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10 DOWNING STREET
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From the Private Secretary

1 February 1988

Dear Alex,

INTEREST RATES

The Chancellor discussed with the Prime Minister this morning the position in the markets and proposed that the Bank of England should signal a half per cent increase at noon. Given that sterling had fallen during the morning against the dollar and deutchmark he did not expect a half per cent increase to lead to sterling pushing up against DM3. He also did not expect this to lead to any increase in building society rates.

The Prime Minister said she was content for some tightening of the monetary stance. However, if in the event higher interest rates did lead to sterling pushing up against DM3, she would be strongly opposed to any intervention and hence to a boost to domestic liquidity offsetting the impact of the interest rate rise. It was only on this basis that she was prepared to agree to the half per cent interest rate rise.

The Prime Minister also noted that the end January Reserves figure had been reduced by an EMCF revaluation of \$600 million. The Chancellor agreed to provide a note setting out the background to this adjustment.

Yours,
Paul.

(PAUL GRAY)

Alex Allan, Esq.,
H.M. Treasury.

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