

SECRET



*See Lord C 39
Comment on p 25*

CHANCELLOR

cc Sir A K Rawlinson
Sir L Airey
Sir K Couzens
Mr Littler
Mr Unwin
Mr Bridgeman
Mr Middleton
Mr Monck
Mr Davies
Mr Mower
Mr Folger
Mr Williams
Mr Cardona

STATEMENT

I attach a redraft prepared in the light of your comments this morning. With the exception of the £1 billion figure for the Post Office arrears in billing, all figures are, as far as we know, correct, subject to any final comments, which should be submitted to Mr Unwin.

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ADAM RIDLEY

15th November 1979

SECRET

With the permission of the House, Mr Speaker, I should like to make a statement on monetary policy.

2. The figures for October, just published, show that £M3 grew by 2 per cent in that banking month. The growth since mid-June, the beginning of the target period, has been equivalent to just over 14 per cent a year. Although the figure for banking October was erratically high, it is clear that the underlying growth of £M3 is still significantly above the target of 7-11 per cent.

3. There have been two principal causes of this excess: a higher than expected Public Sector Borrowing Requirement in the first half of the year and the persistently high level of bank lending.

4. Because of the timing of the Budget measures - in particular receipts from VAT and reductions in public spending - the PSBR was always expected to be higher in the first half of the year than in the second. In the event, the PSBR in the first half year has been further increased by strikes and other industrial action, which have delayed the collection of VAT and telephone bills. At the peak arrears on telephone bills are expected to reach [£1] billion.

/ 5. A large part

5. A large part of these arrears will be made good in the second half-year. Even so, the best estimate which ~~can~~^{could} now be made of the PSBR for the year as a whole ~~is~~^{if no action were taken} is that it would be about £9 billion, compared with the £8.3 billion Budget estimate.

6. The monthly growth of bank lending has averaged about £700 million over the last quarter. Although the timing is difficult to predict, its growth can be expected to fall in due course because of the likely decline in the level of economic activity.

7. Nevertheless it is necessary to take action now to bring the growth of the money supply within the target range. The Bank of England accordingly announced this morning with my approval that Minimum Lending Rate would be increased to 17 per cent.

8. This goes beyond the rise in market interest rates at home and demonstrates the Government's determination to act with the firmness foreshadowed by my Rt. Hon. Friend the Prime Minister earlier this week. The recent increase in our interest rates reflects the general increase in interest rates overseas. In the USA prime rates have risen from $11\frac{1}{2}$ to $15\frac{1}{2}$ since the summer.

/ 9. In addition

9. In addition to sales of gilts, we intend to secure further funding of the PSBR through National Savings. The limit on holdings of the index-linked National Savings Certificates Retirement Issue will be increased next month from £700 to £1,200. A new ordinary National Savings Certificate will be introduced early next year. The Interest Rates on National Savings Bank Investment Account will be raised to 15 per cent from 1st January next.

10. Although much of the increase in the estimate of this year's PSBR is due to the timing of receipts, further action is required to bring the PSBR down. As an additional ^{therefore, we shall require} measure, ~~oil companies~~ to make a payment on account of Petroleum Revenue Tax at the time when they make their returns. This will have the effect of advancing the due date for collection by 2 months and will bring the arrangements for PRT into line with those for collecting royalties. We shall thus ensure that PRT reaches the Exchequer with the minimum of delay, when oil prices are rising.

11. The Bill to achieve this will be introduced shortly. It will reduce this year's PSBR by £700 million and thus bring the estimated level back to the original Budget figure of £8.3 billion.

/ As a result

As a result of this measure, next year's PSBR will also be reduced by £300 million. And telephone bills not paid this year will reduce it by about a further £400 million.

12. I set in hand some months ago a review of methods of controlling the growth of the money supply. The main instruments must continue to be our public expenditure and tax policies, which together determine both the size and the composition of the PSBR, and interest rate policies. Recently the Supplementary Special Deposits scheme, or corset, has also played a part in monetary control. I am well aware of the limitations of this scheme and do not believe that it has a permanent role to play. Nevertheless, the Governor and I have agreed that it is right that it should continue for a further six months. The Bank announced the arrangements this morning.

13. In the future, other techniques, including one of the variants of monetary base control, could play a useful role, without have the disadvantages of the SSD scheme. The Bank and Treasury will therefore shortly issue a discussion paper for consultation. I must, however, stress that no such scheme can replace the right fiscal and interest rate policies. Indeed, one of the possible advantages would be to improve the

/ response of

response of interest rates to monetary conditions.

14. Finally, I am extending the period covered by the present target range for \pounds M3 of 7 to 11 per cent per annum. That target at present applies to the 10 months from mid-June 1979 to mid-April 1980.

It will now cover the 16 months from mid-June to mid-October 1980. The effect will be to avoid building into the target for the new period the excess growth of the money supply in the recent past, while allowing a reasonable period in which to offset that excess.

15. Mr Speaker, the restoration of the economy depends above all on mastering inflation. This can only be done if we bring the money supply under firm control, progressively reduce its rate of growth over the years, and maintain the most rigorous restraint on public spending. There may still appear to be easier alternatives to the policies we are pursuing, but none of them would be responsible and none of them would be sustainable. That is why I have taken action today which demonstrates the Government's total and continuing commitment.