The Chief Cashier

COVERING SECRET AND PERSONAL

SIR DOUGLAS WASS

cc Sir L Airey
Mr Littler
Mr Unwin

MONETARY DECISIONS AND EXPLANATIONS

In view of your conversation with Mr Unwin this morning you may want to discuss the attached reply to the Financial Secretary before it goes forward.

2. The argument for having the roll forward announcement on the 15th is that we are going to get adverse market effects from both the money supply figures and from what is done on the SSD scheme. If, as is likely, we need an MLR change to deal with these (and what has already happened in the markets) it is better to have all the bad news at once, and one change in MLR, than to spread it, and risk two changes!

S. Wilkes
P.P. J M BRIDGEMAN
2 November 1979

cc 2/11 9

SECRET AND PERSONAL
(until 15 November 1979)

FINANCIAL SECRETARY

cc Chancellor
Chief Secretary
Sir Douglas Wass
Sir Lawrence Airey
Sir Ken Couzens
Mr Barratt
Mr Littler
Mr Middleton (OR)
Mr Hancock
Mr Bottrill
Mr P Davies
Mr Riley
Mr Ridley
Mr Cropper
Mr Cardona

Chief Cashier
Mr Quinn

MONEY SUPPLY FIGURES ETC: PRESENTATION

This minute is in response to your request for a note on how the October money supply figures might be presented: it relates this to the policy announcements - already made (notably exchange control) and to come (roll forward of monetary target, SSD scheme etc). It follows discussion with the Chief Cashier, Mr Hancock and Mr Middleton.

The Figures

2. We now have some idea of what may be in store for banking October money supply and bank lending - although we should have better figures on Friday. The main elements are expected to be:-

£M3 - growth of 2% or just over making a cumulative rate of about 14% pa for the first 4 months of the year.

M1 - a sharp increase of nearly £900 million.

CGBR - nearly £1 billion, much higher than expected for the reasons already described.

Debt Sales - virtually flat, partly because, anticipating a lower CGBR we had not timed calls on part-paid gilts for this month.

Bank Lending - well over £1 billion, plus a further increase in acceptances held outside the banking system of over £100 million.

DCE - nearly £1½ billion.

These full figures will be published on Thursday 15 November.

3. The market will get its first indication of what is to come on Tuesday when the total eligible liability figures are published by the Bank and the CLCB publishes figures for the clearers only. We will not know until Friday what the eligible liabilities figures themselves will show. However, the practice of the Bank Press Office is, if the eligible liability figures for some reason point towards a figure for the money supply significantly different from what we expect, to give a steer towards the true figure by indicating any factors which may have caused an unusual difference between the two - this avoids the market trading on a false basis for 9 days, and the problems which then arise when expectations are confounded. If this is done (if it is necessary) this time - and we think that it should be done - then we ought to work on the basis that from Tuesday next the market will be assuming that the October money supply and bank lending figures will be high and that this will be confirmed on the 15th.

The Prospect

4. Mr Middleton's team and the Bank forecasters are looking again at both the month by month forward look, and the prospect for the next 12 months or so in the light of the October figures. They will be completing this as soon as they can after the fuller analysis of these

figures becomes available on Friday, so that Mr Middleton can put forward a note on this early next week in parallel with the policy submissions which will need to relate to them.

5. The present assessment for the immediate future, on the basis that a substantial proportion of the change in the CGBR in banking October was due to timing differences, is that the banking November growth will be substantially less than that 14% pa rate - it could even be flat. The growth in banking December will depend, interalia, on what is done about the SSD scheme.

The Roll Forward of the Target

6. It will be necessary to announce during November:-

a. the roll forward of the monetary target by 6 months;

b. the future of the SSD scheme.

It will also be necessary to decide whether to take any action on interest rates, given the movements in market rates that has already taken place and the possible effects on market confidence of the ending or relaxing of the SSD scheme (if either is decided) and of the October figures. We will put submissions forward on this complex of issues, as soon as we have the revised prospect and as soon as we see the market reaction to the eligible liability figures - probably on Wednesday or Thursday of next week. There would be strong arguments for announcing decisions on these - more especially if there is any action on interest rates - on Thursday 15th so that the market can assess and react to the package of decisions and statistics as a whole, and not to one at a time. I realise that this is a tight timetable for decisions, but it is essentially dictated by the short lead time between information being available and being published.

7. The roll forward would require a statement by the Chancellor to the House: presumably after the business statement on the 15th. If it had

been decided by then whether there should be a medium term financial plan at the time of the second Public Expenditure White Paper, that also could be announced - that would help with the justification for excluding the 1980-81 PSBR from the Industry Act forecast to be published the following week.

Ministerial Speeches

8. We would see advantage in both sets of October figures and those policy decisions being put in context by a series of Ministerial speeches or statements. We would suggest:-

i. Wednesday 7 November: Chancellor's statement to NEDC on the present economic situation giving an extended treatment of exchange control and the domestic market consequences, making it clear that the Government had recognised the implications of its decisions, and referring as necessary to the eligible liability figures. That part of the statement at least would be released in full to the Press. (Drafting of this is in hand.)

ii. Thursday 8 November: Treasury 1st Order for PQs: it will be possible to refer back to NEDC statement.

iii. Wednesday 14 November: Chief Secretary's speech to Financial Times conference. The timing is unfortunate and it will need to be somewhat guarded about what it says on monetary control.

iv. Thursday 15 November: Chancellor's statement to the House on the roll forward of the target, future of the SSD scheme etc.

v. Friday 16 November: Chancellor's speech at Chester. This could be a more philosophical speech about the role of monetary policy, putting Thursday's announcements into a wider context. (Mr Riley has suggested that this should be issued on Thursday, embargoed until Friday: this should secure better coverage in the Sunday papers and might inhibit some of the wilder comments in the Friday morning's treatment of the Thursday statement.)

vi. Tuesday 20 November: Speech to City Merchants. This would repeat the main theme of the Chester speech, but also react to any comment in the meantime.

Guidance to the Press on the Figures

9. It will also be possible to do something to dampen the market reaction to the October figures by Press briefing: but both domestic and external markets will inevitably find these figures disappointing. Points which will need to be made - although the exact way in which it is done will depend on the final pattern of the figures - include:-

a. monthly figures are inevitably erratic - not least because of swings in the CGBR, generated amongst other things by the tax changes in the Budget;

b. the CGBR was higher than expected - partly because of the slower receipt of the higher rate payments of VAT.

c. debt sales were low, because we had been expecting a lower CGBR, and so timed part payments on gilts to avoid the temporary pressures on the banking system. (But we will need to avoid giving the impression that we time gilts to get a smooth money supply from month to month - we manifestly cannot do so);

d. the PSBR and CGBR should be lower from now on (although there will be fluctuations from month to month) because inter alia, the benefits of higher indirect taxes and disposals will now be coming through - in contrast to the direct tax side where the PAYE rebates mean that by mid-November we will have had the effect on the PSBR of 6 months income tax reliefs;

e. the bank lending figure was similarly erraticly high after an erratically low month - the two need to be looked at together (the last three months average about £600-900 million a month);

f. it may have been swelled by the effect of companies funding the payments of tax relief immediately after 5 October. (This effect will have been offset, at least in part, by the slower VAT payments.)

Conclusion

10. I should be grateful to know whether the Chancellor and you are content with this suggested approach. If so we will put it in hand. (Mr Hancock has already in preparation the first draft of Wednesday's statement.)

J M BRIDGEMAN
1 November 1979