THE RT HON DR DAVID OWEN MP

HOUSE OF COMMONS
LONDON SWIA OAA

CH/EXCHEQUER	
REC.	23 OCT 1984
ACTION	Mr Lankester
COPIES TO	EST
	Sir P. Middleton
	Mr Cassell, Mr Hall
	Mr Flett

Mr Ridley, Mr Lord, Mr Portillo.

23 October 1984

The Rt Hon Nigel Lawson MP
Chancellor of the Exchequer
Treasury Chambers
Parliament Street
LONDON
SW1P 3AG

ANNEX !

Dear Nigel.

There are a number of unanswered questions about the Bank of England's decision 3 weeks ago to rescue from collapse Johnson Matthey Bankers (JMB) Ltd, a subsidiary of Johnson Matthey PLC. I recognise that the City of London needs the back-up system which the Bank of England provides, although in this case it is not clear if the Bank was aware that at least some City institutions did not believe that the gold bullion market, of which JMB Ltd is a member, was ever in danger. Nevertheless, a number of questions remain about the propriety of the Bank of England's behaviour and it is in the public interest that a full account of the Bank's role in the rescue of JMB Ltd be made by you as the person ultimately responsible for the Bank's conduct as soon as possible. I imagine you were consulted about the £10 million put up by the Bank as part of the overall deal.

The first question is why the Bank, after negotiating successfully a stand-by credit of loans and guarantees to protect depositors and preserve money market confidence in the short term, did not then proceed to wind down JMB Ltd and ensure a smooth transition to the liquidation of a failed company. Why was it necessary for the Bank itself to take-over JMB Ltd and all its subsidiaries? Such treatment has not been accorded to a number of other and much larger industrial and commercial companies which have also collapsed in recent years.

If one accepts that some of the problems incurred by JMB Ltd were because there was not sufficient money to be earned in the bullion business - owing to shrinking volumes and an excess of new competitors and if the normal economic consequence of a reduced market is a falling number of companies in which some will go out of business, why was it right in this case to leave an uneconomic business in operation and subvert the usual market forces? All this has done is to create an artificial and now commercially supported JMB Ltd which the Bank seems to believe it can force the bullion market to accept as a 'new' member.

The most critical question, however, concerns the prospect of public money being called on in future. The scale of the losses at JMB Ltd is still uncertain, but most reliable estimates suggest a likely figure of £150 - £250 million. Although there is already some £170 million available to meet losses, the Bank itself is contributing £10 million to a £100 million safety net of guarantees being provided by a number of City banks, which can be called on as further losses are discovered. Furthermore, it is my understanding that these banks, in the initial deal with the Bank of England, agreed only to underpin any further shortfall in the JMB Ltd commercial loanbook, but have now been requested to guarantee a set of continuing businesses which have a high degree of exposure to potentially sizeable trading losses in future. Does the Bank believe that it can sell the commercial loanbook of JMB Ltd which it surely has an obligation to the indemnitors to first work off?

The Bank of England press notice for 12 October 1984 outlined the Bank's intentions towards JMB Ltd and its 14 subsidiaries very clearly: ie "... that the various businesses of Johnson Matthey Bankers Ltd should be continued and their strength developed to the point at which there can be a sale on a going concern basis into appropriate private sector hands." My impression is that the Bank does not have much grasp of the credit issues involved in these businesses and the evidence suggests that the prospects of future profitability for most of them are slim indeed. For instance, the ability to be a bullion dealer in current market conditions has a low value owing to the fact that the bullion business is at present depressed and for other participants very unprofitable. Is it the Bank's intention to stand behind all of the JMB Ltd subsidiaries in future, thereby exposing both indemnitor and taxpayer to the likely prospect of further trading and credit losses? And on whose authority has the Bank agreed to guarantee such losses should they occur?

Finally, there are a set of questions concerning the role of the parent company, Johnson Matthey (JM) PLC. Did JM PLC give a guarantee of its subsidiary, JMB Ltd, and if so was that guarantee ever called by the Bank? Is one to assume that the £50 million injection by the parent company into JMB Ltd effectively bought off this liability of JM PLC's shareholders? The central question here is whether the "full and final discharge" of its liabilities, as given JM PLC by the Bank, was excessively broad and provided the parent company with unjustified relief - for example from the employment of JMB Ltd's staff, the pension fund of JMB Ltd, or certain tax obligations of JMB Ltd assured or guaranteed by JM PLC?

Although not directly comparable, the total cost to the Bank, and so indirectly to public funds (because its dividends to the Treasury were damaged) of the secondary banking crisis 10 years ago, was about £100 million. The danger is that the Bank's decision to try and 'turn around' the various businesses of JMB Ltd, operating in the difficult, risky, and at present depressed markets of commodities and precious metals, will inflict in the longer term a similar and potentially even larger toll on both the Exchequer and the taxpayer.

The risk of public money being called on in this way is wholly unacceptable because it reflects a Bank of England policy decision which ignores the commercial and market realities confronting JMB Ltd.

I look forward to receiving your answers to the above questions.

DAVID OWEN