

SECRET

MR. McMAHON

FOREIGN EXCHANGE AND GOLD MARKETS

Thursday, 10th May 1979

Sentiment for sterling soured this morning as news of the accelerated pay award to the police and the armed services followed further consideration of yesterday's banking figures. There was further speculation, too, on sterling's possible entry into the EMS exchange rate system and the lower rate which, it is assumed, this would entail. With this in mind, market operators were more than usually ready to test the Central Bank's resolve and heavy selling of pounds was seen this morning. Sterling's ERI fell from 66.7 to 66.4 (after 66.3 at noon).

The pound closed at 2.0620 in New York yesterday, opened at 2.0630 this morning and touched 2.0635 on the opening exchanges in response to some professional demand in the Far East. Sentiment turned very quickly, however, and widespread selling soon engulfed the pound, driving it down to 2.0510 before calmer waters were reached. An uneasy lull ensued but in mid-morning the marauders returned and, in another swift and savage onslaught, pushed sterling to 2.0493. This afternoon was quieter. The pound traded around 2.0525, despite a stronger dollar, then fell to 2.0511 after the disappointing CGBR out-turn, only to recover to 2.0555 when Iran announced a substantial rise in oil prices from next week. The close came at 2.0533 but Americans resumed selling later and sterling again dipped below 2.05. Forward margins widened in sympathy with the weaker pound. The cost of three months' forward cover was  $1\frac{3}{8}\%$  p.a. and the covered differential against London rose to  $7/16\%$  despite firmer inter-bank sterling deposits.

Sterling lost  $\frac{1}{8}\%$  to the Swiss franc ( $3.52\frac{1}{2}\%$ ) and  $\frac{3}{8}\%$  to both the French franc ( $9.00\frac{1}{2}\%$ ) and deutschemark ( $3.89\frac{1}{2}\%$ ). The yen improved to 211.65 in Tokyo this morning before closing unsupported at 213.00. Later, however, it succumbed to Swiss selling, following a view that it was currently at the high end of its trading range, and closed at 214.52. This provoked a generally firmer dollar and the deutschemark weakened to 1.8987, the Swiss franc to 1.7185 and the French franc to 4.3840. The Swiss bought a net \$6 mn. and swapped in \$150 mn. The snake remained around 2% in width, bracketed still by the Belgian franc (30.41) and Danish krone (5.3492). The lira, however, at 847.55 advanced to  $4\frac{3}{8}\%$  above the franc which accordingly moved out to 85 on the divergence indicator. The Italians took in \$46 mn. The Dutch sold \$15 mn. and \$2 mn. of marks as the guilder eased rather more than most to 2.0676. The punt weakened to 1.9952 but its discount on sterling was reduced to below 3%.

Gold again stormed the heights following a further strong rally in New York yesterday. Fixings were \$251.70 and \$252.25.

Operations:	Market	- \$113 mn.
	N.Ireland Electricity	
	(PSB G'teed)	+ 55
	Ireland	+ 31
	India	+ 6
	BIS (net)	- 10
	Sundries	+ 14
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		- \$17 mn.

*Jm*  
10th May 1979.

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