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CONFIDENTIAL

29. 6.82

NOTE FOR RECORD

Copies to Mr George
Mr Loehnis
Mr Walker
Mr Fforde
Mr Coleby
Mr Dawkins
Mr Sangster
Mr M J Balfour
Mr Holland
Mr Hill
The GPS

NOTICE ON CAPITAL MARKET ISSUES

1 This note records two sessions I had - with the Accepting Houses and with the Treasury - yesterday on aspects of the proposed guidance notice circulated with my note of 25 June.

Accepting Houses

2 I took a meeting yesterday morning with a group of Accepting Houses to get their reactions to the proposition that we might now bring sterling euro-bond issues within the queuing arrangements. The group had been put together at our request by the AHC secretariat: those represented were Barings, Hambros, Hill Samuel, Morgan Grenfell, Schroder Wagg and Warburgs.

3 I explained the impression we had that sterling euro-bond issues might be beginning to attract domestic investment interest; and invited their reactions to the proposition that, to minimise disturbance to domestic issues from this source, we might now move to a position of subjecting sterling euro-bonds to timing consent, as was foreshadowed in our earlier guidance notice.

4 They were strongly resistant to any thought that we might institute some form of structured queue for euro-sterling issues on the lines of the bulldog queue, i.e. with firm dates assigned a month or two ahead. They would regard this as an unwelcome curtailment of the flexibility of timing which they value in our present approach to sterling euro-bonds. This is a perfectly fair point: a queue with firm forward dates would make no sense for a market which opens only fitfully and offers only

occasional windows through which borrowers have to be ready to scramble at short notice.

5 Equally, however, they saw the sense in our being in a position to ensure that euro-sterling issues did not cut the ground from under domestic issues - as nearly happened with the recent New Zealand bulldog. Several of them supposed that this was what we did already. I pointed out that, though we obviously use our common sense, the basic approach is that we do not regulate the timing of euro-sterling issues: where we see a clash in the offing, we try to put the respective lead managers in touch with each other, but we leave the final decision on timing to them.

6 There was considerable diversity of view as to whether euro-sterling issues were already attracting domestic investment interest, with houses contradicting each other's account of the source of demand for recent issues: it is entirely possible that each has a different experience. There was even greater disagreement as to whether integration between the euro-sterling and the domestic market was likely to go further in the future. But there was general agreement that it would be sensible for us to be in a position to stop euro-sterling issues cutting the ground from under domestic bulldogs. It was therefore agreed that we should make it clear that euro-sterling issues did need timing consent from us, with the implication that we might decline to give consent where we felt it appropriate. I explained that, in present circumstances this might very well mean no practical difference from our present procedure in relation to euro-sterling issues. But we would reserve the right to delay the timing of an issue if we saw need, e.g. if there was to be a significant increase in the volume of euro-sterling issues or in their impact on the domestic market. How we would then deal with any backlog - whether by queuing them or otherwise - would be left to be decided in the light of circumstances. This was accepted, and several houses volunteered that they would readily fall in with any indication we gave that we would prefer an issue delayed.

7 On this basis, I have re-drafted the relevant passage in the proposed notice to remove any implication of a queue and have circulated the new text of this extract only (attached) in confidence to the houses for comment. I have made it clear that this is a working draft only. I have made no mention of the rest of the ground covered by the notice.

Treasury

8 On Monday afternoon I attended a long meeting at the Treasury with Peretz (overseas side) and Turnbull (domestic monetary side) to discuss the question of crowding out. In terms of the operation of the queue, the proposition we were discussing is that we should limit foreign issues, both sovereign and corporate, to less than the full capacity of the market in order to leave room for issues by UK companies. Operationally, this might translate into a limit on foreign issues of £100 mn a month.

9 I am afraid we made very little progress. The Treasury side were adamant that rationing foreign issues is contradictory to the Chancellor's declared policy of full freedom for capital flows. They reject as invalid the proposition that crowding out of company issues can occur; and they argue that it is the Government's firm policy to be unconcerned at the possible impact on the exchange rate (they said that ADL's letter on vulnerability had been received in the Treasury with "apoplexy").

10 Specifically, they saw three main lines of objection to the idea of rationing foreign issues:

(i) The fears of crowding out were in their view groundless. They consider that foreign issues, if sold to domestic non-banks, serve to restrain monetary growth just as much as gilt sales; and therefore any increase in foreign issues can be exactly matched by a decrease in gilt sales.

(ii) They argue that discrimination against foreign issues would breach EEC and OECD obligations, which it would be embarrassing to have to defend.

(iii) Most fiercely of all, they argue that rationing foreign issues would open Ministers to political criticism that they were caving in to pressure from the Labour opposition to re-introduce exchange controls, albeit covertly; and that Labour spokesmen would be quick to argue that, having conceded the principle by taking the first small step, Ministers would no longer have any defensible grounds for exempting the rest of outward portfolio investment from control.

11 I pointed out that we had already, with the agreement of the Treasury, been rationing foreign bulldogs to £100 mn a month for some months past; we have said as much, again with Treasury support, to Australia and New Zealand in limiting their issues to that amount; and we were under instructions from the Financial Secretary to siphon off foreign companies from mass exploitation of the green light given to deep discount stocks. The only new element in the present situation was that we now had to come clean about what we were doing. They disputed that this was the policy and cited Kerr's minute of 24 June in evidence.

12 After a good deal of fruitless discussion in this vein, I was left with the distinct impression that what Treasury officials really wanted was a surreptitious limit on foreign issues, i.e. one that they could claim was justified by the need to avoid congestion in the market; or could disown as something imposed by the market on itself without official intervention by us. I pointed out that the latter was impracticable, given the multiplicity of international banks operating in London; and that we could not rely on the justification of congestion, since what we were proposing was a limit well below the capacity of the market - deliberately so, in order to leave room for issues by UK companies.

13 The conclusion was that we could not resolve the drafting of the notice until there had been agreement on the underlying policy which the notice purported to describe. For the moment, therefore, the notice stands in abeyance. I took the opportunity to take the Treasury through the small step on sterling euro-bonds described above. Happily, on this point they saw no difficulty.

IP

29 June 1982

Ian Plenderleith (4491)
Gilt-Edged Division HO-P

Sterling euro-bonds

6 In the Bank's notice of 10 November 1980, it was stated that the Bank did not at that stage consider it necessary to operate a queue for issues of sterling euro-bonds, since such issues appeared at that stage to have only a limited impact on the domestic market. It was indicated, however, that the Bank might wish to bring sterling euro-bonds within the queuing arrangements if they came to have an important impact on the domestic market.

7 Over the past two years the domestic sterling capital market and the sterling euro-bond market have tended to become more closely integrated; and there have been signs more recently that issues of sterling euro-bonds can attract domestic investment interest. The Bank considers that, in order to promote the development of the sterling capital market on an efficient and orderly basis, it would now be appropriate to take steps to ensure where necessary that sterling euro-bond issues are not a source of disturbance to issues in the domestic market. Accordingly, sterling euro-bond issues will henceforth be subject to the requirement, already applied to domestic market issues, that the consent of the Bank should be sought in advance to the timing of the issue. As with domestic market issues, requests for timing consent should in the first instance be directed to the Government Broker at Mullens & Co.

The Governor

CRW 2/7

You had it in mind to speak to Kerr (? and then the Chancellor) about the Treasury's attitude to limiting foreign issues in the UK market. IP's note of 29/6, attached, gives the background on pp. 3-4.

You ~~[illegible]~~ were also going to consider + OFT paper whether and when to revert to the Chancellor about the question of making the corporate bond market more attractive to companies — given the poor reception for the measures recently announced.

SRB 30/6