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FOREIGN EXCHANGE AND GOLD MARKETS

Week ending 4th July 1979

Higher oil prices, talk of a major new discovery in the North Sea, the Chancellor's support for a strong pound to counter inflation, and a rush to buy while high interest rates last, brought persistent and sometimes heavy demand for sterling which drove the effective index up 1.9 to 70.9 after 71.1, the strongest since early March 1976. The dollar weakened again. Although off the bottom, the Belgian franc remained uncomfortable in the snake despite another rise in interest rates.

The outcome of the OPEC meeting brought keen demand for pounds in New York on Wednesday night, where the rate advanced a cent from the London close of 2.1560. Some selling orders took the rate back near to 2.16 on Thursday, but thereafter it rose almost without interruption as sterling attracted keen interest. News of exhausted tap stocks may have helped, and the Chancellor's support for a strong pound for the sake of curbing inflation and reports of a significant oil find in the North Sea helped carry the rate as high as 2.2335 on Wednesday afternoon, the highest since June 1975, until it receded to close at 2.2235. Buying came from all quarters, and readily absorbed any profit-taking and commercial sales. Undoubtedly oil prices and supplies are the main reason, but high interest rates (which are widely expected to fall soon), make sterling an attractive home for funds. Bad news is quickly shrugged off. Sterling gained considerably on the main continental currencies, touching 4.10 against the mark (after quite a time in which the rate had hesitated to advance far beyond 4.00) before closing 2 1/2% stronger at 4.07 7/8; against the French franc it closed 2 3/4% higher at 9.48 1/8. A fall in the cost of forward cover to 3 1/16% helped turn a small covered discount into a premium of 1/16%.

The dollar fell in most other centres, despite support totalling $1,270 mn. On balance the outcome of the OPEC meeting was unsettling, although the higher price and a halving of the period for which Saudi Arabia allows credit create a one-shot increase in demand for dollars. The US monetary aggregates and trade figures cause some concern. The Fed themselves bought $170 mn. in the market against marks. The Bundesbank gave the dollar heavy support on one day, but then left the market largely to itself; they bought $460 mn. altogether as the mark gained 1/2% to 1.8345. The mark remained leading 2 1/4% currency in the snake, closing 2% above the Danish krone (5.28 1/2) at the bottom. The Belgians (who increased Lombard rate by 2% to 11%) supported their currency heavily, selling $50 mn. and $230 mn.-worth of marks; the Danes on the other hand did very little. These currencies scored 73 and 71 on the divergence index. The Dutch (2.0235) were concerned about the position of their currency in the snake, buying in $80 mn. worth, half against marks; and the French (4.26¼), although comfortable in the snake, bought $45 mn. but sold $60 mn.-worth of marks, with their eye on the cross-rate which closed at 2.32¼. The lira remained overall top of the snake, 3¾% above the krone at 824.30. The central bank did not intervene. Outside the snake, the Swiss franc gained 1/2% to 1.6499, after official purchases of $390 mn. Unlike most other currencies, the yen eased back against the dollar, to 216.72; Japan is probably most vulnerable to oil price rises and shortages. There was no intervention. The Irish pound improved to 2.0592 but its discount against sterling rose to 8%. The Swedish crown received another $150 mn. of support.

Gold fell sharply, from $282 to $275, on Thursday afternoon, but subsequently recovered to $283.50 to show a gain of $1.70 over the week. The IMF auctioned 444,000 ozs. at an average of $281.52.

5th July 1979.

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