

1. MR PERETZ *Dec 12/2*
 2. FINANCIAL SECRETARY

cc Principal Private Secretary
 PS/Chief Secretary
 Sir D Wass
 Mr Burns
 Sir K Couzens
 Mr Barrett
 Mr Hancock
 Mr Middleton
 Mr Britton
 Mr Lavelle
 Mr Monck
 Mr Unwin
 Mrs Lomax
 Mr Riley
 Mr Turnbull
 Miss O'Mara
 Mrs Rowlett
 Mr Spencer
 Mr Towers
 Mr Ridley
 Mr Cardona
 Mr Anson - UKTSD
 Mr Sangster
 Mr Byatt
 Mr Gill
 Mr Smeeton } B/E

INTERVENTION IN JANUARY 1981

This note discusses the Bank's intervention tactics in "dealing January" ie 30 December 1980 to 28 January 1981. It also comments on the intervention figures for banking January. Tables showing reserve transactions for January and on a cumulative three and six month basis are attached.

Prospects at the beginning of January

2. At the start of dealing January the Bank had advance knowledge of calls on the reserves totalling £606 million, mainly representing Government expenditure, interest and debt repayment. These would be partly offset by £566 million of maturities of

544/2

337/81

forward purchases of foreign currencies from previous months' operations. In addition about \$300 million was likely to accrue to the reserves as a result of interest received and new borrowing.

January as a whole

3. The main features of January were :

(a) The rate rose steadily in effective terms from 77.9 to 81.6* (4.7%) with sterling frequently in demand from official and some commercial buyers. The pound moved in a fairly narrow band against the dollar which was itself much stronger against European currencies as the markets showed confidence in President Reagan. The sterling-Deutschemark rate rose from 4.63 to 5.01 (8.2%) as the DM weakened sharply reflecting both fears about Poland and expectations of a continuing German current account deficit.

*Effective rate index numbers are shown on the old basis as the new index was not introduced until 2 February 1981.

(b) The Bank bought \$255 million from the market, spread fairly evenly throughout the month.

(c) Bank customer purchases of sterling amounted to \$488 million, of which \$225 million could be offset against off-market purchases of foreign currency by Government departments. \$227 million of these customer purchases occurred on 13 January when there was very heavy official demand from a number of sources, a substantial part of which was turned away by the Bank.

During the month as a whole some very large orders for sterling, including those from the Sheikh of Dubai and the European Commission (to finance our EC Budget refund), were overhanging the market. The background to this exceptional demand for sterling was set out in our note of 29 January.

(d) Maturing forward swaps amounted to £566 million and in the absence of forward market operations the underlying rise in the spot reserves would have been £1102 million. £794 million of this was swapped forward to bring the underlying rise in the spot reserves down to £308 million.

(e) The net effect of forward operations (ignoring the revaluation arising from the renewal of the EMCF swap) was to increase the forward book by £229 million. Total intervention (spot and forward) was £537 million.

Intervention in dealing January

4. At the start of dealing January, sterling stood at £2.3685 and 77.93 effective. In the first two weeks of the month there was very substantial official demand for sterling with the Dubai

order also affecting the markets. Demand from Europe remained heavy during the next week, although towards the end of the month attention switched to the dollar and the DM. However, with little selling of sterling, the rate continued to rise against the continental currencies and in effective terms. The Bank intervened throughout the month to offset some of the upward pressure on the rate. The details are:

(£ million)

<u>Period</u>	<u>30 Dec-13Jan</u>	<u>14 Jan-22 Jan</u>	<u>23 Jan-28 Jan</u>
Closing dollar rate	2.3874 (+0.8%)	2.4120 (+1.0%)	2.4117 (-)
Closing effective	79.33 (+1.8%)	80.33 (+1.3%)	81.6 (+1.6%)
Market intervention	+87	+90	+78
Customer transactions	+295	+177	+16
Net forward transactions	+197	+18	+14

Figures in brackets show percentage change in period

Banking January

5. Intervention in banking January (11 December - 21 January) was as follows

	(£ million)
Market intervention	+89
Central banks (customer transactions)	+202
Government, interest receipts etc	-205
Public sector borrowing (net)	-23
Swaps outside the banking month -	
new swaps	-205
maturities	+94

Total (change in reserves*)	-34
Official borrowing (inc -)	+93
Official transactions contribution to external and foreign currency finance adjustment to £M3	+59

* Components do not sum to total, largely because of different conversion rates.

The central banks figure includes the substantial off-market sales of sterling to customers in the first three weeks of January. No new swaps were undertaken over the January make-up day for the purpose of assisting domestic money market operations. £50 million of the £150 million assistance given in banking October remains outstanding.

(iii) Interest on the reserves	-114	-
TOTAL INTEREST	+308	-229
(iv) Public sector borrowing under ERM		
(a) borrowing	+213	
(b) repayment	-168	
Net	+45	
(v) IMF gold facility repayment	-7	
(vi) IMF SDR allocation	+57	
(vii) Revaluation arising from renewal of 1982 swap	-266	-266
CHANGE IN THE RESERVES	+918	-37

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12 February 1981

30. 201-January levels 2034 1555
 During this period the rate fell from #2.3025 to #2.3035 but rose from 28.42 to 31.14 in effective terms.

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RESERVE TRANSACTIONS FOR JANUARY 1981

	\$ million	
	Spot	Forward
1. End-December levels	27476	1592
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2. Transactions in January		
(i) Market	+255	+1
(ii) Swaps	-794	+794
(iii) Maturities	+566	-566
(iv) EC Commission drawings	-	-
(v) Other Bank customers	+488	-
(vi) Government		
(a) departments' expenditure	-225	-
(b) public sector debt interest	-64	-
(c) HMG debt interest	-32	-
(vii) Interest on the reserves	+114	-
TOTAL INTERVENTION	+308	+229
(viii) Public sector borrowing under ECS		
(a) borrowing	+213	
(b) repayment	-164	
Net	+49	
(iv) IMF oil facility repayment	-78	
(x) IMF SDR allocation	+373	
(xi) Revaluation arising from renewal of ERM swap	+266	-266
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CHANGE IN THE RESERVES	+918	-37
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3. End-January levels	28394	1555
During this period the rate fell from \$2.3825 to \$2.3755 but rose from 78.42 to 81.14 in effective terms.		

RESERVE TRANSACTIONS NOVEMBER 1980-JANUARY 1981

£ million

	Spot	Forward
1. End-October levels	28026	1845
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2. Transactions November-January		
(i) Market	+400	+12
(ii) Swaps	-2083	+2083
(iii) Maturities	+2116	-2116
(iv) EC Commission drawings	-	-
(v) Other Bank customers	+855	+3
(vi) Government		
(a) departments' expenditure	-673	-5
(b) public sector debt interest	-282	-
(c) HMG debt interest	-196	-
(vii) Interest on the reserves	+330	-1
TOTAL INTERVENTION	+467	-24
(viii) Public sector borrowing under ECS		
(a) borrowing	+442	
(b) repayment	-628	
Net	-186	
(ix) IMF oil facility repayment	-78	
(x) HMG ILL capital repayments	-350	
(xi) North American loans - capital repayments	-124	
(xii) IMF SDR allocation	+373	
(xiii) Revaluation arising from renewal of EMCF swap	+266	-266
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CHANGE IN THE RESERVES	+368	-290
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3. End-January levels	28394	1555

During this period the rate fell from £2.4287 to £2.3755 but rose from 79.35 to 81.14 in effective terms.

RESERVE TRANSACTIONS AUGUST 1980-JANUARY 1981

£ million

	Spot	Forward
1. End-July levels	28272	2005
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2. Transactions August-January		
(i) Market	+966	-1
(ii) Swaps	-3750	+3750
(iii) Maturities	+3842	-3842
(iv) EC Commission drawings	-	-
(v) Other Bank customers	+1515	+3
(vi) Government		
(a) departments' expenditure	-1305	-11
(b) public sector debt interest	-414	-
(c) HMG debt interest	-365	-
(vii) Interest on the reserves	+715	-1
TOTAL INTERVENTION	+1204	-102
(viii) Public sector borrowing under ECS		
(a) borrowing	+769	
(b) repayment	-790	
Net	-21	
(ix) IMF oil facility repayments	-158	
(x) HMG III capital repayments	-1500	
(xi) North American loans - capital repayments	-124	
(xii) IMF SDR allocation	+373	
(xiii) Revaluation arising from renewal of EMCF swap	+348	-348
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CHANGE IN THE RESERVES	+122	-450
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3. End-January levels	28394	1555
During this period the rate rose from £2.3321 to £2.3755 and rose from 74.51 to 81.14 in effective terms.		