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Her Britannic Majesty's Embassy present their compliments to the Federal Department of Finance and Customs and have the honour to forward the text of a personal message from the Chancellor of the Exchequer to Federal Councillor Georges-André Chevallaz, Chief of the Department. The message refers to the statement which the Chancellor of the Exchequer is making this afternoon in the House of Commons, announcing the British Government's decision following its recent review of economic policy and reporting on the progress of negotiations with the International Monetary Fund. The Embassy will receive the text of the Chancellor's statement in due course and will forward this as quickly as possible to the Federal Department of Finance and Customs.

Her Britannic Majesty's Embassy would like to draw the attention of the Federal Department of Finance and Customs to a reference in the Chancellor of the Exchequer's message to the text of the Chancellor's Letter of Application to the International Monetary Fund, which is being published today. A copy of the Chancellor's letter is being forwarded to this Embassy by Diplomatic Bag for transmission to Federal Councillor Chevallaz. But the Embassy have been informed that the text will almost certainly be reproduced in full in the London Times and Financial Times of Thursday, 16 December.

Her Britannic Majesty's Embassy avail themselves of this opportunity to renew to the Federal Department of Finance and Customs the assurance of their highest consideration.

BRITISH EMBASSY

BERNE

15 December 1976



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As you will know, over the past few weeks I have been engaged with my Cabinet colleagues here in conducting a review of our economic policies for the next two years.

During the course of this Autumn, despite the considerable progress we had already made, the Government's economic strategy had been put at risk by the development of instability in the exchange markets and by pressures on monetary aggregates, which threatened our objectives both for prices and living standards and - through the steep rise in interest rates - for investment, employment and industrial performance.

In order to bring an end to this instability and to ensure the necessary shift of resources into the balance of payments and investment, the Government has now decided on a range of measures to cut public expenditure and the public sector borrowing requirement in 1977-78 and 1978-79, which I shall be announcing in the House of Commons this afternoon and which I thought you would wish to know about.

In summary, the Government has decided to reduce public expenditure programmes in 1977-78 by Pounds 1 billion and in 1978-79 by Pounds 1.5 billion at 1976 survey prices and to sell during 1977-78 British Petroleum shares calculated to yield Pounds 500 million. An additional Pounds 200 million is to be spent on measures to help industry. But this additional expenditure will be offset by an increase in the duties payable on alcohol and tobacco. These measures

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will reduce the public sector borrowing requirement from its present level of about 9 per cent of GDP to about 6 percent in 1977-78 and to a little over 5 percent in 1978-79. They will also contribute to ensuring a firm control over the monetary aggregates: and, as a result, the expansion of domestic credit will be reduced from Pounds 9 billion in the current financial year to Pounds 7.7 billion in 1977-78 and Pounds 6 billion in 1978-79. I have also made it clear that I shall be ready to take any further action which may be needed to shift resources into exports and investment in 1978-79 in next year's public expenditure review and in my 1978 budget.

Following these measures, and taking account of the increasing benefits of North Sea oil and gas, we expect that there will be a substantial reduction in the size of the current account deficit on our balance of payments in 1977-78 and a swing into substantial surplus in 1978-79. But an improvement of this magnitude both for the UK and other deficit countries must depend on a satisfactory rate of expansion in world trade and on the willingness of those countries with a strong balance of payments to accept a corresponding deterioration in their own external position.

At the same time as I announce these measures I shall also be sending to the Managing Director of the IMF the UK's formal Letter of Application for a



stand-by credit of SDR 3.36 billion in order to help bridge our expected deficit in 1977-78 and to replenish the level of our reserves. This letter sets out the Government's economic policies and objectives in more detail and I am therefore arranging for the text of it to be made available to you during the course of the next few days through the offices of our Embassy. Because of the considerable Parliamentary and public interest, I shall also be publishing the text of the letter here. Dr Witteveen has told me earlier today that he supports both the economic strategy I have described and the measures the Government are taking and that he will recommend the Executive Directors of the Fund to accept my request for the stand-by arrangement.

I understand that steps are now being taken to arrange an early meeting of our deputies to discuss the UK's request for a stand-by. I hope that at that meeting and at the subsequent discussion in the IMF Executive Board, your Government will be able to support our request and to agree to the activation of the general arrangements to borrow in order to ensure the necessary finance for the stand-by.