

*Ami Mish gan to copy 7  
to 5 to Chawath.*

Cabinet Macro-Economic Discussion

*72  
8/6*

The present draft of the Treasury paper is a good one. The purpose of the meeting is not simply to give colleagues a chance to criticise the economic strategy. Instead it is an opportunity to teach them the hard realities of the economic choices. The paper is particularly useful in examining the various blind alleys which have been suggested so often. It should provide a valuable agenda for exposing and nailing the fallacious arguments that lurk behind many of the alternative policies.

The paper does also provide a basis for re-establishing a fresh start and a joint commitment by colleagues. The main objective must be to change the attitudes from scepticism to confident commitment.

I suspect that the main attack will be on the counter-proposition that increased public spending would largely expand employment and output, and would have minor effects on inflation. It will be argued that, contrary to the last point in paragraph 39, there is no need to contract private output; we shall simply employ idle resources. This is another way of saying that "demand is inadequate". Our counter argument is that money demand has been expanding at over 10% a year - so where is the "inadequacy"?

I do not think there is any substantial error in the paper. And I think it performs its main purpose well. But I would suggest the following minor amendments.

- (a) paragraph 7: The second sentence should not refer to the North Sea oil propping up our exchange rate. As you know, I think the North Sea oil was a minor cause of sterling over-valuation; it was mainly a monetary phenomenon. Now sterling has since fallen dramatically - and the oil is still there. I suggest we delete "and, to a much larger extent ... to end of sentence".

(b) paragraph-18: I suggest we also delete  
"An uncomfortable side effect of North Sea  
oil through,"

(c) paragraph 37: last line delete  
"and selfishly used".

ALAN WALTERS

6 June 1981