27-680

See also EA/JC m 13/6
& Bridgeman/Ryrie 10/6
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*NOTE OF A MEETING WITH THE CLEARING BANK CHAIRMEN HELD IN THE CHANCELLOR OF THE EXCHEQUER'S ROOM, H.M. TREASURY AT 5 P.M ON THURSDAY, 26 JUNE 1980

GR 30/6

Present:

Chancellor of the Exchequer (in the chair)
Governor of the Bank of England
Sir Jeremy Morse (Chairman of Lloyds Bank)
Sir Anthony Tuke (Chairman of Barclays Bank)
Mr. Robin Leigh Pemberton (Chairman of the National Westminster Bank)
Sir David Barran (Deputy Chairman of the Midland Bank)
Sir George Kenyon (Chairman of Williams & Glyn's Bank)
Mr. Ryrie
Mr. Middleton

27/6

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The Chancellor invited the clearing bank chairmen to comment on the recent and prospective trends in their lending to the company and personal sectors.

2. Sir Jeremy Morse said that the situation his bank faced was not very different from the one it had been facing at the time of the previous meeting with the Chancellor in March. Lloyds had expected that company sector borrowing would turn down, as personal sector borrowing had already done, although the timing was uncertain. This remained the position. Excepting large borrowers, who had switched their borrowing in a volatile way between the clearers and the market during the period of the corset, industrial borrowers were on the whole still increasing their borrowing. Although capital projects were being abandoned, stock levels were being reduced and short time working introduced, the benefits in terms of

reduced borrowing were still outweighed by the increasing costs from high wage settlements, high interest charges and poor marketing conditions. Although slow payment by some companies had no net impact on the overall figures, it was particularly hurtful to small firms.

3. Meanwhile personal borrowing remained fairly flat, although there were perhaps some signs that people might be turning their savings into goods. The banks had always found that increases in personal incomes encouraged borrowing rather than reduced it. (In this connection Sir Jeremy Morse complained that public sector pay settlements were running at an even higher level than the 18 per cent average in the private sector.) As Lloyds saw the position, the down turn had to come; but it could still be delayed by distress borrowing by the company sector, or even by a further spurt in consumer spending reflecting the recent rapid rise in earnings.

4. There was general agreement that industrial order books had fallen very rapidly in recent weeks, with domestic orders falling off faster than export orders, despite the strength of the exchange rate. It did not appear likely that a reduction in interest rates would lead companies to add to their borrowing, although there were signs that even present interest rates would not discourage firms from going ahead with sound investment projects. Lower interest rates would have a helpful effect in taking some of the worst financial pressure off companies, although it would be desirable to keep a careful watch on the response to them of personal borrowers.

5. Sir Anthony Tuke suggested that, on the basis of experience over the last year, firms could be expected to have increased their borrowing by about 30 per cent. This reflected constant stock levels, 20 per cent inflation, and their being obliged to pay

10 per cent more for goods and services than they had bargained for. In practice, in the year to May 1980, clearing banks' lending had increased by only about 20 per cent, so that they could reasonably say that they had shown a considerable measure of restraint. Barclays had noted a sharp increase in the number of receiverships among their borrowers, but this experience was not paralleled in the other banks, although they all had an abnormally large number of company borrowers who were being "nursed".

6. A good deal of support for the Government's counter inflationary strategy was reported among the bankers' customers; they did not like high interest rates and the high exchange rate, but accepted that the "crunch" would have to come. It was noted, however, that firms producing standard materials and less specialised industrial goods were finding international competitive conditions very difficult, and were losing export orders. Moreover although some medium and large firms who were in contact with the clearing bank directors were not too uncomfortable in the present environment, very many small businesses were in considerable difficulty.

7. The discussion then turned to housing finance, which was said to have accounted for a considerable part of recent growth in lending to the personal sector. The Chancellor noted that although the growth of sterling M3 over the last six months had been in the middle of the target range, there was still grounds for caution and the position in banking June and July was not yet clear. He wanted to minimise the risk of disturbing movements following the abolition of the corset - although the corset had become increasingly ineffective, and its disappearance was not to be regretted, it would still be necessary to avoid "adventures". Ministers were receiving three broad messages from public opinion in relation to the banks: that their profits should be specially taxed; that direct control should be imposed on consumer lending; and that interest rates should be reduced. He acknowledged that the banks had helped by cutting back on their advertising of consumer lending facilities, but was worried that if the banks were to move

significantly into housing finance following the ending of the corset, there could be upward pressures on interest rates.

8. The Chancellor noted that the building societies were holding their interest rates below market levels and were obliged to ration credit; they would also have to contend with the problem of an increase in the composite rate of tax following the abolition of the reduced rate band. If the banks were now to expand their activities in the area of housing finance, the building societies would be driven to respond, and this could have awkward implications for the level of short term interest rates generally.

9. Sir Anthony Tuke said there was no question of promoting new housing finance facilities; such increases as there had been in housing lending were mainly in the traditional area of bridging loans. All five bank representatives agreed that there should be no particular difficulty about continuing to hold back in this area; even where special schemes were already in operation, the total resources devoted to them were being kept within narrow limits. Sir Jeremy Morse asked whether the Chancellor would be content if the banks undertook not to promote housing finance facilities and not to allow lending for house purchase to increase faster than other lending; the Chancellor agreed that he would be broadly content with this, although he would need to be able to indicate to the building societies that the banks would be acting in this way. Sir Jeremy Morse warned that the Government should not look to the clearing banks to achieve an absolutely precise outcome on the growth of their housing lending; in particular the clearing banks would not want specific limits to be announced, so exposing them to criticism if they were not always able to keep within those limits. If the Government had to make any announcement, this should be restricted to the point that the banks had undertaken not to use the opportunity of the removal of the corset to move in on the housing finance market while the building societies were constrained in present circumstances. Subject to this, the clearing

banks were ready to give the Chancellor and the Governor a broad undertaking to keep the rate of increase in lending for housing finance in line with the rate of increase in total advances.

10. The remainder of the discussion was devoted to a brief review of some other matters of concern. Sir Anthony Tuke said that "reintermediation" was unlikely to take place very rapidly. Sir David Barran said that there had been no recent sign of financial stringency causing people to make more use of credit cards, and that a very large proportion of Access and Barclaycard borrowing was repaid before any interest became chargeable. The Chancellor suggested that the true interest rate should be stated on each monthly credit card account.

JW

A.J. WIGGINS
27 June 1980

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Distribution:

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PS/Governor of the Bank of England