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PRIME MINISTER

Interest Rates

You asked for a report on this morning's meeting in the Treasury on monetary policy.

The general conclusion of the meeting was that, as and when the market provides a lead, the opportunity should be taken to reduce MLR. But it would be inadvisable to try and lead the market by reducing MLR in advance. This, it is felt, would give the impression that the Government were not serious about the monetary target.

The Treasury think it most unlikely that market rates will move down appreciably before the May banking figures come out. The best that they expect is that market rates will come down after the May figures have been absorbed.

But the Treasury will not know precisely what the banking figures for May look like until this weekend. First impressions are that the figure of lending to the private sector is not as high as had been feared, though still too high; but that the sterling M3 figure will show a rise of 1½-2%. This is because of a very high CGBR figure of around £1½ billion only half of which has been mopped up by funding.

The banking figures come out next Tuesday; the money supply figures the Thursday of the following week.

The Chancellor is arranging to see the clearing bank chairmen shortly. He will, I am sure, raise the question of credit cards - though he doesn't believe much can be achieved.

On the wider question of quantitative controls, the Treasury are opposed on three grounds: first, it would go against the Government's market philosophy (and indeed it was strongly argued against in the Green Paper on monetary control). Second, they doubt

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whether it would work - borrowers would find ways of getting round the controls. Thirdly, to the extent that controls did work, interest rates would be even higher as borrowers bid up the price of funds.

Notwithstanding these points, I have asked for information on Carter's measures, which included direct controls on lending. These controls were actually taken off very quickly - may be because they were not working or, in view of the falling demand for funds, because they were no longer necessary.

TL

2 June 1980