

NOTE FOR THE RECORD

for Master Set
Euro Pot - Domestic
Monetary
Pot,

Mr. John Sparrow called on the Prime Minister at 1600 on Tuesday 19 June. The following are the main points which came up in discussion.

Mr. Sparrow said that the City was basically pleased with the Budget. The immediate marking down of gilts prices was inevitable, given the increase in MLR - which in itself had been somewhat unexpected. But the MLR increase clearly indicated that the Government was intent on keeping the money supply under control, and this ought to provide a good basis for the sale of gilts over the next few months. The take-up of the new tap stocks on Thursday would be watched very carefully. Another more promising aspect was the fact that corporate loan demand was likely to be rather lower over the next few months because of the recent accrual of cash from the pre-Budget spending spree and because of the short-term cash flow effect of the VAT increase.

Mr. Sparrow went on to say that he did not think the current level of sterling could be sustained - given the recent trade figures. The rate was being pushed up by the combination of high interest rates and the fact that many regarded sterling as a "petro-currency".

The Prime Minister said that she was concerned about the current provisions for corporate stock relief. Her impression - and this was confirmed by Mr. Sparrow - was that it had a distorting influence on company behaviour: companies tended to increase their stocks unnecessarily at the end of the financial year, which was a waste of resources and which meant a loss to the Exchequer. Mr. Sparrow added that corporation tax generally had become an "optional tax". It should either be abolished or made operative: he would prefer the latter. Mr. Sparrow then referred to PRT, and said that he was worried that the Exchequer was losing unnecessary funds because of the "uplift" provision. This meant, for example, that BP would be exempted from substantial amounts of tax when they took over part of the Beatrice Field, as they were reported to be proposing to do.

/The Prime Minister

The Prime Minister asked Mr. Sparrow for his views on the present methods of funding the borrowing requirement. Mr. Sparrow replied that he would let the Prime Minister have his views in writing, but did not accept the Bank's argument that the institutions necessarily required long-dated stock. This was an excessively expensive method of funding. On the other hand, he thought that there must be a revival of interest in equities at the expense of gilts before too long. The Prime Minister commented that she could not see how businesses would be willing to borrow for investment purposes at current rates of interest. Finally, Mr. Sparrow said that in his experience industry was already becoming more aware of the need to negotiate responsibly on the pay front: they were beginning to realise that from now on they, rather than the Government, were responsible for their actions. But it would be helpful if the Government could produce a new "standard of living" index - this would involve regarding tax as part of the cost of living. The Prime Minister said that the Treasury were working on such an index.

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21 June 1979