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MR COLLEBY
THE GOVERNOR'S PRIVATE SECRETARY

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Copies to Mr Fforde
Mr George
Mr Gill
Mr Byatt
Mr Lattar
Mr Foot
Mrs Drummond
DGPS

MONEY MARKETS DURING WEEK ENDED 18 MARCH

General Conditions

After the difficult money markets conditions in the wake of the Budget, we are beginning to see somewhat more settled conditions as far as rates are concerned. However daily conditions have continued to be very tight with exceptional shortages last Thursday (as a result of gilt sales) and on Monday (mainly due to heavy maturities of commercial bills in the Bank's hands). However temporary relief was afforded both on Tuesday and yesterday when virtually no assistance was necessary. Yesterday was the March make-up day and market conditions (a moderate surplus) should have been comfortable enough, although discount houses were finding it hard to attract money late in the day as banks had already positioned themselves for the published RAR figures. The easing of rates in the overnight and week periods this week has also resulted in considerable flows back into the clearers as borrowers were able to pick up cheaper market lines. One clearer, National Westminster, mentioned yesterday that they had seen £400 mn come back which left another £200 mn or so outstanding from the heavy drawings on overdraft during the tight conditions earlier in the month.

Daily money positions

Despite doubts in the discount market about their ability to cope with the heavy shortages at the end of last week, we were able to buy in a total of nearly £900 mn eligible bank bills in the last week, as well as mobilising another £500 mn of bills under the sale and repurchase technique. There has not unnaturally been a return to longer bills by drawers but even on Monday a surprising amount of the bills we purchased outright was newly drawn one month

paper. Nevertheless some houses have seen their liquidity at uncomfortably low levels, and the reduction in the RAR last Thursday certainly did not help.

The rest of this week ie today and tomorrow, we are expecting shortages of £300 mn and £850 mn and it must be doubtful whether we shall be able to buy out shortages of that size by purchases of paper alone. We do not know whether the civil servants' strikes will affect the position but it is likely that if they do, the effect will be favourable to the market! So far there has been little effect on our figures from the dispute.

The Bank papers

Reactions to the Bank papers on 'Liquidity' and 'Monetary Control' have generally been favourable, and the discount houses certainly welcome the proposals for a 'call money' club linked to eligibility. There is considerable interest in the reciprocity angle to it, while many have expressed the hope that the 'eligible club' can be introduced in reasonably quick time. The one doubt which has been aired in some houses is the fine (sometimes negative) margins which will operate (and which they are already seeing on many of their assets) and the greater difficulties which the smaller houses may experience in paying their way, let alone making a profit. They are continuing to see negative margins in maintaining their liquidity at the moment, although this will improve as their average cost of money falls (currently about 12.5%, as against yields on bills of 12% or less).

Treasury Bill Tender

Rather ironically, in view of the cut in MLR earlier in the week, the pro rata price last Friday rose by 6½p. This was partly due to the rate having been pushed too far prior to the Budget, and partly due to the knowledge that this week was already nearly £2 bn short. There was also a tender later that day for £153 mn. Westminster bills. I would not expect to see any great change this Friday.

Other Markets

The inter-bank rates are now showing a fairly flat rate pattern all the way up to a year with a peak at 3 months. So far there are no signs of any bullish sentiment about the timing of the next cut, and my broker contact reports quite a lot of demand for 1 year money. There has been some demand from the continent for Euro-f, reportedly on arbitrage grounds. The local authority market is very active, as authorities rush to meet their requirements before the end of the financial year.

Other points

Discount houses generally are trading well below their capacity at the moment - on the latest figures at an average of around 22 times resources (as opposed to their maximum of 30 times). However with 5 houses due for their end-year at end March or 5 April, we would expect to see them at least increasing the size of their book, for balance sheet purposes.

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Money Markets Division HO-G
18 March 1981

M T R Smith (4710)