

FOREIGN EXCHANGE AND GOLD MARKETSWeek ending 26th August 1981

The exchanges were extremely volatile this week. Sterling met strong demand before the weekend, principally on expectations of a higher Saudi oil price, but was heavily sold after the weekend, following the collapse of the OPEC talks, and a sharp appreciation in the dollar, which stemmed from an apparent reappraisal of the interest rate outlook. The ERI rose from 91.3 to 91.4, after 92.5 on Friday.

Panic commercial buying of pounds in New York late on Wednesday added $2\frac{1}{2}$ cents to sterling's value and the rate approached 1.87 in the Far East on Thursday morning. The market swung widely throughout Thursday, the pound falling as far as 1.8347 but recovering by the close to 1.8632. Increases in sterling base rates by two American banks following the suspension of MLR, Volcker's suggestion of a downturn in US interest rates, and signs of a closer agreement at the OPEC meeting were all supportive. On Friday the pound generally traded above 1.86 but, after touching 1.8765, it eased on the breakdown of the OPEC talks. Nonetheless, following the Saudi decision that oil production would be cut, the pound was dealt up to 1.8950 in New York on Friday and touched 1.8930 again in the Far East on Monday morning. With the dollar hardening, however, following increases in both the US monetary aggregates and orders for durable goods, sterling retreated to around 1.87 by the close. Later, a precipitate decline in American debt markets prompted a reassessment of the outlook and, with the dollar bid on all fronts, sterling retreated to 1.8320. On Tuesday heavy professional selling of pounds further depressed the rate and, following publication of a 1.2% increase in the US CPI in July, the dollar again came into demand and sterling fell to 1.8172 before closing at 1.8260. Wednesday was better balanced. Some profits were taken in the dollar and the pound recovered to close at 1.8375. Sterling was easier on the continent, losing $\frac{1}{8}\%$ in France (10.88 $\frac{1}{2}$), $\frac{1}{8}\%$ in Germany (4.55 $\frac{1}{2}$), and $\frac{1}{8}\%$ in Switzerland (3.95 $\frac{1}{2}$). Against the ECU sterling's discount on its notional central rate was little changed at 2%. Sterling's three-month forward premium widened by $\frac{1}{8}\%$ to 5 9/16% p.a., more than offsetting a rise of $\frac{1}{8}\%$ in three-month eurodollars to 18 $\frac{1}{2}\%$ and producing a covered differential of $\frac{1}{8}\%$ in London's favour.

To some degree the pound and dollar fed off each other's strength and weakness and sterling was the first to be sold as the dollar recovered on Monday. Later, however, both the deutschemark and, on Wednesday, the Japanese yen met heavy professional selling. With Fed funds trading somewhat easier than of late towards the end of the week, the dollar's gains were trimmed. The DM closed $\frac{1}{8}\%$ better on balance at 2.4782 (after 2.4455 and 2.5170). The Bundesbank sold \$120 mn. There was some modest recurrence of week-end pressure in EMS and both the French franc and the Irish punt fell briefly to the bottom of the band. By the end of the week, however, the Belgian franc (40.50) had replaced them, 1 $\frac{1}{8}\%$ distant from the DM. The Irish sold \$75 mn., the French sold \$60 mn. and the Dutch \$15 mn., while the Danes took in \$30 mn. and the Italians recouped \$250 mn. The Swiss franc gained $\frac{1}{8}\%$ on the dollar at 2.1510 and improved to 0.86 $\frac{1}{2}$ against the DM. The yen advanced to 226.60 but was sold down to 232 on Wednesday before closing little changed at 230.45. The Swedes sold \$90 mn. in support of their krona.

Gold reflected the general uncertainty over oil and the dollar. Having topped \$440 in New York last Wednesday, it consolidated around \$430 before the weekend but was sold down sharply on Monday and Tuesday touching \$406 before finishing the week \$17.50 easier at \$414.

JGH
27th August 1981.

JGH

RATES, ETC.

<u>10.15 a.m.</u>		<u>10.15 a.m.</u>
20. 8.81		26. 8.81
1.8565	£/\$	1.8415
92.1	Effective exchange rate index	91.4
4½% p.a. pre.	Forward 3-months	5½% p.a. pre.
18 13/16%	Euro-\$ 3-months	19 1/16%
1/16% disc.	I.B.Comparison	3/16% pre.
2.4735	\$/DM	2.4665
4.59½	£/DM	4.54½
10.95½	£/FF	10.86½
229.32	\$/Yen	230.60
\$432	Gold	\$415
2.1532	\$/S.Fc.	2.1417
3.99½	£/S.Fc.	3.94½