

2. Monetary Control Consultations

31 July – 7 August 1980

Co-operative Bank Limited

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Our Ref. LL/LM

Your Ref.

Please address your reply to the Chief General Manager

31st July, 1980

E. A. V. George, Esq.,
Bank of England,
Threadneedle Street,
London, EC2R 8AH

Dear Mr. George,

I regret the delay in coming back to your letter of the 5th June which has been occasioned by the necessity to take the views of a number of my colleagues and the incidence of annual holidays which has impinged on this.

Our views on the subject matter of the Green Paper are therefore now submitted in the form of the attached memorandum.

Yours sincerely,

A handwritten signature in cursive script, appearing to read "L. Lee".

Chief General Manager

ENCLS.

CMJ-03 1/85



THE BUILDING SOCIETIES ASSOCIATION

SECRETARY GENERAL
NORMAN E. GRIGGS, C.B.E.

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LEHW/PW

As from: Nationwide Building Society
New Oxford House
High Holborn
London WC1V 6PW

Nigel Lawson Esq MP
Financial Secretary to the
Treasury
Treasury Chambers
Parliament Street
London SW1P 3AG

1 August 1980

Monetary Control

Further to your letter of 20 March, I now enclose a copy of a memorandum setting out the views of the Building Societies Association on the Green Paper "Monetary Control" and the consultation paper by the Bank and the Treasury on possible developments in the methods of monetary control.

I am sorry if this paper is rather belated but there has, as you know, been something of a dialogue going on over the last few months between building societies and the Government on the place of building societies in the monetary system and one has wondered at what point it was desirable to pause and submit formal views.

I would be very happy to make myself available for further discussion with you or officials of the Treasury if you should feel it appropriate and, as is indicated towards the end of the memorandum, we may ourselves request an opportunity for discussion in the light of developments.

John Mason
Chairman

FINANCIAL SECRETARY	
REC.	- 5 AUG 1980
ACTION	MR BRIDGEMAN
COM. TO	PPS, PS/CST, PS/MSTC, PS/MSTL
	SIR DWISS
	MR RYRIE
	MR MIDDLETON
	MR UPWOOD
	MRS HIELDS
	MR RIDLEY

MR RILEY
MRS GILMORE

M. McC

MCC (80) 34

6 August 1980

COPY NO. 1

HER MAJESTY'S TREASURY
MONETARY CONTROL CONSULTATIONS

COMMENTS BY THE BSA
Note by the Secretaries

The attached memorandum by the Building Societies Association is circulated for information.

M D K W FOOT
M L WILLIAMS

H M Treasury

MONETARY CONTROL

Observations of the Building Societies Association

Introduction

1. On 20 March 1980, the Government published a Green Paper "Monetary Control" (Cmnd 7858). The Green Paper included a consultation paper by the Bank of England and the Treasury on possible developments in the methods of monetary control. The Government invited the views of the Building Societies Association.
2. On 21 May 1980, representatives of the Association had an exploratory discussion with officials of the Treasury and the Bank and, over the period since the publication of the Green Paper, there have been a number of formal and informal comments by representatives of Government and building societies which have touched on the place of societies in the monetary system. These are reflected to some extent in this response.

The System of Monetary Control

3. The Building Societies Association notes that the Government has decided to choose as its target for the purposes of monetary control the monetary aggregate known as Sterling M3 (£M3) - an aggregate which does not include deposits in building societies. However, the Green Paper makes it clear that £M3 may not remain the most appropriate aggregate in the face of long term changes in the institutional structure and this point was underlined in the speech made to the Annual Conference of the Building Societies Association in May 1980 by the Financial Secretary to the Treasury.
4. Because £M3 has been chosen as the appropriate monetary control target, the changes in monetary control techniques which have been made and suggested by Government as the means of achieving a smoother path in the growth of the money supply over the relatively short term are ones which apply specifically to the banking sector. They thus have no direct relevance to building societies and, indeed, it appears to be the policy of Government to continue to influence the part played by building societies in the monetary system in the long term by general interest rate policies and in the short term by consultation and persuasion. The Association does not therefore propose to comment on monetary base control or on indicator systems - issues which are specific to banks and which are specially mentioned in paragraph 6.4 of the consultation paper. There are, however, consequences which seem likely

to flow from the changes proposed by the Government and the Association wishes to comment on these.

Interest Rates

5. While different commentators have expressed different views, there appears to be a balance of opinion that the Government's intention to achieve smoother short-term growth in the money supply could result in more frequent and possibly wider fluctuations in the general level of interest rates. This is a prospect which building societies cannot view with equanimity for a number of reasons.

6. Although deposits in building societies are raised almost entirely from the personal sector, they now amount to about £45,000 million and include a growing proportion of money which is extremely interest-rate sensitive. While building societies have in recent years endeavoured, by the issue of term shares, to increase the proportion of their capital which is held in relatively stable form, more than 80 per cent of their capital is, in practice, withdrawable at very short notice. At the end of April 1980, 84.3 per cent of balances had a residual maturity of under one month; a further 3.2 per cent had a residual maturity of between one and six months; 6.3 per cent had a residual maturity of between six months and two years and only the remaining 6.2 per cent had a residual maturity of two years and over. Building societies are obliged therefore to keep their deposit interest rates closely in line with short term interest rates in the personal money markets and they have over recent years become increasingly vulnerable to fluctuations in those rates.

7. At the same time, 80 per cent of the total funds of building societies are invested in mortgage loans - almost all in relatively small sums to individuals for home purchase. Virtually all existing building society mortgages contain variable interest rate clauses which permit the rate of interest payable on loans to be raised or lowered on the giving of appropriate notice by the society. Theoretically, the variable interest rate mortgage should enable building society deposit interest rates to be kept in line with the market because any increase or decrease which is required in those rates can be compensated at relatively short notice by an increase or decrease in the rate of interest charged on existing as well as new loans.

8. In practice, however, this ability to adjust readily to prevailing market conditions has seldom proved possible of easy implementation. Apart from the requirement to give notice of interest rate changes to borrowers and the administrative problems of making consequential adjustments (often of an individual and personal nature) to monthly loan repayments, the rate of interest charged to borrowers (particularly existing borrowers) has become a matter of considerable public and political concern. In consequence, most building society interest rate adjustments are the subject of wide coverage and comment in the media and some desirable adjustments have been delayed and some undesirable adjustments brought about by strong political pressure.
9. As a result of this public and political attitude towards building society interest rates, the level of interest rates paid and charged by building societies is sometimes out of line with the market for periods of time, with the consequence that there are substantial flows of deposit monies between building societies and other deposit-taking institutions, particularly the banking sector. The nature and amount of these flows in recent years is illustrated in the appendix to this paper.
10. Methods are being explored within building societies with a view to enabling a more flexible response to interest rate changes and to ameliorating some of the consequences to borrowers. However, the Association wishes to make the point, that, having regard to the pre-eminently personal nature of their business and the role they occupy in the social as well as the economic life of the nation, rapid response to frequent and possibly wide fluctuations in the general level of interest rates is unlikely to be as easy for building societies as it is for other deposit-taking institutions. Nevertheless, if interest rates in the economy generally are to vary more frequently, it is probably for the benefit of building society investors and borrowers as well as for the monetary system as a whole that building society interest rates should follow, and this should be recognised by Government.

Competition

11. Another consequence which seems likely to flow from the changes proposed by the Government is greater competition between financial institutions in areas where they already tend to overlap. The building societies particularly envisage increased competition from the banking sector, especially from the major clearing banks which already have substantial connections with personal depositors and borrowers and large branch networks

equipped to deal with personal customers.

12. At this stage, it is not possible to forecast how energetically the banks propose to compete with the building societies for personal sector deposits and house purchase loans but lending by the banking sector for house purchase has been growing rapidly over the last year or so and, with the abolition of the Supplementary Special Deposit scheme, the major clearing banks have announced new schemes to attract and retain personal deposits. It is understood to be the desire of Government not to see any significant changes in the relative rates of growth of personal sector deposits held by, and house purchase loans made by, major financial institutions and this view has no doubt been made known to other financial institutions as well as the building societies. The relative rates of growth will obviously be carefully monitored.
13. However this may be, it seems evident that a more dynamic approach by other large financial institutions to the marketing of deposit and lending services in the personal sector cannot but affect the ways in which, and the terms on which, building societies conduct their business. Increased competition for personal deposits in particular would seem likely to lead to upward pressures on deposit interest rates with consequential effects, as far as building societies are concerned, on the rates of interest charged on house purchase loans.
14. There are, of course, quite considerable differences between the statutory powers, the methods of operation, and the administrative and other restrictions and requirements placed upon building societies as compared with other institutions and while much has been made of the competitive advantages alleged to be enjoyed by building societies, societies are in fact subject to many restrictions on the way they undertake their business and are certainly required to disclose a great deal more information of value to competitors than are other institutions. Building societies will be observing competitive developments with considerable care and, if necessary, will request the opportunity of discussing these developments at an appropriate time with an appropriate level of Government.

COMMERCIAL BANK DEPOSITS AND BUILDING SOCIETY INVESTMENT RECEIPTS

Personal Sector £m

	<u>Deposits with Banking Sector</u>	<u>Deposits with Building Societies</u>	<u>Building Society Advantage</u>
1967	740	1,090	350
1968	682	762	80
1969	308	890	582
1970	822	1,484	662
1971	953	1,961	1,008
1972	1,767	2,139	372
1973 1st qtr	451	438	-13
2nd qtr	844	755	-89
3rd qtr	900	482	-418
4th qtr	<u>1,186</u>	<u>513</u>	<u>-673</u>
	3,381	2,188	-1,193
1974 1st qtr	820	133	-687
2nd qtr	767	468	-299
3rd qtr	445	540	95
4th qtr	<u>941</u>	<u>828</u>	<u>-113</u>
	2,973	1,969	-1,004
1975 1st qtr	-62	907	969
2nd qtr	641	1,175	534
3rd qtr	220	986	766
4th qtr	<u>175</u>	<u>1,093</u>	<u>918</u>
	974	4,161	3,189
1976 1st qtr	-154 (-146)	1,180	1,334
2nd qtr	399 (218)	912	513
3rd qtr	657 (402)	695	38
4th qtr	<u>355 (355)</u>	<u>514</u>	<u>159</u>
	1,257 (829)	3,301	2,044
1977 1st qtr	-131 (-318)	811	942
2nd qtr	319 (53)	1,689	1,370
3rd qtr	193 (-67)	1,419	1,226
4th qtr	<u>176 (93)</u>	<u>2,013</u>	<u>1,837</u>
	557 (-239)	5,932	5,375
1978 1st qtr	308 (88)	1,259	951
2nd qtr	1,038 (697)	1,093	55
3rd qtr	1,087 (693)	1,048	-39
4th qtr	<u>723 (756)</u>	<u>1,449</u>	<u>726</u>
	3,156 (2,234)	4,849	1,693
1979 1st qtr	725 (611)	1,181	456
2nd qtr	1,681 (1,095)	1,399	-282
3rd qtr	1,863 (1,456)	1,394	-469
4th qtr	<u>1,896 (1,808)</u>	<u>1,645</u>	<u>-251</u>
	6,165 (4,970)	5,619	-546

Source: Financial Statistics - March 1980
Sterling Deposits only from 2nd quarter of 1975

Figures in brackets relate to individuals, households and personal trusts only, i.e. they exclude unincorporated businesses and private non-profit-making bodies.

ACCEPTING HOUSES COMMITTEE

Telephones: 01-481 1896
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Our Ref. AHC/550/C.

ROMAN WALL HOUSE,
2 CRUTCHED FRIARS,
LONDON, EC3N 2NJ

7th August 1980.

The Governor,
The Bank of England,
London, EC2R 8AH.

Dear Mr. Governor,

Monetary Control

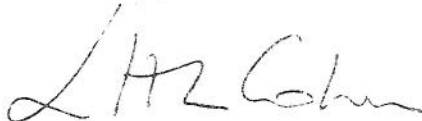
You will remember that you wrote to my Chairman on the 5th June, 1980 inviting the Accepting Houses Committee to comment on the Green Paper, "Monetary Control" (Cmd. 7858).

I subsequently spoke to Mr. Charles Goodhart to obtain an indication as to the timetable within which the considered comments of the Accepting Houses could be collated and communicated to the Bank. I indicated to Mr. Goodhart that I hoped to be able to submit the Committee's comments in the course of this present month.

I now enclose ^{1 att'd} 4 copies of a paper setting out the Committee's comments. I think that it represents the nearest that could be expected to a consensus on the part of the 16 Houses which could reasonably be expected on such a subject.

The paper is at present unsigned. Unfortunately my Chairman will not be back in his office until the end of August. He may wish to put some finishing gloss on to paper; but he did see it substantially in its present form and I do not expect it to be materially altered.

Yours sincerely,



L.H.L. COHEN
Director-General.

ACCEPTING HOUSES COMMITTEE

Telephone: 01-481 1896
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Our Ref. AHC/550/C.

ROMAN WALL HOUSE,
1-2 CRUTCHED FRIARS,
LONDON, EC3N 2NJ

7th August 1980

The Governor,
The Bank of England,
London, EC2R 8AH.

Monetary Control

You have asked for our comments on the Green Paper on monetary control with particular reference to the questions outlined in paragraph 6.4 of that paper. Before discussing these specific questions it may perhaps be best to outline our general approach to the subject.

The first point to be made is that we do not attribute the rapid rate of monetary growth experienced in this country in recent years primarily to defective techniques of monetary control. It follows that we do not believe that improvements in the techniques of monetary control can, in isolation, be expected to resolve these problems. Fiscal policy has been lax throughout the period of high monetary growth and few governments have ever run large and persistent fiscal deficits without experiencing high rates of monetary growth. (In this connection it is worth noting that we regard the argument that, adjusted for inflation, the public sector has been running a fiscal surplus as misleading and dangerous if used as a basis for policy: adjusted for inflation, government was in substantial surplus during the Weimar inflation).

The problem in the U.K. has been that the fiscal deficit has consistently been of a scale which required very substantial funding from outside the banking system. For much of the time this has been obtained, albeit at the cost of substantial distortion of the financial system, but the scale of the deficit has been such that any minor shortfall in funding has had substantial monetary consequences.

These problems have been exacerbated by the growing reliance of the public sector on the gilt-edged market as a source of funding. Up to the mid sixties a very substantial portion of the public sector's debt was held directly by the personal sector through channels such as National Savings, so that the public sector drew fairly evenly from the institutional and the personal savings market. During the decade from the mid sixties to the mid seventies this pattern changed radically with the public sector share of the personal savings market falling sharply while its share of the institutional market rose to a point at which other borrowers were effectively excluded.

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The Governor,
The Bank of England

7th August 1980

Thus a sharp rise in the public sector's borrowing requirement has been accompanied by a significant narrowing of its funding base. The monetary consequences of these two trends have been far reaching. First, the financial requirements of the public sector have become highly inflexible. Whereas in the fifties and sixties the authorities were largely concerned with debt management, by the latter half of the seventies they were committed to meet a demanding funding programme. In the process the authorities have relied almost exclusively on the stock market in which they were the only effective borrowers. The result has been that the public sector has not been able to accelerate the pace of its funding without influencing both the capital account and the savings of the personal sector.

Second, the corporate sector has effectively been excluded from the capital market and thus driven to rely almost exclusively on the banking market for its external funding. It should be stressed that this was not a necessary consequence of inflation but rather of the scale and determination of government funding operations. Where government has relatively modest funding requirements, as in the U.S.A., inflation may cause a hiatus in the corporate bond market but it will not kill it. The closure of the capital market to corporate borrowers in recent years has added very substantially to bank loan demand, and where the funding of this loan demand has conflicted with targets for £M3, sterling deposits held by overseas residents have made up the shortfall.

It should be evident from the above that the background to our views on the technical issues of monetary control is a firm conviction that the overall fiscal stance and funding policy of the public sector are of far more decisive importance. That being said, we would not suggest that the techniques of monetary control are without significance for both the choice of target and the precise control mechanism used to achieve it can have a significant impact.

The use of £M3 as the target monetary variable is now a well established practice in this country with which the markets are thoroughly familiar. The monetary base proposals would involve a radical shift away from this policy and we take the proposals in Chapter 5 of the Green Paper as evidence of a strong official predilection for retaining £M3 as the target monetary variable.

Our view is that reliance on a single monetary variable is inherently undesirable. There are both general and specific reasons for this. On general grounds the continuous structural evolution of the financial system makes it unlikely that any single monetary aggregate will remain an accurate measure of monetary growth over time. On more specific grounds experience has shown that attempts to control a particular aggregate will tend to distort its relationship to the system as a whole, a point well illustrated by the experience of the Supplementary Special Deposits Scheme. If targets were to be expressed in terms of a number of monetary aggregates such distortions would be less likely to occur and a better overall measure of monetary growth would be achieved.

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The Governor,
The Bank of England

7th August 1980

It may be objected that the maintenance of public confidence in the conduct of monetary policy requires the authorities to commit themselves to the control of a particular monetary variable. However, most active market participants are aware of the complexities of the financial system and for this reason watch the development of a number of monetary aggregates: market confidence in official policy is undermined when the authorities are committed to the control of a single monetary aggregate which is widely known to be distorted, not least by official controls. With regard to the wider public we consider that a broad commitment to the control of monetary aggregates will carry more conviction than a particular target for an aggregate whose composition is not understood. For these reasons we would argue that the confidence of both market participants and the public at large would be enhanced by a commitment to the control of a range of aggregates.

The choice of aggregates is obviously a matter for technical debate, but we would argue that measures of both liquidity and credit are required. Liquidity measures should range from measures of the banking system's liquidity through narrow and broad definitions of the money supply to a broad measure of liquidity in the economy. Measures of credit have become of much greater significance in the last year or so with the revival in sterling's international role and the relaxation of exchange control.

A preference for judging policy by reference to a number of aggregates must imply a general preference for the use of interest rates rather than reliance on specific quantitative controls. It does not however necessarily preclude control of specific quantities as a means of influencing the price of money.

The monetary base proposals are radical in two senses. First, they involve relying on the control of base money rather than on direct control over a broader monetary aggregate. Second, they involve acting directly on the volume of money rather than attempting to influence volume through acting on the price of money. The latter approach, in the absence of perfect information, involves a measure of judgement on the part of the authorities as to the level of interest rates needed to achieve a particular rate of monetary growth whereas monetary base proposals are inherently non-discretionary.

There are two distinct questions about the monetary base proposals which have to be answered. The first is whether they are practicable as a way of controlling the monetary system. The second is what the consequences of their adoption would be for the portfolio behaviour of banks and their customers and, by extension, for the economy as a whole.

A non-mandatory base system is, in principle, preferable to a mandatory base system in that it does not create artificial costs for the banking system and thus should not distort the system by inducing disintermediation. However two problems arise in connection with such a system. The first is that it assumes that banks will always find it prudent to carry a similar proportion of base assets in their balance sheets, which may not be true at all stages of the interest rate cycle. The second is that it implicitly assumes that base money is the only form of liquidity available to the banking system. If no discount facility is available it is true to say that base money

The Governor,
The Bank of England

7th August 1960

is the only absolute liquidity available to the banking system as a whole, but in practice short government paper has a high degree of liquidity for both bank and non-bank investors: U.S. Treasury Bills are prime liquidity even though the authorities in the United States do not customarily stand ready to discount them.

In a country such as Switzerland where the authorities have pursued extremely conservative fiscal policies over many years and there is consequently little federal government paper in the market, the supply of such prime assets is necessarily limited so that the banking system as a whole has no real alternative to base money as a source of liquidity. In such circumstances the control of monetary base is probably the most efficient way of controlling the money supply, but it is worth noting that against a background of fiscal conservatism such as has characterised the Swiss economy for many years the problems of controlling domestically-generated monetary growth are not excessive.

The level of the public sector's primary debt and the lack of fiscal conservatism in this country in our view precludes the introduction of non-mandatory base system. The introduction of a mandatory base system in this country would have a profound effect on the banking system. Reserve costs in this country have typically been low, in sharp contrast to countries such as the U.S. and West Germany, and this is reflected in the structure of our banking system.

The imposition of reserve or base costs on the U.K. domestic banking system would necessarily lead to a period of structural change in the banking system and its relationship to the broader financial system. For a time the figures for monetary growth would seriously understate the trend in the growth of liquidity and credit in the economy but this trend distortion would disappear as the adjustment was completed. It can be argued that such problems would be transitional and analogous to those associated with the introduction of Competition and Credit Control. This does not in our view justify ignoring the considerable risks involved in the transition to a mandatory base system.

If the transitional problems could be successfully overcome the workings of the system would depend on which of the two fundamental variants of mandatory monetary base described in the Green Paper was adopted. If all banking claims against the central bank were to be treated as base assets then day to day control of base assets would have to depend on the authorities maintaining an overfunded position and then using discretionary repurchase agreements to inject sufficient base assets into the system to achieve the desired level. Two issues arise from this. The first is that of access to repurchase agreements. These should in our view either be open to all competing banks or restricted to institutions such as the discount houses who do not compete directly with other banks. In this connection we note with approval the decision to open recent repurchase agreements to all listed banks.

The Governor,
The Bank of England

7th August 1980

The second issue concerns the assets against which the authorities are prepared to enter repurchase agreements: although this may appear a technical point it could be a cause of significant problems if the selection of assets were unduly narrowly defined.

We are confident that in principle base asset control could be managed on such a basis with the caveat that a very large public sector deficit would still produce significant strains. On the technical questions of whether the base asset requirement should be leading, coincident or lagging we are agnostic. There seems to be no fundamental reason to consider any of these systems unworkable and no doubt the banking system could adapt to deal with any of them. If we have a preference it would be for a coincident requirement. It should be noted that our confidence that such a system would be manageable depends on our judgement as to banks' likely portfolio behaviour under such a system which is set out below.

The other principal variant of mandatory base asset control set out in the Green Paper is the proposal to create Negotiable Entitlements (N.E.s). As the aggregate supply of these would be arbitrarily set by the authorities it cannot be doubted that such a system could be made to work in the technical sense. There are however two principal objections to such a scheme. First, the removal of pressure on the authorities to either control or fund its deficit could well lead to a dangerous build up of liquidity in the system. Second, the revenue potential of such a system from the official point of view could, if exploited, lead to a very high level of disintermediation.

The issue of disintermediation is crucial to the analysis of the various mandatory monetary base systems. The issue is not a simple one in that both corporate and public funding depend in the first instance on encouraging a process analogous to disintermediation (and both contribute to monetary control). If the public sector sells stock to a bank depositor and reduces its liabilities to the banking system the money supply falls but a similar process involving Treasury Bills although analogous in its initial monetary effect is in practice fundamentally different in that it is readily reversible. However, although these examples may be clear cut there are necessarily many which occupy a less clear cut middle ground such as transactions in floating rate stocks.

Under a mandatory base asset scheme banks would have to resolve the conflict between the desire of their commercial customers for flexible borrowing facilities and the authorities' determination to limit the growth of the base assets of the banking system. They would do so either by carrying excess base assets, which would be expensive, or by holding a growing proportion of their assets in a form which could be readily taken up outside the banking system. The important point to note is that profit maximisation would depend on developing an asset structure which could be cheaply and efficiently disintermediated in times of strong loan demand and reintermediated in times of

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The Governor,
The Bank of England

7th August 1960

weak loan demand. Thus the type of disintermediation and reintermediation encouraged by a mandatory monetary base system would be of little real significance in terms of either liquidity or credit even though it would keep monetary growth in the narrow sense under complete control.

For these reasons we would be opposed to a mandatory monetary base system.

The indicator proposals outlined in Chapter 5 of the Green Paper reject the substance of the monetary base proposals but would involve a major shift from a discretionary to an automatic system of interest rate adjustment, which it has been argued could reduce a bias towards delay in interest rate adjustment. As mentioned above we have considerable reservations about any system based on £M3 and as is outlined in the Green Paper. However, setting this question apart, there are a number of general points to be made about automatic systems even when, as proposed in the Green Paper, there is a residual power to over-ride the indicated rate.

The first concerns the potential instability of interest rates. The experience with market determined changes in MLR was not an entirely happy one and problems were experienced during periods of both rising and falling interest rates. In practice the authorities chose to over-ride the market frequently in the past and we see no reason to expect matters to be different in the future.

Whether the present system of discretionary changes in interest rates is necessarily biased towards monetary ease is in our own view debateable. There will always be pressures influencing the conduct of monetary policy and whether they are to over-ride an automatic change or to initiate a discretionary change the authorities must bear them. The real danger with an automatic system is that the authorities may be inhibited by the system from a proper exercise of their judgement and in consequence lose their direct responsibility for the outcome.

A more general point emerging from these questions concerns the significance of short term fluctuations in monetary growth. The official view as embodied in both the Green Paper and the recent Budget Report would seem to be that short term fluctuations in monetary growth do not matter in any objective sense in that the relationship between money supply and money G.N.P. is essentially a medium term relationship. Importance is nevertheless attached to such movements on the grounds that they affect market confidence, and indeed the indicator system would involve an automatic response of interest rates to such short term fluctuations. Our experience is that market participants share the official view that short term fluctuations in monetary growth are of little fundamental importance but watch them with great attention because they have learnt that they provide a good indicator of the authorities' immediate intentions with respect to interest rates and funding operations. In countries such as Switzerland and Germany the market accepts large fluctuations in the rate of monetary growth quite calmly because they have learnt by experience that the authorities' own policy actions will not be influenced by them.

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The Governor,
The Bank of England

7th August 1980

In sending you our comments we have treated the Green Paper in isolation. However these matters are closely related to both the issues raised by the paper on the Measurement of Liquidity and the promised paper on the Cash Requirement. For this reason we have been somewhat less specific on certain points than we might have wished, but we would hope to revert to them in the light of the continuing discussion with the Bank on the Liquidity paper and of the paper on the Cash Requirement.

Yours sincerely,