

CHANCELLOR

cc Financial Secretary  
Sir Douglas Wass -  
Mr Middleton  
Mr Monck  
Mr Britton  
Mr Turnbull  
Mrs Gilmore

MINIMUM LENDING RATE

You will have seen the piece on the front page of today's Times suggesting that you announced the abolition of MLR to the House yesterday. We have not yet discovered why the story appeared in this way. The story was also carried, though in less dramatic fashion, in the Telegraph and FT.

2. Reports of MLR's death are, of course, much exaggerated. We have been careful not to prejudge the outcome of today's seminar, and have considered carefully the terms of an announcement thereafter, covering particularly the circumstances in which we might still want to announce in advance the rate at which the Bank will deal. We have therefore today been correcting the mistaken impression given in the Times, and have rested on the wording in the PQ you answered, and on what was said in the Financial Secretary's speech yesterday in Oxford (copies attached).

3. There is a further complication of which you should be aware, though there is no reason for it to be raised at today's seminar. MLR appears as a reference interest rate in many contracts and in some legislation. The legislative problems are not great and we are in discussion with Departments about them. But the Law Society and the City Capital Markets Committee have made representations to the Bank about the need for some guidance on an alternative rate to use, if we are not to see what might be a considerable amount of litigation about the interpretation of existing contracts. The Bank have invited the Law Society to propose an alternative rate, which they might find it helpful for the Bank to validate in some way through retrospective publication in the Quarterly Bulletin.

It has been made clear, however, that we shall not be willing to publish an official rate in any way which might affect the achievement of the objectives we have in mind for the new system.

*Howard Davis*

H J DAVIES  
31 July 1981

ORAL

THURSDAY 30 JULY 1981

TREASURY

LA/CO - HARLOW

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MR STANLEY NEWENS: TO ASK  
MR CHANCELLOR OF THE EXCHEQUER, IF HE WILL MAKE A STATEMENT  
ON THE PRESENT LEVEL OF INTEREST RATES.

SIR GEOFFREY HOWE

BOTH SHORT AND LONG TERM INTEREST RATES HAVE RISEN IN THE LAST MONTH. BUT THERE HAVE BEEN SOME SIGNS OF EASING THIS WEEK AND UK RATES REMAIN LOWER THAN THOSE PREVAILING IN THE ECONOMIES OF MANY OF OUR PRINCIPAL COMPETITORS. THE HOUSE WILL RECALL THAT MY BUDGET SPEECH FORESHADOWED A NUMBER OF CHANGES IN OUR SYSTEM OF MONETARY CONTROL, THE PRINCIPAL OBJECTIVE BEING TO ALLOW THE MARKET A GREATER ROLE IN DETERMINING THE STRUCTURE OF SHORT-TERM INTEREST RATES. RECENT DEVELOPMENTS HAVE BEGUN TO SHOW THE WAY IN WHICH THESE ARRANGEMENTS WILL OPERATE IN PRACTICE. I EXPECT THE FULL SYSTEM TO COME INTO OPERATION ON 20 AUGUST, THE FIRST DAY OF BANKING SEPTEMBER.

Extract from Financial Secretary's Speech on 30 July

"The principal objective of the new system, which will come into operation later in the summer, is to allow the market a greater role in the determination of the structure of short-term interest rates. What this means in practice is that in its day-to-day operations with the discount market the Bank will not announce in advance the rates at which it proposes to deal, but will respond to offers of bills from the discount houses.

This means, of course, that the existing MLR will lose its operational significance - indeed it has already to a large extent done so - and, as the Chancellor said, before very long it may be suspended altogether."

Chancellor's Oral Reply on 2 July

"As I explained in my Budget Statement, it is our intention to enable market forces to play a greater role in determining interest rates. Discussions on further improvements in monetary control are well advanced. The Bank has issued the final draft of the detailed provisions. When these are put into effect we shall aim to keep short-term interest rates within an unpublished band. It may then be appropriate to suspend the practice of publishing the MLR."