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The Governor
Copies to the Deputy Governor
Mr. Fforde
Mr. George

NOTE OF A MEETING HELD AT 11 DOWNING STREET ON THURSDAY, 20 NOVEMBER, 1980 AT 9.00 A.M.

Present:

Chancellor of the Exchequer	Governor of the Bank of
Financial Secretary	England
Mr. Rylie	Mr. Fforde) Bank of
	Mr. George) England

NOVEMBER ECONOMIC STATEMENT

The Chancellor noted that the Governor had seen the current draft of the Statement it was envisaged he might make on 24 (or possibly 25) November: were the steps there set out sufficient to justify a change in Minimum Lending Rate (MLR)?

2. The Governor welcomed the clear indications of the determination with which the Government were pursuing their policies; substantial fiscal changes were contemplated, and it would be all the more important that the Government maintained their firm stance on pay in the public services. So far as MLR was concerned, the question was whether the fiscal action taken, and the fact that the monetary target would in a sense be "out of action" until the next Budget were sufficient to make possible a reduction. Since recent movements in monetary statistics would provide no justification, it would be important to emphasise the real factors affecting the economy, and the impact of the present sectoral financial imbalances in relation to the monetary statistics. The Governor felt that the real economy had already felt the intended effects of a tight stance of monetary policy, despite recent monetary statistics; no-one would want a lax monetary policy, but there seemed to be some prospect that the desired counter-inflationary results might now be secured with somewhat less pressure from monetary policy. Bank lending was likely to



be insensitive to changes in interest rates in the short run, so there was little risk that a reduction in interest rates now would increase bank lending between now and next spring - and lower interest costs would also reduce the PSBR. The Governor felt that if no change were made now in MLR, the pressures from the real economy could be irresistible, with the end result that the Government would be forced into more damaging action later than an MLR reduction now. He therefore favoured a reduction in MLR when there was a suitable opportunity; and he thought the circumstances of the economic statement provided the best occasion for making the move the Government were likely to have.

3. The Financial Secretary noted that the underlying inflation rate was now well below MLR, so that short-term real interest rates had become substantially positive during the period since MLR was moved up to 17 per cent. The Governor agreed that the success already achieved in reducing inflation was itself an argument for lower interest rates; but the point would need to be made with care, since the authorities were not supposed to be steering by reference to real interest rates.

4. On the size of the reduction in MLR, there was general agreement that this could not be larger than 2 per cent; and a reduction smaller than 2 per cent would be thought to imply that another reduction could be expected in the near future. As to the timing of the announcement, the Governor preferred that the change should actually be included in the Chancellor's Statement; it would not be possible to make the change in advance of the Statement, and to wait until 27 November risked an adverse market reaction to the rest of the Chancellor's Statement which would make it impossible for the authorities to move at all. It was therefore agreed that the Bank should make the formal announcement at a time which coincided with the end of the Chancellor's Statement.



5. Other points made in relation to the Statement were:-

(i) the revised estimate of the 1980-81 PSBR (£11½ billion) should be stated explicitly in the Statement, so that there could be no question of the Government trying to cover it up; given that the £8½ billion PSBR during the first half of this year would be known by then, the revised estimate would in practice give some reassurance to financial markets.

(ii) The changes in the reserve asset ratio and the arrangements for determining short-term interest rates should be presented positively as improvements, even though further changes might be made after several years' experience of the new regime. It would also be important not to give the banks the impression that they would be net beneficiaries when the present 1½ per cent cash requirement disappeared.

(iii) Consideration would need to be given to the press briefing about the monetary control changes; there was a question whether it would be possible to wait until the Chancellor's speech on Thursday, 27 November before giving any further explanation of the monetary control changes.

JW

(A.J. WIGGINS)
20 November 1980

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