

SECRET

MR. McMAHON

FOREIGN EXCHANGE AND GOLD MARKETS

Tuesday, 31st July 1979

Sterling plummeted today - by 2½% against the dollar and almost as much on the ERI - as end-month squaring mounted into an avalanche and few, if any, willing buyers were found to take the strain. The dollar drew comfort from this and remained very firm. Sterling's ERI fell from 73.8 to 72.1.

The pound was heavily offered in the United States yesterday, chiefly by the Chicago IMM, and fell from 2.3177 at the London close to 2.2872 before closing at 2.2900. The first hour this morning was very nervous. Sterling opened at 2.2885, touched 2.2940 as overnight profit-taking orders were executed, but then sold off sharply as Continentals came in to test the new levels. The pound fell to 2.2790 before steadying and this brought out a large commercial buyer who acted as a useful prop and restored some order and calm. The news that Kuwait was to reduce its oil production also applied some modest pressure to the dollar and consequent relief for sterling. Once American markets reopened, however, the pound was immediately under pressure once more. Chicago was again prominent, New York banks were outright forward sellers and at least one major European was a large seller. For a wild half-hour sterling was a one-way market as pounds were passed on at any price. The rate fell to 2.25 before turning and thereafter swung widely and nervously between that level and 2.2650 before closing at 2.2595. Later still sterling was sold down to 2.24. Forward margins continued to widen. Three months' cover cost 3½% p.a. at the finish and sterling's intrinsic discount rose to 7/16%.

The pound gave up 2½% to the French franc (9.63½) and 2½% to each of the Swiss franc (3.75) and deutschemark (4.14½). These all continued to give ground to the dollar, closing at 4.2625, 1.6595 and 1.8345 respectively. The Bundesbank sold \$60 mn. late yesterday but were idle today. The Swiss, however, sold \$65 mn. and swapped in \$75 mn. while the French swapped out \$40 mn. At the bottom of the snake the Danish krone (5.28½) weakened so that the band was 2½% in width at the day's end and the lira (821.05) 4 5/16% above the floor. The Italians took in \$65 mn. The punt (2.0460) recovered to 9½% discount on sterling. The yen closed at 216.90 in Tokyo and 216.77 in London.

Gold was heavily sold in New York yesterday and fell further this morning before fixing at \$295.35. There was some recovery this afternoon and the later fix set a level of \$296.45.

Operations:	Market	- \$53 mn.
	Saudi Arabia	+ 34
	Post Office	+ 5
	(PSB G'teed)	
	Sundries	- 14

		- \$28 mn.
		=====
	Overnight	- \$18 mn.
		=====

The result for July is an increase of \$1,429 mn. to a reserve level of \$23,499 mn. after net public sector and IMF debt repayments of \$276 mn. The ECU swap contributed \$349 mn. (purely the effect of valuation). The overbought forward position was reduced by \$286 mn. to \$1,559 mn. but this was more than accounted for by the forward leg of the ECU swap.

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