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THE GOVERNOR'S PRIVATE SECRETARY

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on 2/14

MONEY MARKETS DURING THE WEEK ENDED 8 APRIL

General Features

After the initial set-back (notably in the gilts market) on the announcement of the March M3 figures, the market yesterday shrugged off its disappointment and while accepting that the next drop in MLR may be postponed a little longer, feels that too much can be read into one month's figures. The fact that the annualised rate of increase in M3 over the last four months is only 9% has served to smooth concern. However, there are some, notably in the discount houses, who are concerned at the level of bank lending shown in the figures and at the implications of this for the future.

It is difficult to judge how much the March lending figures were affected by round-tripping and hard arbitrage, but when I called on the Treasurer of Barclays yesterday, he told me that their lending had fallen back a bit since the March make-up day and that the general picture was of a relatively flat level of lending which they thought would be unlikely to change for at least six months.

Daily money conditions

The continuing disruption in the Civil Service has been the main contribution to easy, if somewhat volatile, conditions in the money markets. The overall impression is of a high level of liquidity which is able to cushion the volatility of daily conditions, as we have seen swings of up to £200 mn. in a day (both ways) due to delays in disbursements or non-payment of taxes. Some of the Clearers are running reserve asset ratios of 10-12 1/2% as against the minimum requirement of 8%. Short-term inter-bank rates have eased on the comfortable daily positions, discount houses have

built up their liquidity considerably (bills totalling nearly £600 mn. have been sold back to them in the last week), and as a result banks are finding it difficult to get their surplus funds away after lunch, except at very low rates. Some houses are even uncomfortably close to their 20x (undefined assets) limit and would probably welcome the chance to sell paper to the Bank, since there has been only spasmodic demand in the market for bills. As a result of the general easing of short-term rates, the houses have seen their average cost of money drop to about 11 3/4%, thus providing them with a more favourable running margin in maintaining liquidity.

Our new method of inviting bids or offers of bills at a rate of the market's choosing has operated on most days in the last week but few conclusions can be drawn at this early stage on how the market will respond, especially in more difficult times. The rate structure in the market has shown little change in the last week, especially as far as bank bills are concerned. One question which is being raised is whether the Bank will have a preference for a particular type of bill in relieving a shortage i.e. will Treasury Bills be accepted in preference to bank bills? If the market discern any such preference on the part of the Bank, this will inevitably have repercussions on the rate structure of the different types of eligible bills.

Treasury Bill tender

The rise in the pro rata price last Friday was by 2½p to £97.15 with 77% of the bills going to the market. With little demand, any move this week is likely to be minimal, possibly by 1 or 2p upwards.

Other points

Our quarterly revision of total discount market resources has produced an increase of some 2.2% since the end of the year.

While discussions are taking place with the various banking associations on the future monetary control system, the discount market are discussing their response to the proposals and hope to

come forward with something very soon. Houses appear a little more relaxed about the future, possibly as a result of experiencing easier trading conditions in the last 10 days or so.

MTS

Money Markets Division (HO-G)
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