

SECRET

1981/20

FOREIGN EXCHANGE AND GOLD MARKETS

Week ending 20th May 1981

The abiding weakness of the French franc and the relative firmness of U.S. interest rates continued to dominate the exchanges this week, drawing substantial official support for European currencies. The dollar touched new benchmark levels. Sterling traded in modest volume and the ERI finished unchanged at 98.5.

After closing in New York last Wednesday at 2.0740, the pound began on Thursday at 2.0722 and, in the face of a very strong dollar, declined quickly to 2.0630, its lowest level for 18 months. The dollar soon ran out of steam, however, as the market seemed sated by recent official offerings and, when Federal funds in New York began to soften sterling recovered ground, touching 2.0825 on Friday morning. Wide-spread confusion over the import of Friday's U.S. monetary aggregates brought a sharp fall in eurodollar deposit rates on Monday and, when a large commercial buyer of pounds appeared, sterling was dealt up to 2.1005. An increase in U.S. prime rates to 20%, however, turned the tide in the dollar's favour again and, following Tuesday's substantial upward revisions to first quarter U.S. G.N.P. statistics, the dollar broke new high ground in New York, sterling falling to 2.0710. This new strength was met with heavy and aggressive official selling in Europe on Wednesday which put the dollar to flight and brought sterling to close at 2.0805. The pound was a little firmer in France (11.51 $\frac{1}{2}$) and Germany (4.77 $\frac{3}{4}$) but lost another 1 $\frac{1}{2}$ % in Switzerland (4.25 $\frac{3}{4}$). Against the ECU sterling's premium over its notional central rate rose to 2 $\frac{1}{2}$ %. Although remaining relatively firm, the three-months eurodollar rate finished the week at 18 7/16%, lower by around 1% (after technical adjustment for the forthcoming holiday weekend). Sterling's forward premium narrowed by $\frac{1}{2}$ % to 6 13/16% p.a. and the covered differential moved to $\frac{3}{8}$ % in London's favour.

EMS was fully stretched for most of the week and very heavy support was again given to the French franc, the Bundesbank buying francs worth \$370mn. and the Bank of France selling deutschemarks worth over \$1 $\frac{1}{2}$ bn. The Dutch, too, spent \$50mn.-worth of deutschemarks. On Thursday the dollar set new recent highs in most centres and, as these levels were approached again on Wednesday morning, vast official sales of dollars were unleashed. During the week the Bundesbank sold over \$800mn. but the deutschemark closed a touch easier at 2.2960 (after a 4-year low of 2.3150 on Tuesday in New York). The Italians spent \$425mn., the lira finding a new nadir at 1150.50 before closing at 1141.70. Other participants in EMS together spent around \$175mn. but the Belgians were able to recoup nearly \$100mn. The Belgian franc and Dutch florin touched their lowest levels for 5 years, respectively 37.75 and 2.5737 while the French franc (5.5850) was at its cheapest since 1969, as panic selling developed before the weekend. It finished the week, however, at 5.5340 and at 82 on the index of divergence. The Swiss franc (2.0927) found a 3 $\frac{1}{2}$ -year low on Thursday but, as fears of tighter domestic liquidity mounted, it recovered to finish at 2.0447. Against the deutschemark it advanced strongly to 0.88 13/16 at one stage, continuing to benefit from the French outflow while the German currency was weighed down by the volume of support for the French franc. The Swiss sold a few dollars on Wednesday, as did the Japanese on Thursday when the yen touched a 9-month low of 223.55. It finished the week at 220.82. The Swedes added over \$150mn. to reserves.

Gold traded in a narrow range throughout the week, never far from \$480. Volume, however, was somewhat increased. Overall the price fell by nearly \$5 with the final fixing at \$479.75.

20th May 1981.

JGH

RATES, ETC.10.15 a.m.10.15 a.m.

<u>14th May 1981</u>		<u>21st May 1981</u>
<u>2.0686</u>	<u>£/\$</u>	<u>2.0900</u>
<u>98.3</u>	<u>Effective exchange rate index</u>	<u>98.9</u>
<u>7 11/16% pre</u>	<u>Forward 3-months</u>	<u>6 13/16% p.a. pre.</u>
<u>20. 1/16%</u>	<u>Euro-\$ 3-months</u>	<u>19 1/4%</u>
<u>1/16% disc.</u>	<u>I.B.Comparison</u>	<u>1/8% disc.</u>
<u>2.3047</u>	<u>\$/DM</u>	<u>2.2940</u>
<u>4.76 1/4</u>	<u>£/DM</u>	<u>4.79 1/2</u>
<u>11.48 5/8</u>	<u>£/FF</u>	<u>11.55 5/8</u>
<u>222.40</u>	<u>\$/Yen</u>	<u>220.92</u>
<u>\$480</u>	<u>Gold</u>	<u>\$481</u>
<u>2.0812</u>	<u>\$/S.Fc.</u>	<u>2.0455</u>
<u>4.30 1/2</u>	<u>£/S.Fc.</u>	<u>4.27 1/2</u>