11. Monetary Control

Consultants

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HER MAJESTY'S TREASURY

MONETARY CONTROL CONSULTATIONS

CITY UNIVERSITY CONFERENCE

Note by the Secretaries

A note by Mr Pickford, recording the City University conference on 20 May, is attached. Also attached is a shorter note by Mr Foot summarising some of the points of interest arising from the discussion. A number of papers were available at the conference; as well as some already circulated in the TR(MON) series, these included: James Meigs "Monetary Control in the United States (May 1980) and George Rich and Kurt Schiltknecht "Targeting the Monetary Base - The Swiss Experience" (March 1980). Copies of either of these papers can be obtained from Mr Williams.

H M Treasury

M D K W FOOT
M L WILLIAMS

MONETARY CONTROL - CITY UNIVERSITY CONFERENCE

This note records the proceedings of the Conference on the Monetary Control Green Paper and the consultation paper on The Measurement of Liquidity held on Tuesday 20 May at the Glaziers Hall.

2. The note does not follow the Conference programme precisely. It is instead organised to cover the following topics:

1. The goals of monetary policy.
2. The theoretical arguments concerning the relative merits of controlling the monetary base or interest rates as a means of meeting money supply targets in the medium term.
3. International experience of monetary base control.
4. Practical considerations for the relative merits of monetary base and interest rate control.
5. Indicator systems.
6. Gilt-edged funding tactics.
7. The Bank's liquidity paper.

Many of the arguments in particular sessions (a copy of the programme is attached) crossed these boundaries, but hopefully this organisation will present the differences of opinion more clearly.

3. As a whole the Conference suffered from attempting to cover too much ground in too short a time. Therefore speakers tended to concentrate on restating their own positions rather than on responding to others' points. The two notable areas where the 'communications gap' was reduced somewhat were in combatting widespread belief that the Green Paper ignores the role of the supply side in monetary control; and in weakening the City's belief that the liquidity paper is the thin end of the wedge leading to strict control of banking business.

1. Goals of monetary policy

4. Professor Meltzer opened the Conference with a lucid argument that monetary policy cannot be used to achieve 'real' goals since ultimately it controls only the price level. If monetary policy was used to control interest rates or the exchange rate, the price level then became a variable rather than the control target. The first goal of monetary policy was therefore to reduce the level and variance of inflation to the minimum consistent with imperfections in market structure. Meltzer accordingly concluded that money supply growth in the long term should be set relative to real income, and that in the transitional period the growth rate targets should be progressively reduced.

5. There was general agreement (from Gordon Pepper, Griffiths et al) that inflation could be controlled through regulation of the money supply in the medium term (generally thought to be about 6 months). Harold Rose emphasised that the Government had to establish the credibility of its resolve to control the money supply in that medium term, but once that credibility had been established short-term control became less important.

2. Monetary base versus interest rates : theoretical considerations

6. Meltzer argued that the Green Paper was wrong to imply that monetary policy was equally effective whether it operated on the quantity of money or the price of money (interest rates or the exchange rate). He argued that it made little difference whether the authorities chose to control interest rates or the exchange rate since the two were linked via interest rate parity - the ratio between UK and US interest rates is related to the ratio between the forward rate of sterling against the dollar and the spot rate. Exchange rate intervention and intervention in the bond market have much the same effects, especially as the exchange rate is primarily determined by market expectations of the actual increase in base money relative to the increase in base necessary to achieve the money supply targets.

7. However, he saw a crucial distinction between operating on interest rates (or the exchange rate) and controlling base money. In monetary theory only unanticipated/permanent shocks, such as discovery of North Sea Oil or the election of a government committed to control of the money supply, affect the real economy. All other shocks can be absorbed by adjustments in interest rates. However, it is sometimes difficult to decide whether a change is permanent or transitory. If the money supply target is fixed via base control, permanent shocks can cause the rate of inflation to change permanently, but at least the market will be free to operate without additional uncertainty about the authorities' actions. If, however, the authorities alter interest rates in response to a shock and they misjudge whether the shock is permanent or transitory, they will anyway affect the real economy. And since the authorities are no better placed than the market to assess the effects of shocks, they are bound sooner or later to get it wrong.

8. Griffiths et al endorsed this view by emphasising that the great advantage of monetary base control was to reduce the uncertainty associated with monetary policy. By removing discretion from the authorities it removed their ability to react wrongly to shocks. Furthermore since politicians have an inbuilt predilection for low and stable interest rates, if they have discretion to act on interest rates their actions will always contain a bias. To resolve their desire to control both the quantity and price of money they are eventually led towards quantitative controls.

9. These arguments of principle were generally agreed (by default), but there was considerably less agreement about the desirability in practice of operating a non-discretionary monetary base system. These points are picked up in the fourth section.

3. International experience of monetary base control

10. Two papers were presented, one covering the Swiss experience of operating MBC with non-mandatory requirements, and the other piecing together the recent changes in the US Federal Reserve Board's system of monetary control.

11. Dr. Schietnecht outlined Switzerland's use of MBC since 1975. In 1975 the Swiss National Bank (SNB) adopted an M1 target, with the base chosen as the instrument of control. The decision to target on the base rather than on interest rates was not the result of a well-thought-out monetary theory, but rather because of institutional factors. The public sector in Switzerland is not very important - even in the 1970's they had no problems in financing the PSBR; and the lack of a well developed domestic money market makes it virtually impossible to use open-market operations. If (unlike in Switzerland) banks have virtually unlimited access to discount facilities and hold virtually no excess reserves, then in the short term the base is endogenous. But the SNB felt that active control of the base wold lead to medium-term control of the money supply, especially since the absence of complex reserve requirements made banks' behaviour relatively easy to predict. From 1975 to 1978 the SNB used a money multiplier model which assumed that banks only adjust their interest-earning assets in response to changes in the base which are expected to be permanent, so that daily control of the base was not necessary. This model produced satisfactory results - the deviations of actual M1 from the target were -1.6% in 1975, +1.7% in 1976 and +0.5% in 1977.

12. In 1978 the SNB intervened massively in the foreign exchange markets to prevent excessive revaluation of the Swiss franc, and because the monetary base could not be controlled without reducing the balance of payments surplus inflow controls were necessary. However, since expected appreciation of the exchange rate led to increases in the demand for money* measures to keep the money supply on target exacerbated the deflationary impact of the exchange rate appreciation. In spring 1979 the SNB returned to MBC, but with the target for the base fixed directly since the greater volatility of exchange rate expectations had caused a significant deterioration in the predictive power of the multiplier model. The monetary base is now the control target rather than M1.

13. Professor Meigs, who described himself as a professional 'Fed-Watcher', gave a brief description of US monetary policy in the 1970's. Before about 1970 there were no money supply targets. After 1970 the Fed began to pursue a wide range of money supply and interest rate targets,

*Relating deviations of actual M1 from predicted values to changes in the Swiss franc/dollar rate explained 85% of the variance.

and from 1975 it announced the money supply targets in advance. Although the Fed's open-market operations were intended to maintain a discount rate consistent with the money supply targets, they were far more successful in hitting the target for the Fed-funds rate than in meeting the money supply targets. As a result money supply growth was consistently above target; it also became more variable and highly procyclical.

14. In October 1979 the Volcker measures were introduced (and a description of them published in February 1980 after a period of considerable uncertainty). They put more emphasis on controlling banks' reserves directly. They are appropriate to the US institutional framework. Of the 14,000 US banks, 5,700 are members of the Fed and account for 70% of deposits. The Volcker measures extended reserve requirements, previously only imposed on Fed members, to all banks. Since all banks in the US are inter-connected via the money markets, any Fed moves to alter the level of reserves are quickly transmitted throughout the banking system anyway. Open-market operations are the principal policy instrument of the Fed, with the discount window only a vestigial feature. Meigs believes that open-market operations are capable of controlling the money supply over a period of months, but up to now have not succeeded because other policy targets have taken priority.

15. He sees the crucial difference introduced by the Volcker measures is to require the open-market operations manager to adjust banks' reserves so as to hit the money supply targets rather than the interest rate targets. The control process follows a number of steps : the Fed decides on the desired money supply growth rate over the next 6 months consistent with the published annual (fourth quarter on fourth quarter) targets; the desired growth of banks' reserves is established; reserves are broken down between member banks and non-members; changes in banks' liability portfolios and excess reserves are established; and reserves available from the discount window are estimated. Non-borrowed reserves become the operational target. This system is not a true monetary base system because it concentrates on the reserves component of the base;

and the lagged accounting framework accentuates interest rate volatility. However, Meigs believes that provided the authorities continue to accept more volatile interest rates (which would previously have been considered a sign of disorderly markets) the new system should enable the Fed to control the money supply. The extreme movements in interest rates seen so far are partly a reflection of the new system, but also stem from money market operators having to learn new rules and a number of conjunctural external influences.

16. In subsequent questioning it was generaly agreed that the Fed had partly been responsible for the interest rate volatility by fostering uncertainty about the new procedures and specifically about the availability of discount facilities. They were not expected to lead to a significant degree of disintermediation, although if this happened the Fed was still free to reduce the targets for the measured money supply accordingly. It was thought that the US financial system was stable enough to adjust to greater volatility of interest rates. A single dissenter (Michael Hamburger) questioned whether the Fed had given up total control of interest rates, suggesting that they might subsequently take precedence again over the money supply targets. Nevertheless so far the new system appears to be controlling the base effectively.

4. Monetary base versus interest rates : practical considerations

17. Discussion of the practical problems of different forms of control concentrated on the MBC adherents emphasising the difficulties in the present system (and the scheme of interest rates coupled with case ratios implied as a minimum-change alternative in the Green Paper); and the MBC opponents pointing out the problems of both mandatory and non-mandatory forms of MBC without generally answering the criticisms of the existing system.

18. All the MBC proponents (Meltzer, Pepper and Griffiths) stressed the necessity under the present system for the authorities to guess the level of interest rates consistent with money supply targets, with perhaps a 6-9 months lag before interest rate changes had the necessary impact on the demand for money. Harold Rose however pointed out that

an MBC system required a stable base multiplier relationship, so that it should be possible to test whether this or the demand for money function was a more reliable guide. No empirical evidence was presented, although Meltzer claimed a base multiplier relation would be more reliable.

19. The other main line of attack was to emphasise that giving the authorities discretion to set interest rates at a level not consistent with the money supply target merely invited them to use this discretion all the time. This would necessitate the introduction of quantitative controls. Michael Foot questioned whether discretion was necessarily undesirable - an automatic system ran less risk of the authorities acting too slowly, but it carried more risk of a movement in interest rates which had subsequently to be reversed. However, he did acknowledge the attraction that interest rates would be seen to be set by the market. Of the practical bankers, Mr Petherbridge (LDMA) expressed a preference for central bank discretion rather than automatic rules and Mr Weyer (Barclays) questioned whether it would not have been better to retain the corset.

20. On the general problems of MBC, Michael Foot and Peter Middleton reiterated that any major institutional change involved costs which would have to be weighed up against the putative benefits of a new scheme. Griffiths et al. acknowledged that this was a valid point; but Pepper thought that removal of the corset and the reserve asset ratio, coupled with the emergence of sterling as a petro-currency, would anyway force institutional changes so that the extra cost of a move to MBC would not be large. David Lomax expressed the opinion that the City viewed the costs of transition as small, and they would be prepared to operate under any rules provided they were made clear; Petherbridge on the other hand thought a gradualist approach was the correct path.

24. Both Griffiths and Lomax questioned the Green Paper assertion that MBC would lead, via liability management, to more volatile interest rates. Although MBC was likely to increase the volatility of very short-term rates, the reduction in uncertainty about the authorities' role would if anything reduce the volatility of longer-term rates. Indeed under the present system interest rates had exhibited very large swings.

22. There was little discussion of the problem of disintermediation, although Weyer thought that a mechanical control system, coupled with a detailed prudential system, would encourage disintermediation overseas. Most speakers were much more concerned about the potential effect the liquidity proposals would have on the ability of the City to retain business, and this is discussed later.

23. Pepper, in support of an MBC system with mandatory requirements, agreed that the transitional problems would be minimised with this form. Griffiths et al. opposed a mandatory scheme because it represented a tax on banks, although Foot questioned why the tax had to be large. Griffiths also seemed to have an ambivalent attitude to the transitional costs of a non-mandatory scheme - the costs would be large, but the changes in institutional structure were desirable on wider efficiency grounds. Charles Goodhart reiterated the view in the Green Paper that a mandatory system would lead to disintermediation, and that a non-mandatory system which worked (because the Bank's lender of last resort facility was curtailed) would carry with it prudential risks. Rose saw some advantage in rationing individual banks' recourse to discount facilities along US lines, so that they would be forced to hold excess reserves.

24. Lomax, Pepper and Rose all commented that to some extent the liquidity paper preempts monetary control since the quality of paper which the Bank is prepared to rediscount (and hence qualifies as 'primary liquidity') determines partly the Bank's role as lender of last resort. However, Peter Cooke was at pains to divorce the liquidity paper and the Green Paper - the liquidity proposals were designed solely for prudential supervision, not for monetary control.

5. Monetary base indicator systems

25. There was little discussion on MBI systems. Griffiths et al. dismissed them as variants of the present system. Weyer agreed that if the authorities had discretion to override the MBI rate they would probably use that discretion continuously. Foot repeated that MBI systems were included in the Green Paper as systems which removed discretion from the authorities but avoided the structural upheaval which MBC would entail.

Lomax was not in favour of MBI systems, but thought that some element of discretion was essential for them to work. He also saw no advantage in linking the MBI to base because the authorities might as well control the base directly. If the system was linked to £M3 there was some merit in not publishing the decision rule used to trigger interest rate changes, since this would reduce the extent to which the money markets tried to second-guess the authorities.

6. Gilt-edged tactics

26. Again little time was devoted to this. Pepper (who introduced himself as a gilt-edged broker) argued that a tender method for marketing long-dated gilts was not necessary since an MBC system would rule out hiatuses in funding. Petherbridge regretted that the Green Paper had dismissed changes in gilts techniques in such a peremptory fashion. He thought that within the existing framework of monetary control a more aggressive pricing policy for long taps would be preferable to operating on short rates.

7. Consultation paper on The Measurement of Liquidity

27. A new departure in the liquidity paper is the unified approach combining the measurement of liquidity of the banking system as a whole and of individual banks. Both Pepper and Franco Redi (Citibank) were against this unified approach. Pepper was of the opinion that the liquidity of the system as a whole should have been covered in the Green Paper since it was an integral component of monetary control. Redi argued that it was a matter only of concern to the Bank, and to link it with the liquidity of individual banks led to confusion; individual banks could not create liquidity except by holding negotiable paper. Petherbridge (LDMA) on the other hand welcomed the unified approach. He saw the role of the discount houses as to provide a market in liquidity. A shortage of liquidity in the system as a whole would only be manifested on the books of the discount houses since individual banks would attempt to play 'pass the parcel'.

28. A number of speakers expressed concern (to some extent unfounded) that it was inappropriate to apply a single liquidity test to every bank, when they displayed such different characteristics. Lomax suggested that

variable, non-mandatory liquidity requirements might be desirable to give the necessary flexibility; while Redi was concerned that the proposals would force all banks to adopt the same liquidity strategy. Cooke, in reply to these criticisms, was at pains to stress that the liquidity paper was very much designed for consultation; that it was concerned with the measurement of liquidity rather than prudential control; that the appropriate level of liquidity would be decided on a case-by-case basis, taking into account the different characeristics of individual banks; and that the only requirement proposed is that banks should hold primary liquidity (expressed as a norm rather than as a minimum).

29. The liquidity proposals caused worries about the effects on the banking system. These worries fell into three main categories : that banks would be less able to meet customers' needs, especially from companies; that business would be forced overseas; and that wholesale banks would be harder hit by the proposals than the retail banks. Both Redi and Weyer thought the proposals would discriminate against maturity transformation. Banks have traditionally borrowed short and lent long, which enabled them (for example) successfully to recycle the OPEC surplus and to finance industry despite the virtual demise of the commercial bond market. The proposals would adversely affect banks' ability to continue performing these functions. On a more detailed point, the proposals were thought to lead to the decline of the overdraft system because of maturity-uncertainty; but the Bank subsequently affirmed that some notional maturity would have to be attached to overdrafts.

30. Redi argued that the liquidity proposals would adversely affect the business of all UK-based banks. He warned that excessive legality of prudential supervision and excessive levels of liquidity requirements (since holding primary liquidity has an opportunity cost) would simply push business away from the banking system towards non-regulated institutions and markets, such as Luxembourg. Cooke replied that any increase in regulation carried the danger of disintermediation, but emphasised that it would be linked in with a more integrated system of international supervision, in particular supervision of euromarkets. He echoed the Governor's speech of the same day that it was by no means the Bank's intention to see the decline of London as an international financial centre.

31. Many speakers (Lomax, Redi and Weyer) saw the liquidity proposals as discriminating against wholesale banks in favour of retail banks. The favourable treatment of retail deposits (maturity-uncertain) as against wholesale inter-bank deposits for liquidity cover was singled out for criticism, although Cooke argued there was some evidence that maturity-uncertain deposits were more sticky than maturity-certain. The increasing liquidity requirements of loans nearing maturity was regarded as anomalous, and the uncertainty about treatment of roll-overs and stand-by credits caused particular worries.

32. A number of specific points were made about the treatment of different components of liabilities and liquidity. Redi and John Cooper (BBA) saw the distinction between interbank and non-interbank sources of funds as a false one; and Lomax foresaw it pushing the wholesale banks in particular away from liability management. Also th e distinction between eligible and ineligible bankers' acceptances was criticised, but for differing reasons. Petherbridge was concerned that banks should not hold all their primary liquidity in the form of eligible acceptances, whereas Redi thought that the scope of primary liquidity should be extended to include wider eligibility of bills and currency swaps. Redi went further to argue that since secondary liquidity was not in practice a readily realisable source of funds, there should be no requirement on banks to hold secondary liquidity.

Conclusion

33. The last word of the Conference belonged to the Green Paper. In the last session there seemed to be a greater awareness of the arguments on both sides of the debate for and against monetary base control. On the one hand officials (Messrs Middleton, Bridgeman and Goodhart) stressed that a step change to MBC which involved transition costs could on ly be undertaken if there was a reasonable certainty that the benefits of better control of the money supply outweighed those costs. On the other hand MBC proponents (Messrs Meltzer and Hamburger) argued that the present system (and/ the Green Paper's proposed default system of PSBR, interest rates and cash ratios) carried such heavy costs, mainly through inexactitude of control and the resultant uncertainty, that the benefits of a system offering better control were overwhelming. On this point both sides agreed to differ.

THE CENTRE FOR BANKING AND INTERNATIONAL FINANCE

THE CITY UNIVERISTY

MONETARY CONTROL

A One-day Conference on the Government's Green Paper on Monetary Control and the consultative document on The Measurement of Liquidity will be held on Tuesday, 20th May 1980 at Glaziers Hall, 9 Montague Close, London SE1.

PROGRAMME

9.15 - 9.45am	Introduction to Monetary Control	PROF. A. H. MELTZER Carnegie-Mellon University
9.45 - 11.00am	A Critique of the Green Paper and consultative document	PROF. B. GRIFFITHS MR R. A. BATCHELOR MISS E. BENDLE MR G. E. WOOD Centre for Banking & International Finance The City Univeristy
	DISCUSSANTS:	MR M.D.K.W. FOOT Bank of England MR D. LOMAX National Westminster Bank
11.15 - 12.45am	Foreign Experience of Monetary Control: Switzerland and the USA	DR. K. SCHILTNECHT Swiss National Bank PROF. J. MEIGS Claremont Mens College, California
12.45 - 14.15pm	LUNCH	

14.15 - 15.45pm	Views from the City on the Green Paper and Liquidity document	MR F. REDI Citibank N.A. MR G. PEPPER Greenwells & Company MR R. PETHERBRIDGE Union Discount Company of London MR D. VANDER WEYER Barclays Bank Limited
16.00 - 17.30pm	PANEL DISCUSSION	PROF. B. GRIFFITHS Chairman MR P. COOKE Bank of England MR P. MIDDLETON H.M. Treasury PROF. H. ROSE Barclays Bank Limited MR A. H. MELTZER Carnegie-Mellon University USA MR J. COOPER Singer & Friedlander Ltd

NOTES ON PARTICIPANTS

Professor A.H. Meltzer: Maurice Falk Professor of Economics and Social Science at Carnegie-Mellon University, USA. Along with Professor Karl Brunner he was responsible for developing the concept of the monetary base method of control and has been active in research and public discussion on monetary policy in the US.

Mr M.D.K.W. Foot: Assistant Adviser at the Bank of England specifically concerned with problems of monetary policy.

Mr D. Lomax: Economic Adviser to National Westminster Bank and editor of the Bank's Quarterly Review.

Dr. K. Schiltnecht: Head of the Economics Department at the Swiss National Bank, Zurich.

Professor James Meigs: Chairman of the Claremont Economics Institute, Claremont, California and has written widely on the money supply process in the US.

Mr F. Redi: Senior Vice-President of Citibank, N.A., in charge of treasury operations.

Mr G. Pepper: Partner in Greenwells & Company and author of their Monetary Bulletin.

Mr R. Petherbridge: Senior Managing Director of the Union Discount Company of London and Chairman of the London Discount Market Association.

Mr D. Vander Weyer: Vice-Chairman of Barclays Bank Limited, Chairman of Barclays Merchant Bank Limited and President of the Institute of Bankers.

Mr P. Cooke: Head of Banking Supervision at the Bank of England.

Mr P. Middleton: Deputy Secretary at H.M. Treasury with specific responsibility for monetary, fiscal and industrial policy.

Professor H. Rose: Group Economic Adviser to Barclays Bank and Professor of Finance at the London Graduate School of Business Studies.

Mr J. Cooper: Managing Director in charge of all commercial banking operations at Singer & Friedlander and Chairman of Executive Committee of the British Bankers' Association.

THE CITY UNIVERSITY CONFERENCE (20 MAY) ON MONETARY CONTROL

1 This note summarises the points of interest arising from this Conference, concentrating on what was new (to me) rather than on restatements of position and omitting discussion of the Liquidity Paper except where clearly relevant to monetary control.

2 Professor Meltzer's (Carnegie-Mellon University) opening address covered familiar ground. Only non-transitory unanticipated shocks to the money stock affect real output; the difficulty for a central bank in distinguishing between transitory and permanent shocks when they first occur is the justification for operating a money or base control rather than an interest rate policy. Meltzer wanted the central bank to control the base (by operating on its assets) over a fairly short time period, such that the money stock definition considered most important could be kept to within 1%-1½% of the target over a quarter. It became clear later than Meltzer favoured a non-mandatory cash ratio approach to base control, or if there were mandatory requirements then interest should be paid on them.

3 The first main paper - by Griffiths, Wood Batchelor and Bendle (City University) also covered familiar ground, being essentially their submission to the Select Committee. The authorities should not have discretion over short-term interest rates; they should target the base in the context of a non-mandatory system and lending of last resort should genuinely be last resort.

4 David Lomax and I discussed the paper. My emphasis was on the importance of one's priors (eg, on the importance of short-run stability of the money stock) and on the points that doubters of the Griffiths line would put at each stage of his arguments - all familiar stuff. In addition, I sought to establish the difficulty we have had in understanding the assertion that MBC systems might lead to an interest rate/quantity of money equilibrium different from that reached under the present system. This was not taken up in subsequent discussion but, over lunch, Roy Batchelor (one of the authors of the paper) denied any such assertion, on his part at least.

5 Lomax's (National Westminster) contribution followed his draft paper on the Green Paper (circulated as MCC4) and contained the same

ather strange mixture of comments. He clearly sympathised with MBC roposals and made the very valid point that the indicator approach ested on encapsulating an enormous range of possible circumstances n one pre-announced policy rule.

6 In general discussion, Geoffrey Wood accepted the point that the ore confidence markets had in the underlying strength of the Government's resolve, the less he would be concerned about short-run fluctuations in the money stock.

7 The last session before lunch covered foreign experience with the base and comprised Kurt Schiltknecht with his now-familiar survey of policy at the Swiss National Bank and American James Meigs (Claremont). Schiltknecht again made clear the fact that the Swiss had not sought to use their system to obtain short-run stability of the base or money (indeed, as I pointed out in discussing Griffiths' paper, it is hard to see how the approach could be used in this way). He also commented briefly that the base multiplier in Switzerland had become less predictable since 1978 because - it seemed - of the impact on the money stock of changes in exchange rate expectations. Meigs added nothing of value to our existing information on the position in the USA since 6 October.

8 The first of two panels in the afternoon brought together four City views on the Green Paper and the Liquidity Document. Pepper (Greenwell's) began the session and, although much of what he said was familiar, he did, for the first time (I think), dismiss the indicator system outright as representing the worst of the present and of the MBC worlds. He also repeated the comment he made at the Money Study Group on 16 May to the effect that his mandatory requirement proposal was a first step towards a Swiss-type system; he has clearly been disturbed by the lack of support for his own proposals.

9 Pepper was followed by Petherbridge (Union Discount) who concentrated on the liquidity proposals. On monetary control, his vote goes in favour of discretion by the authorities on short-term interest rates and also for greater aggression on their part in the gilt-edged market.

10 Redi of Citibank talked exclusively about liquidity. Vander Weyer (Barclays) in contrast covered a wide range of interests. Surprisingly, he had some kind words for the "corset", as he favoured a flexible

approach to monetary control which could get "a bit blurred round the edges". He also made the interesting remark that the clearers would r[illegible] in subject to political and social pressures to put their interest rates up last and bring them down first; if, therefore, a new system of control meant more volatile interest rates, arbitrage (round-tripping) would be an even greater problem than at present. Arguing against his own book he was not in favour of overprotecting retail banking, as the result would be a less flexible and competitive system overall. However, he was anxious that the authorities should not underestimate the value to the economy of the overdraft system and that they should get clear in their own minds whether they wanted to encourage banks to lend for longer periods (as they had done in recent years) or not (as implicit in the new prudential proposals).

11 The second panel session turned into a series of questions from the floor aimed at Messrs Cooke of the Bank and Middleton, later Bridgeman, of HMT. These, in general, followed well-worn lines but many questioners seemed grateful for the opportunity to air their thoughts. Professor <u>Rose</u> (Barclays) also spoke for a few minutes, essentially summarising his submission to the Select Committee (circulated as MCC6). He clearly gives the present system higher marks than he might have done a year ago and also clearly accepts the need for a fairly active lender of last resort facility on a daily basis. Beyond that the central question for him (in which he seems far from decided) is the relative predictability of (i) the base to money ratio and (ii) the interest elasticity of the demand for money.