Bank of England

Report and accounts for the year ended 28 February 1977

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Issued by Order of the Court of Directors 7th July 1977

Printed by Blades, East & Blades Ltd, London

ISSN 0308-5279

Court of Directors

28th February 1977

The Rt Hon. Gordon William Humphreys Richardson, MBE, *Governor*
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George Adrian Hayhurst Cadbury, Esq.[1]
Sir Robert Anthony Clark, DSC
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Sir Lionel Alexander Bethune (Alastair) Pilkington, FRS
The Rt Hon. Lord Robens of Woldingham, PC
Sir Eric Roll, KCMG, CB[2]
The Rt Hon. Viscount Weir

The terms of office of Mr C. W. McMahon, Mr J. C. R. Dow and Sir Robert Clark expired on 28th February 1977; they were reappointed for a period of four years.

[1] Created a Knight Bachelor in June 1977.

[2] Sir Eric Roll retired as a Director when his term of office expired on 28th February 1977. He was created a Life Peer in June 1977.

Senior Officials

28th February 1977

Departmental

Chief Cashier	J. B. Page
Chief Accountant	G. J. Costello
Chief of the Overseas Department	S. W. Payton, CMG
Chief of the Economic Intelligence Department	M. J. Thornton, MC
Chief of Exchange Control	E. B. Bennett, DSC
Banking Supervision	W. P. Cooke
Chief of Administration	P. A. S. Taylor
Chief of Establishments	K. J. S. Andrews, MBE
General Manager of the Printing Works	M. J. S. Cubbage, MBE

Adviser to the Governor

Sir Henry Benson, GBE

Chief Advisers

J. A. Kirbyshire

M. J. Balfour

Secretary of the Bank G. C. Gough

Introduction

This *Report* relates to the year ended 28th February 1977. The economic and financial events of last year, and the operations in which the Bank were involved, have already been described in detail in the relevant issues of the *Quarterly Bulletin*. The purpose of this *Report* is to give a brief account, in the context of the year as a whole, of the Bank's operations in areas where their responsibilities lie.

The first part of this year was a period of financial difficulties for the United Kingdom and also, therefore, for the conduct of monetary policy, both domestic and external. These difficulties required a progressively firmer monetary policy, but were not finally surmounted until the budgetary measures in December.

As will be clear, then, in the year under review the main financial markets in which the Bank operate went through two distinct phases. Up to November, sterling depreciated sharply at times, and interest rates were generally rising. Towards the end of 1976 there was a marked improvement in confidence, particularly after the conclusion of negotiations with the International Monetary Fund: sterling came into heavy demand, interest rates began to fall, and a record amount of gilt-edged stocks was sold in the December quarter. Confidence was further strengthened in January by the agreement in principle with the Bank for International Settlements, supported by a group of eleven countries, on a facility related to official sterling balances.

There were a number of new developments in monetary policy of considerable significance. The most important of these was the increasingly explicit public commitment to monetary targets. Although policy had for some time been designed to achieve an appropriate rate of growth in money supply, the public adoption of quantitative targets introduced a new dimension into the conduct of policy and especially into the management of official operations in the gilt-edged market. A related development around the end of the year was the initiation of new types of government stock on offer to the public.

Part 1 of this *Report* summarises the Bank's operations in domestic and exchange markets, both in pursuit of domestic monetary policy and in the discharge of policy relating to the exchange rate and the reserves.

The Bank's responsibilities for the supervision of the banking system were further developed during the year and will be extended to cover other deposit-taking institutions when the legislation envisaged in the August 1976 White Paper is enacted. Continued progress has also been made in the support operations undertaken by the Bank (and the members of the support group).

Part 2 contains a series of notes on these and other responsibilities and activities of the Bank. The Bank's accounts are shown in Part 3.

Part 1 Monetary and exchange rate policy

The conduct of monetary policy was heavily influenced by the state of the foreign exchange market, which is described first below. Later sections discuss the increasing emphasis on explicit monetary targets and give details of the Bank's operations in gilt-edged stocks in this context.

Foreign exchange operations

There were two phases in the course of the exchange rate during the year under review. Until November, the underlying tone was weak: periods of uneasy calm were interrupted by days when sterling depreciated sharply in extremely nervous markets. After November, the trend was reversed, with bouts of heavy demand causing the pound to appreciate markedly at times. Sterling's effective exchange rate index fell during the year from 72.2 to 61.8;[1] and the exchange rate against the dollar fell from \$2.02½ at the beginning of the period to a low point of \$1.55½ on 28th October, before recovering to \$1.71¼ by the end of February 1977.

The United Kingdom's relatively fast rate of price inflation, together with a continuing large trade deficit, made some decline in the exchange rate during 1976 almost inevitable. Expectations of such a decline led to a series of responses which accelerated the fall – traders engaged in 'leading and lagging' (i.e. they advanced sales or delayed purchases of sterling); overseas holders moved out of sterling; and banks abroad took positions against the pound by borrowing sterling and then selling it. Changes in market sentiment, arising from unfavourable economic or political news, at times exerted very strong downward pressure on the rate, which the foreign currency resources of the Exchange Equalisation Account were insufficient to contain.

Within this tight constraint, it was the aim of policy to moderate downward pressure on the rate. However, on days when pressure was particularly intense, it was sometimes necessary to withdraw temporarily from the market and return later in an attempt to restore more settled conditions at a lower rate. In order to provide additional support for the exchange rate at a minimum cost to the reserves, the Bank occasionally 'borrowed' sterling in swap transactions, by simultaneously buying spot and selling forward sterling, thereby raising the cost of such transactions to other operators (see the December 1976 *Quarterly Bulletin*, page 430).

The rate steadied in November before appreciating in the following two months. The agreement between the Government and the International Monetary Fund on a stand-by arrangement reassured the market. And other factors contributing to a stronger demand for sterling included exchange control measures severely restricting the use of sterling in third country trade,[2] the arrangement to finance certain reductions in official sterling balances, the reversal of leads and lags in commercial payments, and the announcement of a \$1.5 billion medium-term loan to the Government (see page 17).

On 9th December the \$1.5 billion drawing on the stand-by provided by a group of central banks in the previous July was repaid, leaving the reserves seriously depleted. It was therefore a first priority of policy to take every opportunity to rebuild the reserves to a level where control over the exchange rate could be re-established and conditions of stability better assured. To this end, and also because much of the

[1] See March 1977 *Quarterly Bulletin* (page 46).
[2] See *Quarterly Bulletin* for September 1976 (page 310) and for December 1976 (page 412).

inflow was in any case of a once-for-all nature (arising from the change in exchange control – see footnote 2 on page 6), the Bank intervened frequently as the exchange rate appreciated: a total of \$3.7 billion, including the \$1.1 billion from the IMF, was added to the reserves during January and February while the rate settled at between \$1.70 and \$1.72.

In carrying out their exchange rate policy the Bank remained in close contact with other central banks. The main European central banks formally exchange information on their foreign exchange markets four times each day, and the Bank also maintain daily contacts with other central banks, in particular the Federal Reserve Bank of New York.

The Bank's foreign exchange operations included the normal volume of commercial business on behalf of customers – mainly government departments and overseas central banks. The Bank also continued to manage the \$2.5 billion euro-dollar loan to the Government announced in March 1974, as well as handling the \$1.5 billion loan mentioned above.

Monetary policy

Over the year as a whole, the monetary aggregates rose more slowly than GDP in money terms; and domestic credit expansion was kept well within the limit for the year to mid-April 1977, which was agreed with the International Monetary Fund in December 1976. But for a time during the late summer of 1976, the money stock expanded rapidly when a sharp increase in bank lending coincided with large public sector borrowing and a pause in the demand for government stocks.

The early months of the year

At the beginning of the period, external considerations became the predominant influence on monetary developments. From March until November, sterling came under bouts of pressure, interspersed with intervals of uneasy calm. In the first such interval – late in March – the opportunity was taken to announce a new short-dated stock, to be issued on 1st April – £800 million of $9\frac{3}{4}\%$ Treasury Stock 1981 at a price of £95.50 per cent, giving a gross redemption yield of 10.94%. Thus, for the first time for nearly three months, both a long and a short-dated tap stock were available; but there was little demand for them, except during a brief period around the middle of April when the March trade figures were well received. Sterling's continuing weakness was the main reason why the market was depressed, though uncertainties over the next stage of incomes policy also contributed.

On 23rd April, after prolonged pressure on sterling – and prompted by a signal from the Bank in the form of lending to the discount market for seven days at minimum lending rate – the market sharply lowered their bids for Treasury bills, thereby raising minimum lending rate from 9% to $10\frac{1}{2}\%$. Early in May the pressure on sterling eased, and the Government and TUC leaders announced an agreement on incomes policy. The long tap – $12\frac{1}{2}\%$ Treasury Loan 1993 – was heavily sold, and official supplies were exhausted on the 19th. Meanwhile, however, what proved to be a temporary rise in US interest rates had again put the pound under pressure: minimum lending rate rose again on 21st May, to $11\frac{1}{2}\%$, and with the market unsettled it was not judged timely to announce a replacement for the exhausted tap. Yields rose strongly up to the end of May, only to be partly reversed early in June when the \$5.3 billion stand-by credit was arranged.[1] A new long-dated issue, £800 million of $13\frac{1}{4}\%$ Exchequer Loan 1996, was announced immediately, and official sales – particularly of the short tap – were heavy during the remainder of the month.

By July, it was possible to compare the course of monetary developments in the new financial year with the projections made at the

[1] See June 1976 *Quarterly Bulletin* (page 163).

time of the Budget. The growth of total M_3 – just over 10% at an annual rate in the three months to mid-June[1] – was consistent with the indications given in the Chancellor's Budget. But this at least partly reflected the contractionary effect of a large outflow of funds. Domestic expansionary forces appeared to be somewhat stronger than had been expected; moreover, in July there was a particularly sharp increase in bank lending to the private sector, though this was thought to relate essentially to leads and lags in commercial trade,[2] and liable to be reversed when confidence in sterling had been restored. The public sector borrowing requirement also appeared to be larger than expected during this period. On the other hand, sales of public sector debt outside the banking system were much as the authorities had intended. (Within the total, sales of gilt-edged were supplemented by a take-up of Treasury bills by institutions other than banks, particularly in early May. The banks had an ample supply of bills – weekly offerings had for a time amounted to £600 million, a record first reached in May – and were unwilling to bid for funds in the inter-bank and certificate of deposit markets, so that Treasury bills became an attractive asset for other institutions with surplus liquidity.)

The summer and autumn months

One objective of the Chancellor's July measures was accordingly to restore confidence in sterling, chiefly by exerting tighter control over public sector spending. A move was made towards the adoption of a monetary target when the Chancellor stated in quantitative terms his expectation for monetary growth.[3] Monetary measures were confined to a reinforcement of the Governor's guidance to banks and finance houses on the direction of their lending.[4]

Both the central government borrowing requirement and bank lending were projected to be no more than moderate over the months ahead. If the July package were to be successful in restoring confidence, the growth of the money stock in the short term could be expected to be comfortably within the target, with no need of additional measures to stimulate sales of gilt-edged. In the event, the July package did not succeed in restoring the requisite market confidence; the weakness of sterling and slackness of demand for gilt-edged were aggravated by poor trade and money stock figures announced in August and began to interact on each other; and it was becoming clearer that the rate of price inflation was unlikely to go on declining but instead might accelerate again, partly because of sterling's earlier depreciation.

Even though gilt-edged yields were accordingly expected to rise, there was, in fact, no heavy selling by investors. Indeed, on one day around the middle of August, the authorities sold a substantial amount of the long tap (almost exhausting official supplies), with a yield no higher than had prevailed in early June. Otherwise, the gilt-edged market was inactive throughout this period.

It was rather the foreign exchange market that became the focus of attention. By September, sterling was again under heavy downward pressure, intensified by the possibility of a seamen's strike. On the 9th, official support at around \$1.77 seemed to be no longer sustainable, and the exchange rate fell sharply.

The Treasury bill rate rose steeply on the following day, raising minimum lending rate from $11\frac{1}{2}\%$ to 13%; and on 16th September, in a

[1] Later revised to 13%, mainly because more recent information led to changes in the seasonal adjustment.

[2] See September 1976 *Quarterly Bulletin* (page 310).

[3] The phrase in the Chancellor's speech was: 'For the financial year as a whole, the growth of the money supply should amount to about 12%.'

[4] Banks and finance houses were asked to ensure that, through strict restraint on lending and on the provision of facilities for other purposes, sufficient funds would be available for both working capital and fixed investment by manufacturing industry, and for the expansion of exports and import saving.

related move designed to reduce the liquidity of the banking system, the Bank announced a call for special deposits amounting to 1% of eligible liabilities. During this period, gilt-edged yields had risen to above 15% at the long end; and after the announcement of the August money stock figures on 20th September the time was judged ripe to introduce a new long-dated issue – £600 million of 14½% Treasury Loan 1994 at a price of £96.50 per cent, giving a gross redemption yield of 15.07%. The gilt-edged market responded favourably: a surge of buying exhausted official supplies of the short tap, and the new long-dated tap was heavily oversubscribed. Official sales during the week amounted to almost £1,000 million (net), and a new short-dated issue was announced on 24th September – a second tranche of £600 million 11½% Treasury Stock 1979.

The recovery of the gilt-edged market was short-lived. Renewed pressure on sterling developed early in the following week, prompted by a proposal to nationalise some major banks and insurance companies. Gilt-edged prices fell in response, official sales again dried up, and applications for the new short tap were very small. Extremely tight conditions in the domestic money market appeared necessary in order to check sales of sterling, and a further call for special deposits equivalent to 2% of eligible liabilities, and an administered increase of 2% in minimum lending rate to 15%, were therefore made on 7th October.

The response of the gilt-edged market to these moves became an important influence in achieving the desired tightness of money. After an initial sharp fall in prices – which the authorities followed immediately in the price at which they made the 1979 tap stock available to the market – that stock came into heavy demand, as did also two new stocks announced on 8th October – £600 million of 15½% Treasury Loan 1998 at £96 per cent, with a redemption yield of 16.16%, and £400 million of 3% Treasury Stock 1982 at £70 per cent, a low-coupon stock designed to appeal to tax-paying investors, including those paying higher rates of income tax. Pressure on the exchange rate again interrupted sales later in October: yields and interest rates reached a peak near the end of the month, but sales were resumed early in November when confidence began to improve.

Total official sales of around £1½ billion in the month to mid-October encouraged hopes of a much smaller rise in the money stock, after the extremely rapid growth in the previous three months. Such hopes proved unfounded, and M_3 rose by a further 1½% (seasonally adjusted) in the month. Though there were some special factors, bank lending contributed most to this further expansion: lending in sterling to the private sector increased by around £600 million during the month. As earlier in the year, it proved difficult to reconcile this increase with what was known of the course of domestic economic activity, and two related steps were announced on 18th November.

The first was the exchange control measure severely restricting the use of sterling in the finance of third country trade, which was expected to lead to the repatriation, over a period of months, of a substantial amount which had accumulated in the form of sterling claims on non-residents (see footnote on page 6). The move was supported by a modification of the guidance to banks, designed to prevent loans and advances being replaced by sterling acceptance credit facilities.

The second step, aimed at controlling the growth of bank balance sheets, was the reintroduction of the supplementary special deposits scheme, which had been in suspense since February 1975. As before, the scheme allowed a six-month period before any deposits would become payable. During that period, the penalty-free growth of interest-bearing eligible liabilities was set at 3% – not, in fact, more restrictive than in 1973, because of the prospective repatriation of funds associated with the first measure noted above.

The market interpreted these measures as supporting its view that interest rates had passed their peak. The 1979 and 1998 tap stocks had become exhausted on 4th November, and one of their immediate replacements – £600 million of 14% Treasury Stock 1982 – ran out on the 17th. New issues followed each other in quick succession as the market, in contrast to earlier in the year, confidently anticipated reductions in interest rates after a successful conclusion to the Government's negotiations with the International Monetary Fund for a stand-by credit. In spite of the pressure on the money market, stemming from official sales of gilt-edged, competition for Treasury bills from the discount houses and banks grew steadily and, with smaller amounts on offer at the tender, the average rate of discount began to fall. Minimum lending rate was reduced by ¼% after the reintroduction of the supplementary special deposits scheme in November, and the Bank lent frequently to the discount houses at minimum lending rate for seven days in order to restrain further falls in advance of the Chancellor's statement on 15th December, when negotiations with the IMF had been successfully concluded.

The winter months, when confidence returned

In that statement, the Chancellor announced that the Letter of Intent to the IMF included plans to reduce public expenditure in 1977/78 and 1978/79, and to contain the public sector borrowing requirement for those years within limits of £8.7 billion and £8.6 billion respectively. However, the statement was preceded by the announcement of a very large overseas trade deficit for November, and for a while markets were hesitant and subdued. But expectations of declining rates were quickly re-established. Minimum lending rate fell by ¼% in two successive weeks, and heavy official sales of gilt-edged were resumed. A long-dated issue – a second tranche of £750 million 15¼% Treasury Loan 1996 – was announced on 22nd December and offered for subscription on New Year's Eve.

During the fourth quarter as a whole, official sales exceeded £3 billion, making a total of more than £4½ billion in the first three quarters of the financial year. In the Letter of Intent, the monetary target for the year was redefined as a ceiling for domestic credit expansion of £9 billion in the twelve months to mid-April. The Chancellor also stated in December that he expected an increase of 9%–13% during 1976/77 in the sterling component of M_3 to be consistent with such a limit for DCE. This would still have required further sales of gilt-edged, if the public sector borrowing requirement were to turn out to be much as projected in December, and if bank lending were broadly to absorb the resources permitted by the supplementary special deposits scheme. But the urgency was now reduced, and a somewhat larger decline in interest rates and yields could be countenanced by the authorities, although they had to judge how far such a fall should go in the light of continuing uncertainties over inflation and the prospective size of public sector borrowing in the next financial year.

There were in fact heavy sales of gilt-edged in the first half of January – encouraged by the arrangement of the facility related to official sterling holdings – and a short-dated issue made on 13th January (£600 million of 12¾% Exchequer Stock 1981) was oversubscribed. No more short-dated stocks were issued until April. The long tap, issued on New Year's Eve, had run out just a week later, and on 14th January a successor was announced – 13¾% Treasury Loan 1993, priced at £96 per cent to yield 14.38% to redemption, more than one percentage point less than the issue yield of the 1996 stock which it replaced. The amount offered (£1,250 million) was unprecedentedly large and was intended to moderate the market's immediate appetite for gilt-edged. It did not succeed in this respect, being sold out within a week of issue. But even though a successor was not announced, yields at the longer end were little changed by early March.

As the quarter advanced, however, it became increasingly clear that domestic credit expansion in the year to mid-April was likely to fall well short of the ceiling set in December. The central government borrowing requirement for 1976/77 (and, by inference, that of the public sector as a whole) was proving much smaller than had been forecast in December. At the same time, as also became increasingly clear, bank lending in sterling had fallen away sharply – no doubt largely reflecting the unwinding of leads and lags, and the November measures relating to the finance of third country trade (see above). In the circumstances, further receipts from sales of gilt-edged would clearly have been redundant, and no more issues of the conventional type were made after the end of January.

Meanwhile, minimum lending rate, which had fallen by $\frac{1}{4}\%$ after the first Treasury bill tender in the New Year, declined by $\frac{3}{4}\%$ and 1% in successive weeks in the second half of January, to $12\frac{1}{4}\%$. These falls occurred over a period when the money market was exceptionally short of funds because of the sales of gilt-edged, reinforced by heavy tax payments. The shortages were relieved partly by the release of special deposits: a release equivalent to 2% of eligible liabilities was announced early in January, and payment of the second half of the call announced in October (which had already been twice postponed) was cancelled. Subsequently, a temporary release of 1% was announced, to be redeposited on 10th March when $6\frac{1}{4}\%$ Treasury Stock 1977 was due to mature. As well as buying Treasury, local authority and commercial bills, the Bank also gave some help by placing funds in the local authority deposit market and, from time to time, by buying bills from the discount market for resale at fixed dates. Very heavy assistance was also given by lending to the market, much of it overnight, but frequently at minimum lending rate for seven days, as an indication of the Bank's view that the fall in rates was proceeding too rapidly.

To prevent a further possible sharp decline in interest rates stemming from strong competition for Treasury bills from outside the discount market, the Bank announced a reduction in minimum lending rate to 12% on 3rd February. It was made clear, at the same time, that the rate would remain at 12% until the Treasury bill tender rate moved into the range which would result in a minimum lending rate of 12% under the usual formula, or until the Bank administered a further change. As expected, the tender rate fell more sharply, by $\frac{1}{2}\%$, thus moving too far to reinstate the formula. Minimum lending rate accordingly remained at 12%, even though the tender rate had fallen by a further $\frac{1}{2}\%$ by the end of the month. On 10th March, however, the Bank again administered a reduction in minimum lending rate, this time to 11%; and when the tender rate came into line on the next day, the Bank announced that in future they reserved the right in exceptional circumstances not to follow the usual formula in whole or in part if that would result in an undesirable reduction in minimum lending rate. This right was exercised during the following week, when minimum lending rate was reduced by only $\frac{1}{2}\%$ to $10\frac{1}{2}\%$, even though the tender rate fell by 1%. Minimum lending rate remained at $10\frac{1}{2}\%$, with the formula suspended, until 31st March, when the Bank made an administered reduction of 1% to $9\frac{1}{2}\%$. On the following day, the tender rate came into line, and the formula accordingly became operative again.

As already indicated, it had become apparent by January that it would not be desirable to raise cash within the current financial year by further sales of gilt-edged. But while market conditions remained receptive, there were good grounds for starting the finance of the following year's borrowing requirement by sales of debt for which payment would largely fall in that year. Accordingly, on 18th March, a new long-dated issue was announced – £800 million of $12\frac{1}{4}\%$ Exchequer Stock 1992, to be issued at £96 per cent with a redemption yield of 12.85%. One of its unusual features was that only £15 per cent was payable on application on 24th March; the balance was to be paid in two instalments – £40 on 25th April and £41 on 13th June. The issue was oversubscribed.

Transactions in gilt-edged stocks during the year to 31st March 1977

Official transactions in gilt-edged stocks are analysed in the following table by type of holder and by maturity.

£ millions

Net purchases by the public +/sales –

	Financial year 1 April – 31 March				
	1976			1977	1976–77
	2nd qtr	3rd qtr	4th qtr	1st qtr	Year
By type of holder[a]					
Overseas holders	+ 1	+ 34	+ 106	+ 202	+ 343
UK banking sector	+ 29	– 41	+ 398	– 201	+ 185
Other UK holders	+ 829	+ 599	+ 2,676	+ 1,658	+ 5,762
Total	+ 859	+ 592	+ 3,180	+ 1,659	+ 6,290
By maturity					
Redemptions	– 4	– 261	– 191	– 247	– 703
Up to 1 year	– 268	– 358	– 240	– 536	– 1,402
Over 1 and up to 5 years	+ 385	+ 247	+ 1,293	+ 675	+ 2,600
Over 5 and up to 15 years	+ 28	+ 34	+ 737	+ 18	+ 817
Over 15 years and undated	+ 718	+ 930	+ 1,581	+ 1,749	+ 4,978
Total	+ 859	+ 592	+ 3,180	+ 1,659	+ 6,290

[a] Further details may be found in the statistical annex to the *Quarterly Bulletin*. Changes in the holdings of the UK banking sector are shown mainly at book value, other changes at cash value. Any differences between book and cash values in the banking sector are reflected in the residual figures for 'other UK holders'. Overseas holdings are partly estimated, and any errors are again reflected in the residual item. The banking sector here excludes the Banking Department of the Bank of England.

Part 2 Other responsibilities and activities

Support operations

The special committee of the Bank and the London and Scottish clearing banks, set up in December 1973 under the chairmanship of the Deputy Governor, met regularly throughout the year. The number of active companies receiving support through the Committee again declined.

In the accounts of the Banking Department (see page 29), further provision has been made against possible losses from the Bank's share in these support operations and in other operations which the Bank have undertaken outside the special committee.

The Burmah Oil Company Limited

Financial support for The Burmah Oil Company continued throughout the year. Following the sale by Burmah of its main North American assets and the subsequent repayment of dollar borrowings guaranteed by the Bank, new arrangements were concluded in November under which the Bank agreed to guarantee further dollar borrowings of $100 million and to provide sterling stand-by facilities covering the period up to June 1982.

In October 1976, Burmah served a writ on the Bank claiming, *inter alia*, the restitution of the 77,817,507 British Petroleum ordinary stock units purchased from Burmah in January 1975. A defence has been entered to this claim.

Banking supervision

During the year, further discussions were held with the London and Scottish clearing banks and with British banks whose main activities are overseas, as part of the process of extending the Bank's supervisory arrangements. These discussions will continue to take place annually. Supervision of other institutions is generally based on the examination of quarterly returns, followed up by discussions with senior management of the institutions concerned.

In August 1976 the Government published a White Paper (Cmnd. 6584) entitled *The Licensing and Supervision of Deposit-Taking Institutions*, which proposed that the Bank's supervisory role be extended to include all deposit-taking institutions not already supervised in other ways. Any institution other than a recognised bank would need a licence from the Bank in order to carry on the business of taking deposits from the public. The Government plans to introduce legislation giving effect to these proposals as soon as possible; consultations with the banking sector, as envisaged in the White Paper, have been taking place.

Regulation of the securities market

Following an inquiry by the Department of Trade in 1974 and subsequent discussions with the Bank, the Secretary of State for Trade announced in October 1976 that it was proposed to introduce a series of measures designed to improve the supervision and regulation of the securities market. These provided, among other things, for a joint review body to be established by the Department of Trade and the Bank to monitor developments in the securities market and to identify deficiencies in the regulatory machinery; the Bank were also to develop their surveillance of the securities industry so that the existing self-regulatory machinery might become more effective.

The joint review body met for the first time in February 1977.

Sterling Brokers' Association

The Governor of the Bank and the Chairman of the Committee of London Clearing Bankers accepted the recommendation of a working party – chaired by the Bank and consisting of members nominated by principals and brokers in the sterling inter-bank and certificate of deposit markets – that an Association of Sterling Brokers should be established. A joint standing committee, comprising representatives of the brokers and of the British Bankers' Association, under the Bank's chairmanship, has begun work on establishing the constitution and rules of the Association, in consultation with other interested parties.

The note issue

The fiduciary issue was £6,775 million at the end of February 1977, £725 million (12%) larger than a year earlier. As in previous years, the issue reached a peak (of £7,375 million) during the Christmas period.

Value of notes in circulation by denominations

£ millions; end-February

	1973	1974	1975	1976	1977
10*s*[a]	13	13	13	13	13
£1	908	906	884	831	805
£5	2,400	2,513	3,014	3,261	3,431
£10	487	644	815	1,157	1,596
£20	224	324	397	500	652
Other notes[b]	155	173	232	280	261
Total	4,187	4,573	5,355	6,042	6,758

[a] The 10*s* note ceased to be legal tender in November 1970; but notes still in the hands of the public can be cashed at the Bank.

[b] The issue of denominations higher than £20 was discontinued in 1943, but such notes are still used internally in the Bank, e.g. on behalf of banks of issue in Scotland and Northern Ireland as cover for their note issues in excess of their permitted fiduciary issues.

At the end of February this year, £10 and £20 notes together accounted for 33% of the value of the circulation, compared with 27% a year earlier. The proportion represented by £5 notes declined for the second successive year, from 54% to 51%, while the share of £1 notes fell to a new low of 12% – less than half as large as five years earlier.

As a result of the growing use of higher denomination notes, together with an active campaign to promote the recirculation of clean used notes, the number of new notes required for issue has increased only slowly over the last two years, despite the sharp rise in the value of the note circulation.

Number of new notes issued by denominations

Millions; year to end-February

	1973	1974	1975	1976	1977
£1	1,004	981	1,092	1,021	985
£5	340	382	446	482	553
£10	32	42	55	111	107
£20	6	8	8	11	16
Total	1,382	1,413	1,601	1,625	1,661

Management of stock registers

The nominal value of stocks managed by the Bank increased by nearly 20% for the second consecutive year: new issues amounted to over £9,000 million and redemptions to nearly £2,500 million.

The number of accounts in British government stocks rose by some 165,000 to more than two million.

	Nominal value of stocks in issue (£ millions)				Number of accounts (thousands)			
End-February	**1974**	**1975**	**1976**	**1977**	**1974**	**1975**	**1976**	**1977**
British government securities:								
Stock[a]	25,221	27,769	33,491	40,436	1,766	1,859	1,878	2,044
Bearer bonds	29	35	40	50	[b]	[b]	[b]	[b]
	25,250	27,804	33,531	40,486				
Other securities:								
Government-guaranteed	908	908	908	908	113	114	116	117
Common-wealth etc.	167	164	161	154	51	49	47	43
Local authorities	687	663	753	812	160	145	145	136
Companies[c]	222	331	339	407	37	39	41	41
Miscel-laneous[d]	55	53	51	50	9	8	7	7
	2,039	2,119	2,212	2,331	370	355	356	344
Total	**27,289**	**29,923**	**35,743**	**42,817**	**2,136**	**2,214**	**2,234**	**2,388**

[a] The figures for British government stock do not include amounts on the registers of the Bank of Ireland, the Department for National Savings, and the trustee savings banks.

[b] The number of separate bonds in these years was 1974: 43,000; 1975: 45,000; 1976: 47,000; 1977: 56,000.

[c] Comprising stocks of the Agricultural Mortgage Corporation Limited and, from 1975, Finance for Industry Limited.

[d] Includes securities issued by public boards.

Transfers

Turnover was heavy in the gilt-edged market, especially in the latter part of the year, and the number of transfers registered exceeded one million for the first time. Figures for the last four years are:

Thousands

Year to end-February	**1974**	**1975**	**1976**	**1977**
	668	768	873	1,025

Repayments and issues

The main repayments and issues undertaken during the year are listed below:

£ millions nominal

Repayments at par

1976	1 March	6½% Exchequer Stock 1976	600.0
	15 March	New Zealand Government 6% Stock 1975/76	7.0
	15 May	Metropolitan Water (F) Stock 1971/76	0.8
	21 May	Liverpool Corporation 5½% Redeemable Stock 1974/76	6.0
	11 August	Greater London 6¾% Stock 1976	50.0
	15 August	6½% Treasury Stock 1976	894.6
	14 December	10½% Treasury Stock 1976	897.3
1977	15 February	Greater London 6½% Stock 1977	20.0

£ millions nominal

Issues for cash

1976	4 March	@ £96.50	Greater London 12½% Stock 1983	100.0
	1 April	@ £95.50	9¾% Treasury Stock 1981	800.0
	11 June	@ £94.00	13¼% Exchequer Loan 1996	800.0
	24 September	@ £96.50	14½% Treasury Loan 1994	600.0
	30 September	@ £98.75	11½% Treasury Stock 1979 (second tranche)	600.0
	14 October	@ £96.00	15½% Treasury Loan 1998	600.0
	14 October	@ £70.00	3% Treasury Stock 1982	400.0
	11 November	@ £98.25	14% Treasury Stock 1982	600.0
	11 November	@ £97.50	15¼% Treasury Loan 1996	600.0
	25 November	@ £96.25	13% Exchequer Stock 1980	800.0
	10 December	@ £99.00	15½% Treasury Loan 1998 (second tranche)	500.0
	31 December	@ £99.00	15¼% Treasury Loan 1996 (second tranche)	750.0
1977	13 January	@ £96.25	12¾% Exchequer Stock 1981	600.0
	20 January	@ £96.00	13¾% Treasury Loan 1993	1,250.0
	11 February	@ £99.50	Finance for Industry Limited 14% Unsecured Loan Stock 1983	50.0
	24 February	@ £98.50	Corporation of London 13¼% Stock 1983	25.0

In addition to the above, twenty-four issues of short-term bonds (with a value of £32 million) were redeemed during the year, and there were thirty-six new issues (with a total value of £52.5 million). Also, 4% Victory Bonds – which were subject to redemption by annual drawings – were extinguished by a final drawing of £0.3 million (nominal), for redemption at par on 1st September 1976.

Southern Rhodesia stocks

No funds have been received since November 1965 to service Government of Southern Rhodesia stocks for which the Bank act as paying agents. At the end of February 1977 the approximate amounts due but unpaid were:

Gross interest	£22,554,000
Redemption moneys[1]	£33,914,000

At the same date, contributions due but unpaid to sinking funds managed by the Bank totalled some £3,669,000.[2]

Tax reserve certificates

Tax reserve certificates have not been available for purchase for several years. During the year ended February 1977, the number of certificates outstanding fell from some 19,000 to 10,000, with a nominal value of about £5 million.

Local authority markets

In the period under review, the Bank arranged eight issues of 91-day bills for the Greater London Council and four issues for the City of Liverpool. The total nominal value of local authority bills outstanding rose from £421 million to £441 million.

[1] Relating to Government of Southern Rhodesia 3½% Stock 1961/66, 3½% Stock 1967/69, 2½% Stock 1965/70, 3% Stock 1971/73 and 4% Stock 1972/74. The registers for these stocks remain open.

[2] Including some £240,000 in respect of Government of Southern Rhodesia 3½% Stock 1967/69 and some £417,000 in respect of Government of Southern Rhodesia 4% Stock 1972/74. The sinking funds for 3½% Stock 1961/66, 2½% Stock 1965/70 and 3% Stock 1971/73 are not managed by the Bank.

Foreign currency borrowing by the public sector

Arrangement of a $1.5 billion loan for the Government

In January 1977 the Bank arranged for a group of UK, West German and North American banks to raise a medium-term loan of $1½ billion on behalf of the Government. A first tranche of $1 billion had been drawn by the end of March 1977; the balance is due to be drawn after an interval of six months.

Borrowing under the exchange cover scheme

Foreign currency borrowing by nationalised industries under the exchange cover scheme was particularly heavy during the period. A total of $2.3 billion was raised through market operations and private placements, and $0.6 billion was borrowed from the European Investment Bank and European Coal and Steel Community. At the end of February 1977, total borrowing outstanding under the scheme amounted to $9.6 billion.

Among particular developments, there were three medium-term syndicated bank credits amounting in total to $1 billion: the Post Office borrowed $200 million in this way, the National Water Council $300 million, and the Electricity Council $500 million. A further $175 million was raised by public issues in the euro-dollar bond market – $50 million by the Electricity Council in March, $50 million by the National Coal Board in July, and $75 million by the South of Scotland Electricity Board in November.

Foreign exchange and gold

The Bank's dealing room was extensively remodelled during the year, and their links with the foreign exchange market were accordingly strengthened. Representatives of the banks and brokers met regularly in a joint standing committee, chaired by the Bank, to discuss matters of common interest, including possible improvements in the market mechanism in order to maintain the attraction of London as a major foreign exchange market.

Production of sovereigns dated 1976 began during the year at the Royal Mint in Llantrisant. Demand was weaker than in the previous year and the premium declined accordingly.

City liaison

As well as maintaining close contacts with other City institutions, the Bank again provided secretarial facilities to the Committee on Invisible Exports and to the various specialist City committees established by the Governor several years ago. These committees continued effectively to co-ordinate City opinion and to express an independent City view on many topics.

The City Liaison Committee continued to meet, under the chairmanship of the Governor, to review matters of common concern.

The formation of a new autonomous body – the City Communications Organisation – was announced in March 1976, under the sponsorship of a wide range of city associations, to co-ordinate the provision of information both within the City and for the public.

Among its other activities during the year in following developments in the EEC affecting the financial community, the City EEC Committee submitted a paper to the European Commission, which summarised reactions from the UK private sector to a proposed EEC code of conduct covering transactions in transferable securities.

Among the specialist committees, the Capital Markets Committee considered a wide range of subjects, including the impact on investors and capital markets of proposals for inflation accounting, employee participation and nationalisation, and the provision of finance for industry.

In June the Company Law Committee published its comments on the discussion paper, *The Corporate Report*, prepared by the Accounting Standards Committee; and in August it published a further study on insider dealing, which received wide circulation and was submitted to the Department of Trade. Following the report of the Committee of Inquiry into Industrial Democracy early in 1977, the Committee has again been actively considering the question of employee participation (on which it published its first report in 1975).

The Taxation Committee remained in close touch with the Inland Revenue and made a number of representations on Finance Bills and other tax matters.

The Telecommunications Committee continued its work with the Post Office and with users of Post Office services in the City.

The Bank and industry

The Bank continued to develop their close contacts with industrialists throughout the United Kingdom, with particular reference to the financial needs of industry. To this end, the Industrial Finance Unit makes special studies of individual sectors of industry, and one such inquiry led the Bank to invite Mr J. P. Koppel, formerly Deputy Chairman of Courtaulds Limited, to examine the structure and financial resources of the clothing industry. These inquiries also provide a useful background for considering the problems of individual companies.

The Bank's concern for the provision of finance for industry is reflected in their membership of the Committee on Finance for Investment, set up by the National Economic Development Council, and in their support for Equity Capital for Industry Limited, which is now fully operational.

Finance for Industry Limited

In February 1977, Finance for Industry (in which the Bank are shareholders) made an issue of £50 million loan stock. By the end of March 1977 the FFI group had lent or committed some £450 million since its formation in 1973.

Exchange control

As mentioned in last year's *Report*, measures were taken in April 1976 to reduce the extent to which authorised banks are required to refer applications to the Bank, and minor changes were made to simplify administration and to reduce costs.

In August 1976, the rules governing the provision of sterling finance by banks in the United Kingdom to the overseas sterling area were tightened; and in November these facilities were further restricted to the finance of trade with the Scheduled Territories (see footnote 2 on page 6).[1] Also with effect from November, merchanting by UK residents in goods traded between non-Scheduled Territories had to be conducted in foreign currency rather than in sterling, except for commodities covered by special exchange control schemes. Subsequently, the maximum period of sterling trade credit which participants in commodity schemes could offer to non-residents was reduced from six months to a term broadly in accordance with normal practice; and in March 1977 sterling finance by UK banks for trade in commodities covered by exchange control schemes was brought into line.

Authorised depositaries were reminded in April 1976 of their responsibilities under the Exchange Control Act 1947, in particular

[1] The Scheduled Territories at present comprise the United Kingdom, the Channel Islands, the Isle of Man, the Republic of Ireland, and Gibraltar.

when satisfying themselves that foreign currency securities or holdings of foreign currency qualify for the 'investment currency premium'. A review of the authorised depositary system was undertaken with the Treasury during the year, and in December 1976 arrangements were announced whereby transactions in foreign currency securities and investment currency were to be monitored more closely by the Bank.

It was also announced in December that the Bank were prepared to sell manuals containing exchange control notices to the general public, together with an up-dating service; and in February 1977 a revised version of *A Guide to United Kingdom Exchange Control* was issued (free of charge to the public), incorporating changes in policy and practice since the previous issue in July 1973.

Commodity markets

The Bank continued to maintain close contact with the markets. During the first half of 1976, the Bank became concerned about an increase in non-trade dealing in the zinc market; and in May the Committee of the London Metal Exchange advised ring-dealing members not to accept new business of this nature. The restriction was lifted in July, when a more appropriate balance had been restored between trade and non-trade activities.

Certain changes in the period of trade credit which participants in commodity schemes could offer to non-resident customers are mentioned in the preceding section.

An article in the March 1977 *Quarterly Bulletin* (page 34) gave the results of a survey of the contribution made by the commodity markets to the United Kingdom's invisible earnings.

External affairs

Other sections of the *Report* have mentioned the important external developments in the year under review. The Bank continued to be closely engaged in discussions on international economic and financial developments, both in the International Monetary Fund and elsewhere. They again provided an alternate director of the IMF for the United Kingdom, and another member of staff was seconded to the UK Treasury and Supply Delegation as a technical assistant. The Bank also continued to be represented on the Economic Policy Committee of the Organisation for Economic Co-operation and Development, and on that Committee's Working Party No. 3.

During the year, the Bank took part in the negotiations with the IMF for a stand-by credit; they also negotiated a short-term swap facility with overseas central banks and a facility related to official sterling balances, as well as the arrangements for a medium-term loan mentioned on page 17.

In April 1976, the Governor assumed the chairmanship of the EEC Committee of Central Bank Governors and of the Board of Governors of the European Monetary Co-operation Fund. The Bank were also represented on the Monetary Committee, the Economic Policy Committee and a number of specialist groups working either to those committees or to the Commission, as well as on the Council working group dealing with harmonisation of banking legislation. As in the past, the Bank provided an alternate director of the European Investment Bank, and a member of staff continued to be seconded to the Office of the UK Permanent Representative to the European Communities in Brussels. Mr S. W. Payton, Chief of the Overseas Department, was appointed co-chairman of the Finance Commission of the Conference for International Economic Co-operation for the period of the United Kingdom's presidency of the European Economic Community. The committee on banking and foreign exchange regulation and supervision, which was established in February 1975 by the Governors of the Group of Ten countries and Switzerland, continued its work under the chairmanship of Mr George Blunden.

The Bank received some 1,800 visitors during the year, mainly from other central and commercial banks, and 22 members of the staff were working abroad in various capacities at 28th February 1977.

Economic and statistical information and research

An article in the December 1976 *Quarterly Bulletin* (page 436) described in detail the work of the Economic Intelligence Department, which was reorganised in May 1976. The Bank participated with several other central banks[1] in a special survey, conducted by the BIS, of lending by commercial banks. The survey, relating to end-December 1976, gave information about the maturity structure of bank lending to individual countries outside the reporting area, and about unused facilities; it also covered lending through branches in off-shore centres, as well as from the reporting area itself. Among other statistical developments, a survey was carried out into the invisible earnings of UK commodity markets (see page 19). Research work by the Economics Division included a further study of corporate finance: the results were published in an article, 'The cost of capital, finance and investment', in the June 1976 *Quarterly Bulletin* (page 193).

Select Committee on Nationalised Industries

The report of the sub-committee of the Select Committee on Nationalised Industries on its inquiry into the affairs of the Bank was published in December 1976.

The Wilson Committee

A committee to review the functioning of financial institutions was set up in January 1977 under the chairmanship of Sir Harold Wilson. Its terms of reference are to inquire into the role and functioning, at home and abroad, of financial institutions in the United Kingdom and their value to the economy; to review in particular the provision of funds for industry and trade; to consider what changes are required in the existing arrangements for the supervision of these institutions, including the possible extension of the public sector; and to make recommendations. The Bank was invited to provide their overall view of the arrangements in the United Kingdom for channelling savings into industry and trade, and of the monetary environment in which these arrangements operate. A member of the Bank's staff has been appointed to the committee's statistics panel.

History of the Bank of England, 1891–1944

In the *Annual Report* of 1968 it was announced that Professor R. S. Sayers had been asked to write a history of the Bank during the first half of this century, in continuation of Sir John Clapham's work published in 1944. The book has now been completed under the title *The Bank of England, 1891–1944* and was published in three volumes by the Cambridge University Press in September 1976.

Staff and administration matters

Following the Government's call for cuts in public spending, the Bank reduced their current expenditure in real terms during the year; this was reflected in the charges for services to Government. Further reductions in real terms are planned over the next three years.

[1] In the Group of Ten countries, Ireland, Denmark and Switzerland.

The Government's programme of cash limits on public spending in 1976/77 included the costs of administering exchange control. During the present financial year, an overall cash limit applies to four areas in which the Bank provide services to Government – the note issue, management of the national debt, management of the Exchange Equalisation Account, and administration of exchange control.

Numbers of staff

The weekly average number of staff employed during the year was nearly 7,900, slightly lower than in the previous year. Their aggregate annual remuneration amounted to £32,862,000.

At 28th February 1977 the Bank employed nearly 6,800 full-time and rather more than 900 part-time staff, distributed broadly as follows:

Banking staff		
Cashier's Department (including 350 at Branches)	1,175	
Accountant's Department	1,075	
Exchange Control Department	750	
Economic Intelligence Department	250	
Overseas Department	250	
Printing Works (banking staff)	225	
Administration Department	425	
Establishment Department	350	
Unallocated (including seconded staff and trainees)	75	4,575
Technical and services staff		1,050
Printing Works staff		1,625
		7,250[a]

[a] Including 450 in respect of the 900 part-time staff who work either alternate weeks or half-days each week. Such staff were excluded from last year's figures, but this is allowed for in calculating the change over the year.

The banking staff was reduced by about 225 during the year and the Printing Works staff by about 50. These reductions formed part of the Bank's response to the Government's request for expenditure cuts noted above.

Staff wastage and recruitment

In order to achieve the necessary reductions during a period of exceptionally low natural wastage – turnover of junior staff was only about one third of the normal rate – a selective offer of early retirement on special terms was made to clerical staff within ten years of normal retirement age. Applications were accepted from more than 100 members of staff.

Apart from a few specialist appointments, only 16 graduates and a similar number of entrants with 'A' levels were recruited during the year, compared with averages of around 30 and 80 in earlier years. The London intake of entrants with 'O' levels for junior clerical work, at 46, was unusually small for the second successive year: in earlier years the average annual intake was around 250.

Secondments

As in previous years, the Bank responded to requests to provide staff on secondment at home and abroad. At the end of the year, five members of staff were working in government departments (two at the Cabinet Office, two at the Treasury and one at the Department of Industry); and nine were attached to various City and commercial organisations.

Staff representation

Around the turn of the year, the staff associations representing weekly-paid technical and services staff gave notice of their dissolution and, with more than 50% of such staff having by then become members, the Bank of England Staff Organisation requested, and obtained, recognition by the Bank as sole bargaining agent. (The Organisation was already recognised as the sole bargaining agent for the banking staff, other than the most senior.)

Developments in the use of computers

A new sub-system was installed in the Cashier's Department, enabling more routine banking operations to be conducted 'on-line'. The sub-systems which process statistical work for the Economic Intelligence Department were further developed, and the Time Series system is being used to exchange information with the Organisation for Economic Co-operation and Development and the Bank for International Settlements. Since the end of the Bank's year, the first phase of a staff information system has been inaugurated.