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Please pass to Richard Ryder

PM

The PM might possibly be interested to glance at this. It will be in the Paper on March 3.

Sorry for the bad photostat.

Sam Brittan

PM

Corrected Proof

Proof Only 60
FOR MONDAY

LOMBARD

Beware still of bank advice

BY SAMUEL BRITTAN

THE CASE for a central bank, at arm's length from the government of the day, has been made in different ways. Professor Milton Friedman has often proposed that the U.S. Fed, which is already independent on paper, should be under an obligation to maintain the growth of the money supply within a stated range, to be departed from only in prescribed emergency conditions. Mr. Peter Jay, before he went to Washington, suggested that Parliament should establish an independent Currency Commission, bound by a similar formula, of which the Bank of England would become an executive agency.

Rules

Sir Geoffrey Howe, when Shadow Chancellor, once suggested that the Bank of England should be directly responsible to Parliament via the appropriate Select Committee. He did not elaborate a great deal; but the object of any sensible reform is surely not to give the Bank, whose directors are neither elected by voters nor chosen in the market place, discretion to do what it likes, but to make it subject to rules. These could in principle be Parliamentary, although the British system would make that difficult.

It is noteworthy, however, that the Bank of England has not been pushing for any of these changes. And with good reason from its own point of view. For although such plans might loosen Ministerial reins, they would also reduce Bank of England discretion. The Bank, as at present constituted, has a vested interest in opposing all elements of automaticity or guidelines. It prefers the real if undefined powers it possesses from discretionary action in the financial markets and from being able to put in a word in high places to any more automatic framework. If we are to have a monetary constitution, the central bank would look very different to today's Bank of England. ~~While it is probably right that the Governor should sit on NEDC, this is in no sense a triumph for the~~

of England. ~~While it is probably right that the Governor should sit on NEDC, this is in no sense a triumph for the monetary approach.~~

Meanwhile, there is little ~~on~~ in the record of that institution which would make one wish it to have particular influence with the Prime Minister or the Chancellor. In the 1920s, Montague Norman discredited sound money for two generations by pulling the wool over Churchill's eyes and persuading him to go back to gold at an overvalued parity. In the 1950s and 1960s many people were put off anti-inflationary policies by the sheer badness of arguments put up on their behalf by the Bank. Then in the late 1960s, the Bank used its influence to delay devaluation, thus increasing its pains. Although the prime responsibility for the monetary explosion of the early 1970s was with the Heath Government's "dash for growth," the Bank was all too ready to provide rationalisations for what occurred, together with plenty of errors of its own.

The top levels of the Treasury and Bank must share responsibility for the delay in establishing monetary targets in the middle 1970s and the resulting traumatic negotiations with the IMF. The Treasury dragged its feet more on the idea of the target and the Bank more on the means of implementation. The targets—whose complete fulfilment has been a good deal better than nothing — were mainly due to the work of middle - level officials, with occasional encouragement from Mr. Denis Healey himself. In the U.S. a good case can be made for the view that the country had more monetary stability before the establishment of the Fed in 1913 than after.

A study of Bank of England Governors' speeches suggests that the Bank line has for a long time been to favour a mixture of pay controls with some short-term and discretionary monetary guidelines. At a more technical level the Bank of England's archaic method of selling stock, which works by creating crises and giving a free ride to gilt-edged speculators must bear some of the responsibility for recent failures of monetary policy. As for the design of the ill-fated variable interest stock, the less said the better.

Headmaster

~~Just as Mr. Jim Prior's consultative documents on union law are merely a springboard for discussion, the same applies to the forthcoming paper on monetary control.~~ Part of the trouble is that the Governor of the Bank of England sees himself not merely as a central banker, but as headmaster of the whole financial system~~, and to some extent of the whole corporate sector.~~

Of course Mr. Gordon Richardson has particular experience in these areas, which is all to the good under present arrangements. But what would one not give for someone who was content to be judged in terms of his success in maintaining pre-announced medium-term monetary guidelines — which would be perfectly compatible with a "lender of last resort" function?