

*Mr Hasbany*

CONFIDENTIAL

DEPARTMENT OF TRADE

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*From the Secretary of State*

The Rt Hon Sir Geoffrey Howe MP  
Chancellor of the Exchequer  
HM Treasury  
Parliament Street  
SW1

25 May 1979

*Dear Chancellor of the Exchequer,*

EXCHANGE CONTROLS

Thank you for copying to me your minute of 23 May to the Prime Minister.

As you know I share your view that the liberalisation of exchange controls would be helpful to British industry and exports. I believe also that a firm move to dismantle the constraint of these controls could be an important sign to the outside world of the Government's determination to tackle bottle-necks on the supply side of the economy.

In this respect I was assuming that you would remove all controls on overseas direct investment, since there can be little firm evidence that it would create substantial flows across the exchanges - and it would be seen as a symbolic gesture to markets indicating considerable self-confidence on the part of the in-coming Government. Announced with firm fiscal and monetary policies, embracing significant reductions in public spending, the two measures taken together, might well have the perverse effect of actually strengthening Sterling. The argument that our policies on exchange controls should be dictated by the impact of consequent moves in the exchange rate on exports is not one that I accept at this particular juncture, not least because it is so difficult to predict.



Your proposals therefore whilst welcome as far as they go may, I suggest, be regarded by markets as being unduly timid. For this reason they may not bring about the full political and economic benefits which might otherwise have been obtained. Undoubtedly they will meet criticism from the TUC which will be repeated each time that you take a further step. It is ironic that our outward capital flows should still be more tightly controlled than in almost any other major western industrial country, in spite of North Sea Oil. It is the excessive caution of successive governments in this area of policy that has brought about this situation - and I am disappointed that we cannot grasp this useful opportunity by taking a more courageous step.

The re-introduction of Sterling financing for third country trade is welcome. I accept that it would be unwise to abandon controls on portfolio investments at this stage but I fully support the limited steps that you are taking here at this time and I note your intention to study further relaxations in this field as circumstances permit.

I am copying this to the Prime Minister, the Secretaries of State for Foreign and Commonwealth Affairs and Industry, the Governor of the Bank of England and to Sir John Hunt.

*Yours Sincerely,*

*T. Callaghan*

JOHN NOTT  
(approved by the Secretary of State  
and signed in his absence)