

PRIME MINISTERTHE MARKETS

I have confirmed with the Chancellor a meeting for 1845 on Sunday evening. The Chancellor wants to talk about the markets and about the succession to De Larosiere. He has a meeting with the Bank and officials arranged for 0800 on Monday morning and will have to leave for Luxembourg immediately after it.

The Chancellor's meeting this evening was apparently rather confused. But I am told (please give no indication to the Chancellor that you know this) that the general feeling was in favour of a 1% increase in base rates next week. The meeting recognised that to raise base rates on Monday would look too obvious and would confirm the belief that the Government had postponed the increase simply in order that it should not coincide with the Party Conference. The idea instead would be to raise base rates a few days later. This was a tentative conclusion and market movements in the early part of next week could easily change it.\* (The inter bank rate for example closed this evening at 10<sup>11</sup>/16%.)

Any increase in base rates next week will be used as ammunition to accuse the Government of playing politics with the nation's finances, though of course the accusation will have less force the later the increase happens. Any increase will tend to take the shine off the Party Conference and the unemployment numbers.

The Government's reputation for doing what is right rather than what is politically expedient is its most precious asset. The decision should be taken with a view to whatever is best for restoring that reputation in the financial markets. The Chancellor's Mansion House speech on Thursday is likely to help to buy a little time. If rates go up on Wednesday or Thursday, how will he explain the increase and the delay?

*DKN*  
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\* Opec is likely to continue until  
Tuesday or Wednesday.