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MONEY MARKETS UP TO 7 JANUARY

Over the holiday period the main problem in the daily money position was the wide Exchequer swings which apart from Christmas Eve, 2 January and 7 January were in the market's favour. This led to rather more comfortable conditions than expected and one effect on the discount houses was pressure (mainly last week) on their 20X limit as they were unable to sell bank bills to the Bank or in the market (at the same time quite sizeable quantities of bills bought by the Bank earlier were maturing). As a result we saw bank bill rates climbing, to - at one time - a 1m bid rate of over 14½%. Following shortages on Monday and Wednesday this week, the Bank have been able to buy in bank bills (some £275 mn) and rates have softened as a result with the 1m rate now standing at 14½ - 14%.

Reduction in Reserve Asset Ratio

Market concern over the January tax season and its effect on liquidity was reduced by the announcement last Friday afternoon that the RAR was being reduced to 10% on 5 January. Houses however were then faced with the prospect of a lower level of call money and reactions to this were mixed. In practice we have so far seen few problems and the clearing banks which account for the major portion of call money have not resorted to wholesale calling (fully realising the effects of such a move on other rates in the current 'surplus' conditions), proposing instead to reduce their reserve asset rates<sup>10%</sup> gradually as the liquidity pressures build up. Those with holdings of Treasury and Local Authority Bills expect to reduce their holdings slightly.

The effect of the reduction was quickly reflected in the inter-bank market where rates eased - most noticedly in the week rate which had

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dropped by  $\frac{1}{2}\%$  at one stage. Overnight rates were particularly soft and at one stage a discount house was bidding a higher rate in morning trading than could be obtained on the inter-bank market.

#### Treasury Bill Tender

The average rate at the tender has fallen from 13.1347 on 19 December to £12.9871 last Friday - a pro rata price of £96.76. The reduction in the amount on offer this Friday - to £100 mn - has of course been a talking point, and the immediate response has been that the rate is likely to be pushed down further despite an apparent (not unnaturally) drying up of demand from the banks. Indeed the houses have been buying bills and because of the unattractive yield in relation to cost of money (currently about 13.6 - 13.7%) have been selling them onto the Bank. Clearly any step taken to remove the 15% requirement for TBs as security for market borrowing may have an effect on the discount houses which currently see a need for a certain level of holding.

#### Other points

Two houses - Union and Alexander - had their year-end on 31 December and indications are that both will be reporting reasonably encouraging figures for the year. Union in particular have seen very profitable trading conditions. Alexander have made a satisfactory recovery after their difficulties in 1979.\* There is plenty of speculation on the course of events 'in the spring', with eligibility and primary liquidity of particular interest and relevance to the discount houses. There is still some concern over the difficulties the market may encounter in providing sufficient paper to relieve forthcoming shortages, given the Bank's likely reliance on bills.

\* An interesting point is that as a result of very heavy mopping-up on 31 December, both these houses were allowed to exceed their 30X limit that night by the amount of bills they bought. This will result in a higher level of footings in their annual accounts than would normally have been warranted, but of course these limits are only known to the house concerned and the Bank.



The revision of the morning forecast as a result of information from the Treasury coming through after 9.45 am has stirred up views on the value/effects of the forecast which does tend to have an immediate effect on rates. The question of information flows on money positions is of course likely to require greater attention in the future monetary system and liaison on trying to improve the Exchequer figures has already started.

Money Markets Division HO-M  
8 January 1981

M T R Smith

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