

SECRET

FOREIGN EXCHANGE AND GOLD MARKETS

Week ending 21st January 1981

Exchange markets were active and nervous in the days leading up to the departure of the US hostages from Iran. Their release saw a return to the more normal pre-occupation with interest rates and, as US rates fell temporarily, the dollar surrendered earlier gains. Sterling was in strong demand, establishing new highs on the Continent. The ERI rose 0.8 to 80.2.

Good commercial and professional buying of sterling was seen on most days during the week but official demand seemed to be on a smaller scale than last week. Sterling closed at 2.40 in New York on Wednesday night and opened a little lower at 2.3983 against a stronger dollar the next morning. The rate traded around the opening level in a very stable market but dipped in New York on Thursday night to 2.39 when the dollar firmed after the publication of the 1% rise in the Industrial Production index. A large buying order, probably of Middle East origin, took the rate to 2.4025 on Friday afternoon but it fell back to close firm at 2.3985 that evening. After the weekend, with the dollar slightly easier, sterling was in widespread demand on commercial account and the rate moved steadily upward reaching 2.4245 on Tuesday morning when substantial buying interest from Switzerland was seen. As the dollar weakened further on Wednesday, following the release of the hostages and an easing in Euro-dollar rates, sterling rose to touch 2.4330 in early business before settling to trade around 2.42½. The rate closed very firm at 2.4260, a rise of 3 cents on the week. The pound moved to new benchmark levels in Europe, rising 1½% against the deutschemark to 4.83 (after 4.84½), 1% in France to 11.16½ (after 11.21) and 1½% in Switzerland to 4.38½ (after 4.41½). An all-time high of 2303 was established against the lira on Tuesday. Against the ECU sterling went to 1.8725, a premium of 17½% on the notional central rate. Euro-dollar rates fell ½% over the week, three-month deposits closing at 18 5/16% after allowance for technical factors. With the cost of cover falling to 3½% there was a covered differential of 1/16% in favour of London.

The dollar's performance was influenced by the release of the hostages by Iran, concern over future Iranian intentions towards the dollar and the volatility of US interest rates. Probably the last of these factors was the most significant and, when Fed Funds broke well below the 20% level on Tuesday, the dollar gave up earlier gains, closing little changed over the week. Fed intervention amounted to net sales of \$130mn. against deutschemarks and the mark closed at 1.9907. There was no change in EMS, where the Belgian franc (32.01) closed 2½% below the French franc (4.6022) with the lira (946.55) 3 13/16% adrift after sales of \$210mn. Elsewhere, the Swiss franc (1.8090) fell to 0.90% against the deutschemark. As the dollar eased, the yen again moved through the 200 level, closing at 199.12 after purchases of \$120mn. by the Bank of Japan. The Swedish crown came under very heavy pressure, the Riksbank sold \$640mn. and Swedish discount rate was raised by 2% to 12%. The Canadian dollar was firm and the Bank of Canada were able to buy \$20mn. net.

The gold market moved uncertainly, mostly in the \$560-570 range, prior to the release of the hostages. Once this source of anxiety was removed the price started to rise, helped by lower US interest rates. It reached \$578 at the afternoon fix on Wednesday, a rise of \$20 over the week.

21st January 1981.

TRS

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RATES, ETC.

<u>10.15 a.m.</u>		<u>10.15 a.m.</u>
<u>15th January</u>		<u>22nd January</u>
<u>2.4015</u>	E/\$	<u>2.4208</u>
<u>79.7</u>	Effective exchange rate index	<u>80.5</u>
<u>4 5/16% pre.</u>	Forward 3-months	<u>4½% pre.</u>
<u>18 15/16%</u>	Euro-\$ 3-months	<u>18 11/16%</u>
<u>¾% disc.</u>	I.B.Comparison	<u>3/16% pre.</u>
<u>2.0000</u>	\$/DM	<u>2.0102</u>
<u>4.80¼</u>	E/DM	<u>4.86¾</u>
<u>11.11½</u>	E/FF	<u>11.25¼</u>
<u>202.70</u>	\$/Yen	<u>200.15</u>
<u>\$565</u>	Gold	<u>\$569</u>
<u>1.8130</u>	\$/S.Fc.	<u>1.8218</u>
<u>4.35¾</u>	E/S.Fc.	<u>4.41</u>