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Econ Pol

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Money supply figure
looking slightly better
because of lower borrowing
by government. The

Treasury Chambers, Parliament Street, SW1P 3AG

01-233 3000

Chancellor will be
sending you a further
note on monetary
developments before you
mtg with him on
Thursday.

PRIME MINISTER

GILT EDGED MARKET

I thought that you might like to know a little of the background to the decision to announce the new tap stocks on Friday, of which you have already heard.

Thursday.
TL
10/9

2. The growth of the money supply in banking August was less than we had expected - a little below 1 per cent - largely because it was reduced by a net switch of overseas residents holdings of sterling from the non-bank private sector to bank deposits. Domestic credit expansion was still disturbingly high - about £1 billion for the third month running.

3. The Treasury and Bank's best guess is that the growth of the money supply in banking September will be about the same, but that thanks to the Central Government actually being in surplus, money supply may fall in banking October, before growing again in November. The net effect may be to bring the rate of growth of the money supply over the first five months of the target period to the middle of the target range. But there are so many uncertainties that we cannot rely on this happening; we may feel more confident in a month or so when we know what is happening to the CGBR. More important it will not be apparent to the market that the money supply is coming within the range until the October figure is published in mid-November: until then the rate of growth will not appear much different from that which we inherited.

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4. While there is not therefore an absolute necessity for further gilt sales until November, the Governor and I would feel considerably happier if we could achieve some more before then, given the uncertainties and the one sided risk for the Government if events do not turn out as expected. The sooner we can be seen to be bringing down the rate of growth of the money supply, the greater confidence in our policies and their effect on inflationary expectations, and the sooner we may be in a position to allow some fall in short and ~~long~~ long term interest rates.

5. We have been without either a medium or long tap for nearly a month now. But the gilts market has been such that the announcement of a new tap would only have depressed it further. However the market, somewhat unexpectedly, revived sufficiently on Wednesday for the Bank to conclude yesterday that it would be possible to announce a further issue without adverse effects, with a prospect of achieving sales as soon as the market was heartened by further good news. I concluded that it was right to take the opportunity to get a new tap stock into place: it had to be announced on Friday, if at all, as we cannot for technical reasons announce one next week.

6. One stock is a medium - maturing in 1988-89 - as envisaged in Nigel Lawson's minute to you of 19th July: there will be £600 million, £400 million for the market and the balance for the National Debt Office. But I decided that it was also necessary to issue a long tap, since the Bank considered that to issue a medium alone would be interpreted as a signal that we were ready for long term rates to fall - which we are not yet. For this purpose a modest amount, £500 million, of an existing stock, 12 per cent Exchequer 1999-02, should suffice. Both Stocks will be part paid, with the greater part payable in banking November.

S E C R E T



7. The intention is to get the stocks in place, so that they are there to be sold whenever the market strengthens further. This may not be in the next few weeks, although it would be very useful if there were some sales before banking September ends on 19th September, so that the initial payments reduce the rate of monetary growth this month.

8. I am sending a copy of this minute to the Governor.

A handwritten signature in black ink, appearing to be "G.H.", written in a cursive style.

(G.H.)
10 September, 1979

S E C R E T