

SECRET

THE DEPUTY GOVERNOR

FOREIGN EXCHANGE AND GOLD MARKETS

Thursday, 21st May 1981

The absence of any policy changes from the Bundesbank Council's weekly meeting, the lower profile of their dealers in the exchange market and extremely tight conditions in the Federal funds market combined to propel the dollar to new high levels this afternoon. As usual in these conditions, sterling was largely ignored and scored gains against all but the dollar. The ERI rose to 98.7.

The pound closed at 2.0907 yesterday in New York where the dollar was generally softer. This morning, sterling opened at 2.0895 and hovered around that level for some time while the market tested the Bundesbank. Eventually eurodollars edged firmer and the dollar began a steady advance, largely unimpeded in Germany. Sterling drifted quietly back to around 2.08 by midday. With nothing emerging from the Bundesbank's weekly meeting, the upward pressure on the dollar intensified and large sums were bid for in the Frankfurt fixing. Again the rate took the strain. Federal funds in New York began the new week very firmly and were soon trading over 20%. The dollar marched on to new benchmark levels and sterling fell back to 2.07 before closing at 2.0722. Three-month eurodollars closed nearly $\frac{1}{2}$ % better bid at 19 $\frac{1}{2}$ % (after adjustment). Sterling's forward premium widened to 7 $\frac{1}{16}$ % p.a., giving interest parity on the covered comparison.

The pound regained $\frac{1}{2}$ % in France (11.58 $\frac{1}{2}$) and Germany (4.80 $\frac{1}{2}$) and $\frac{1}{2}$ % in Switzerland (4.28 $\frac{1}{2}$). Against the dollar, the deutschemark closed at 2.3195 (later 2.3230, a four-year low). The Bundesbank sold \$75mn. The Swiss franc was 2.0690 (later 2.08) and the French franc 5.5915. Earlier the latter had traded to 5.6150, thought to be its lowest level since the First World War, if not earlier. The Belgian franc (37.84) and Dutch florin (2.5800) found new five-year lows and the Swedish krona (4.92) a ten-year floor. EMS was under almost continuous pressure. The Bundesbank bought \$96mn.-worth of French francs while the Bank of France spent deutschemarks worth \$882mn. At the close the lira (1149 $\frac{1}{2}$) led the system, after official Italian sales of \$190mn., some 2 $\frac{1}{2}$ % above the French franc - which stood at 87 on the index of divergence. The yen eased to 222.15.

After a quiet morning session in which the price was fixed at \$480, gold gave ground before the burgeoning dollar. The later fixing was \$475 and the close around \$472.

Operations:	Interest	+ \$8mn.
	India	+ 6
	Sundries	+ 3
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		+ \$17mn.
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