

SECRET

19.6.79

See 18679

MR. FFORDE

Copies to The Chief Cashier  
Mr. George  
Mr. R.H. Atkinson  
Mr. Foot

*A, pl. return for why with  
J.S.G.*

DRAFT PAPER ON "MONETARY MANAGEMENT:  
SOME POSSIBLE CHANGES"

With the Bulletin articles on the Gilt-edged Market and Monetary Base Control out of the way, you suggested that it was appropriate time to draft a paper indicating some possible positive steps that we might envisage with the aim of improving monetary management. I attach a first <sup>18.6.79</sup> draft of a paper that, when it is revised reformed, redrafted and agreed, might initially go to the Governor. At our meeting last Monday (11.6.79) you suggested that the first step might be to prepare an outline of such a paper. In the event, I found it easier to follow a line of argument through by preparing a draft in rather fuller detail, and this is attached.

Two problems stand out. The first, and in some ways the most intractable, is what to do about direct controls. Even with some possible technical reforms to the working of the present 'corset', continued reliance on this scheme looks singularly unappealing. Yet a shift to direct controls on bank lending would look in some ways even nastier. On the other hand, it seems extremely difficult to envisage conditions persisting in which we can safely abandon all resort to such direct controls.

The second issue, which may now emerge, is how strongly we may be pushed towards some form of monetary base control. This raises a drafting question about the kind of tone to use in such papers about monetary base control. Much more importantly, however, if there should be pressure for us to adopt a version of monetary base control, it would give the Bank an option to move away from complete emphasis on EM3, towards more emphasis on the narrower aggregates, which can be more easily controlled through market mechanisms alone. But such a shift would almost certainly involve tailoring the form of banks' required cash reserve ratios, including bankers' balances, to that end. Thus if there is any great likelihood of a move towards monetary base control the question of bankers' balances would come back to the fore.

19th June 1979. *CAEG*  
C.A.E. Goodhart

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