

CONFIDENTIALEconomic Reconstruction Group

Minutes of the meeting held at 10.00 a.m.  
on Thursday, 11th December, at the  
House of Commons.

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Present: Sir Geoffrey Howe (Chairman)  
Mr. Biffen  
Mr. Griffiths  
Mr. Howell  
Sir Keith Joseph  
Mr. Gott  
Mr. Prior  
Mr. Gilbert

Mr. Ridley } (Secretaries)  
Mr. Cardona }

Apologies: Mr. Gilmour  
Sir Leonard Neal  
Mrs. Oppenheim

1. Sir Geoffrey Howe explained that shortage of time made it impossible to circulate to the Group the paper on the economic situation and its implications which would shortly be submitted to the Shadow Cabinet. However the paper would accurately reflect the Group's discussions.

Monetary Policy

2. There was a discussion of Mr. Griffiths' paper on monetary policy. Mr. Griffiths explained two alternative views of the conduct of monetary policy since the introduction of Competition and Credit Control (CCC). The Bank of England's view now was that both the demand for and supply of money are unstable, and that the monetary aggregates must be controlled by ceilings rather than interest rates. The alternative view was that the Bank of England had failed to control the money supply through the reserve asset system, that the demand for money was stable, and that many of the failings of CCC had been because of political pressures on interest rates.
3. There was a discussion of the reserve asset system. The banks could expand lending simply by depositing more call-money with the discount houses, who in turn used the money to expand their holdings of Treasury bills. The Bank of England had wanted to subsidise the discount houses; but we should look at the possibilities of moving to control through the total cash base, as in the USA and Germany.
4. The political pressures that prevented interest rates moving freely were discussed. It was thought possible that with proper monetary management, one would not be placed in a position such that one would have to treat mortgage borrowers harshly. It was pointed out that if interest rates rose, there were still the options of subsidising mortgage borrowers either through the building societies or through taxation. While recognising political realities, it was on the other hand felt that there should be a reluctance to give in to special pleading by groups such as owner-occupiers or farmers.
5. There was a discussion of the relationship between increases in the money supply and inflation, and of whether the increase in 1972-73 was genuine. Mr. Griffiths felt that although 'round-tripping' by firms had inflated the M3 statistics, there had nevertheless eventually been an impact on the rest of the economy.

because when corporate redeposits were withdrawn from the banks a certain proportion of them created effective demand. Mr. Ridley suggested that the changes in real demand that occurred in 1972-73 would probably have taken place even if there had not been spectacular growth in the monetary aggregates. On the other hand - monetary expansion had clearly affected asset prices, rents, mortgage costs, interest rates and inflationary expectations, and built up pressures which manifested themselves in 1974-5.

6. It was agreed that it was impossible to prove conclusively whether the relation between money supply expansion and inflation was one of cause and effect. But there was no doubt that the monetary side of economic policy had been neglected in the past, and that this was a mistake against the repetition of which we should have to guard.

Questions for further consideration

7. The Chairman identified the following questions as ones of high importance:-
- 1) Is it legitimate to attempt to reinstate CCC?
  - 2) Are selective credit controls needed?
  - 3) Are selective hire purchase controls needed?
  - 4) Should control through the banks' cash base be attempted?
  - 5) What was the relationship between the recent problems of monetary policy and inflation in the UK and the partially comparable problem of development world wide?
  - 6) What were the consequences of our monetary policy for our pledge about mortgage interest rates?

additions to this list would be made.

8. It was decided that the Group would meet every fortnight in the New Year.

George Cardona