GPO

US file

Treasury Chambers, Parliament Street, SW1P 3AG
01-233 3000

21 October 1983

Andrew Turnbull Esq
10 Downing Street

Dear Andrew

MR KINNOCK AND THE US BUDGET DEFICIT

I enclose, as promised, a short note on which you might draw in response to Mr Kinnock's suggestion that we should emulate the US budget deficit in pursuit of growth. As you will see, this refers to Mr Volcker's outspoken remarks to the Joint Economic Committee yesterday. We do not have a full text of Mr Volcker's speech but you will have seen it reported in the FT and we have checked the particular references with Washington.

Yours sincerely,

Margaret O'Mara

MISS M O'MARA
Private Secretary

~~Higher US budget deficits and economic recovery~~

Background

Mr Neil Kinnock has claimed in a speech to the Newspaper Press Fund in Glasgow that increases in public spending and borrowing, as in the United States, provide a route to economic recovery. It is true thatthe US economy is growing strongly but if this recovery is to prove durable and not be dissipated in rising inflation and interest rates, the US budget deficit will need to be curbed, and the Administration is committed to doing just that.

2. On the same day that Mr Kinnock was making his speech, Mr Paul Volcker, the respected chairman of the US Federal Reserve - who has more experience in these matters than Mr Kinnock has or is ever likely to have - told Congress in Washington that the huge Federal budget deficits were a threat to economic expansion and 'a major factor propping up interest rates.'

3. Mr Volcker pointed out that there were already signs, for example, in the housing sector, of private investment being crowded out by high interest rates. He also cited the poor US external trade performance as being one of the problems created in part by high interest rates which have helped keep the dollar artificially high.