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SECRET

THE DEPUTY GOVERNOR

FOREIGN EXCHANGE AND GOLD MARKETS

Tuesday, 15th September 1981

An absorbing session on the exchanges with many a cross-current beneath the surface. Sterling was tossed to and fro this morning as doubts were cast on its new-found buoyancy. By the end of the day, however, the pound was borne up on a flood-tide and coasted home on the crest of a wave. The dollar meanwhile gave up further ground elsewhere. Sterling's ERI leapt from 87.0 to 88.5.

The pound closed over two cents better at 1.8067 in New York yesterday. With Federal Funds trading below 16% and the Federal Reserve executing repurchase agreements for customer account (when many expected them to drain funds from the system), the dollar was generally a good deal easier, but sterling itself was particularly firm as sentiment continued to change in the wake of the Bank's earlier operations in the money market. This morning saw a similar trend. The pound opened at 1.8045; the dollar was quickly adjusted downward and sterling advanced rapidly to 1.8155 on the early exchanges. Still skeptical of the official resolve, the major players in London and Continental Europe then sold sterling down in a concerted drive to 1.8035. A guiding hand on the tiller, however, and a sudden sharp increase in inter-bank sterling deposit rates soon had them running for cover. The movement was reinforced by a softer tendency for the dollar, which emanated from Switzerland where the money market, too, was very tight. The pound surged on to 1.8185 and succeeded in consolidating around 1.8150, even though deposit rates came off around mid-day. New York returned determined to sell the dollar and, once again, dealers were now very anxious to stay on sterling's right side. The pound was swept on up to 1.8340 before profits were taken and the rate receded to 1.8242 before closing on an upbeat at 1.8320. Later, in a still volatile market, sterling retreated to 1.8262, only to recover again to top 1.84. Three-month Euro-dollars closed 3/16% easier at 17 9/16%, comparable sterling deposits 1/2% firmer at 14 9/16%. The forward premium, however, narrowed by only 9/16% to 3% p.a. so that interest parity prevailed on the covered comparison.

The pound rose by 1 3/8% in each of France (10.30%), Germany (4.29%) and Switzerland (3.67%). The dollar fell by around 1 1/2% in these countries to 5.62%, 2.3455 (later 2.3345) and 2.0060 (later 1.9965) respectively. EMS was stretched to 2 3/16% between the deutschemark and Belgian franc (38.43). The Dutch bought \$20mn. but the Belgians sold \$26mn. (all in deutschemarks), the Danes \$75mn. and the French \$190mn. (one-third of which in deutschemarks). The Swedes recouped a further \$163mn. in response to yesterday's devaluation. With the Japanese otherwise engaged showing respect for their aged, the market showed long overdue respect for their yen, which was bid up by over 2% to 225.45.

Having traded near to \$460 in New York yesterday, gold suffered profit-taking and was held in check this morning by the weakness of silver. The yellow metal was fixed at \$455.25 at the first session and later, in a long and difficult fixing, set a level of \$456. Towards the close, New York then took the price towards \$460 again, only to find renewed profit-taking.

Operations: Sundries + \$3mn.

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