

cc Mr Wilson



JRF 5/11/75

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PRIME MINISTERMONETARY PROSPECT

I am afraid that the October monetary figures are going to be worse than disappointing, and not encouraging as we had originally hoped.

2. The eligible liabilities figures, to be published tomorrow, Tuesday 6th, will show an increase of 2.4 per cent. The market will deduce from this that the money supply grew by about 2 per cent - correctly. The preliminary figures show that £M3 grew by 2.0 per cent and that Domestic Credit Expansion was £1.6 billion. (The components shown in the Annex, and the DCE figure, may change somewhat before they are published on Thursday 15th, but it is unlikely that there will be much change in £M3.)

3. The main change from expectation was in the Central Government's Borrowing Requirement which was nearly £1 billion rather than virtually nothing. This was due to the estimates of a number of components all going the wrong way. The largest single factor was that VAT receipts, which included the first significant payments at the higher rate, were £500 million less than expected: some of this was clearly a matter of timing (possibly due to the after effects of the computer strike) and has already been partly made good.

/4. Net



4. Net debt sales were negligible, partly because the authorities were wrong-footed by the CGBR forecast: the calls on the part-paid stocks issued in banking September were timed for banking November, in expectation of a negligible borrowing requirement in banking October.

5. Perhaps more disturbing, the bank lending figure of £1.2 billion is a record. It is reasonable to look at this with last month's figure of £0.2 billion - bank lending, after allowing for acceptances taken up outside the banking system, still seems to be running at about £0.9 billion a month, as it has since the beginning of the year.

6. It is clear that monetary policy since June has not been as tight as we had intended. The rate of growth of the £M3 statistic has been about 14 per cent pa. If allowance is made for avoidance of the SSD scheme, for example through acceptances, the underlying growth is higher still.

7. While there are good grounds for thinking that the October figure was a "hump", and will be followed by lower figures, there are a number of further factors which have convinced the Governor and myself that we must consider whether we should act to tighten policy further. Market uncertainties have halted debt sales, which had been good until September. The borrowing requirement has been running at a level which is casting considerable doubt on whether it will be as low as the Budget estimate of £8½ billion for the year as a whole. Other countries' interest rates have moved higher - most notably in the United States, but more recently in Germany and Japan.

/8. The



8. The market reactions to our policies, including exchange control relaxation, had generally been good, until the Public Expenditure White Paper last week.

9. Any immediate reaction to the monetary developments would have to be on MLR. Domestic market rates have already shifted upward in the last few weeks as a result of some of the factors I have just mentioned: the 3 month inter-bank rate is now over 14 $\frac{3}{4}$  per cent, leaving MLR out of line. Market rates are likely to move upward on the announcement of the eligible liability figures tomorrow, possibly with some further movement on Thursday week when the money supply figures confirm the worst. There could also be a further adjustment then, if we decide to announce the ending of the SSD scheme at the same time as the roll forward of the monetary target. It will certainly be necessary to move MLR by at least sufficient to validate these changes in market rates. The Governor and I will be considering whether a move may be needed to achieve our monetary targets.

10. We might discuss this briefly when we meet later this afternoon. But any decision should depend on the market reaction to Tuesday's figures, and on the further analysis by the Bank and Treasury of the implications of those figures. If there were a marked adverse reaction in the foreign exchange market, it might be necessary to decide at very short notice on Wednesday to move MLR this week. But I would hope that we could make the change the following week, when it could be presented in context with the roll forward of the target, and the full set of figures.

11. I have, of course, discussed these disagreeable developments with the Governor, who receives a copy of this minute.

A handwritten signature in dark ink, appearing to be 'G.H.'.

L-5 NOV 1979

