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GPA 10/9

MONEY MARKETS DURING THE WEEK ENDED 9 SEPTEMBER 1981

General

A mood of uncertainty and caution has become apparent. The accumulating tide of depressing, albeit perhaps not positively alarming, economic news - money figures, inflation, exchange rate, industrial activity, etc. - leads the majority in the market to the view that generally higher interest rates will come sooner or later, but few are confident enough in such a prediction to stake their books on it. Meanwhile, the market has become well attuned to our own new practices and there are no notable complaints.

Daily operations

We bought a total of some £660 mn of bills outright on three days, with no business the remaining two. Our purchases were all in bands 1 and 2, continuing at rates of 12 5/8 - 3/4%. Broadly speaking, the need for this assistance can be ascribed to the sizeable flow of repos unwinding in this period, which had been entered into on short days in the run-up to 1 September.

On Monday the banks found themselves running short, long after the houses were square and after we had concluded that the day's position, without any intervention, was close to balance. The clearers' balances turned out to be some £160 mn below target and one of them only struck a positive balance after negotiating with others at the clearing. Such a practice ahead of the final clearing, if it became common, could theoretically allow the clearers to manage with considerably smaller operational targets, but there is no indication that they intend to have recourse to such deals in any but the most exceptional circumstances.

Interest rates

Rates have moved little on balance over the week. Those at the short end (up to one month) remain very much under the influence of our dealing rates, which have remained unchanged for several weeks; the exception is the overnight inter-bank rate late in the day, which has perhaps showed more volatility under the new arrangements, since banks have less fat to feed a late drain and are more anxious to find a haven for a late surplus. It looks at present as if the Treasury bill price will fall back (i.e. higher rate) tomorrow.

Bills

Drawings are currently concentrated very heavily on one-month paper. The conjunction of base rates and our dealing rates has established a fine choice for a blue-chip borrower between overdraft and acceptances; meanwhile, the discount houses are able to earn a positive, though small, margin from holding the one-month paper. Many of the houses express reluctance to hold longer paper (e.g. 3 months) at present rates; it appears anyway that drawers are not much attracted at current longer rates - perhaps because they do not wish to commit themselves for longer than a month at any price.

The market in ineligible bills has been very quiet since 20 August. The margin against eligible bills stands at about 3/8% for bills within a month of maturity, reflecting the concentration of our operations in this area, and at about 1/8% at three months. While admitting that conditions may not at present be particularly helpful for ineligible names seeking to develop their business, market contacts suggest that it is too early to draw definite conclusions. The houses remain willing to make the market in ineligible paper, but point out that they can only offer to take the paper at rates which provide a trading margin for them.

We continue to tackle a stream of enquiries about the quality and clausung of eligible bills.

A few banks are now quoting two-way prices for bills - an indication of willingness to trade them rather than lock their holdings away.

This is a helpful development so far as the health of the bill market is concerned, but it will put the houses on their guard against any hint of the banks not conforming to the new arrangements or any suggestion that we might, in any but the most extreme circumstances, purchase paper direct from the banks.

Money Markets Division
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A R Latter (4710)
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