a deliberately cautious assumption about economic growth for the years after 1980, would enable us to achieve the illustrative fiscal balance - with, in the last two years of the period, a margin in hand. The public expenditure figures are in effect set out in the 1980 Public Expenditure White Paper: not, of course, the detailed components, which are subject to annual review, but the annual totals, which we are committed not to exceed.

There is no precisely corresponding tax commitment. We have simply given our estimate of the tax that is likely to be collected, at current real rates of taxation, on a number of reasonable and prudent illustrative assumptions (in particular for the level of North Sea oil output and for overall economic growth - which, outside the North Sea sector, is taken to be marginally negative over the period as a whole). The difference that emerges between this tax figure and the tax take required to meet the fiscal framework is shown

in the medium term financial strategy, as published in the Red Book, as an 'implied fiscal adjustment'.

Yet to read the Committee's report you would imagine that this implied residual within the medium-term financial strategy is what the Government's whole strategy is all about. You would think that total public expenditure cannot be reined back unless the White Paper sets out in detail every single figure for every single component for the whole period and these are all validated by events. You would think that the whole strategy is suspect (and, incidentally, that the economy is incapable of pulling out of recession) unless every economic variable - consumption, investment, exports, imports and all the rest - can be precisely predicted and controlled.

The truth is the precise opposite of this. What really would be suspect would be a strategy that did depend on a claim to be able to predict or control any of these variables. That is exactly why we have so constructed our strategy that its success does not require that any of these items take any particular value.

The heart and core of the strategy is the monetary target. There are many ways of meeting this target. What we have done is simply to set out one possible fiscal framework that is consistent with the target, plus a firm commitment that the target will indeed be met. As Dr Alan Budd, one of the Committee's expert advisers, declared a few weeks ago: "I think that the Government's policies take the country in the right direction, and that's the best one could hope for."

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