

THE DEPUTY GOVERNOR

FOREIGN EXCHANGE AND GOLD MARKETSFriday, 25th September 1981

The market's response to President Reagan's package of expenditure cuts was clearly somewhat sceptical. Europe bought the dollar, though more on interest rate expectations than on enthusiasm for the package, while Americans tended to sell as short-term interest rates remained soft. In the end, however, Wall Street's negative response to the President (which included record high long bond yields) ensured a firm close. After an uncertain start, sterling performed well against the Continental currencies and the ERI rose from 85.7 to 86.4.

Following the sharp fall in the dollar during London's twilight hour yesterday, the exchanges were relatively calm and sterling closed with little further change at 1.7940 in New York. This morning, pound and dollar were sold in the Far East for the deutschemark. Sterling opened in London little changed on the dollar at 1.7935, dipped to 1.7905 on professional selling but rebounded strongly to 1.8005 as the official hand lent support. Central bank selling of deutschemarks for dollars turned the dollar firmer and, when the German trade and current account figures were released - both sharply worse than expected - the dollar continued to strengthen. Sterling declined progressively - to 1.7827 by early afternoon - but managed to outpace the Continentals. With Federal Funds opening at 14½% and easing quickly to 14% the dollar was sold in New York and sterling recovered to 1.7990 before relapsing to close at 1.7920. Later, however, the Federal Reserve's matched sales and the poor performance of Wall Street's Stock and Bond markets injected new life into the dollar and sterling was quoted down to 1.7787. The three-month forward premium narrowed by 3/16% to 1 11/16% p.a. although both dollar and sterling deposits, having each erased early losses, closed little changed. Sterling's intrinsic premium was thus reduced to more modest levels.

The pound gained ¼% on the deutschemark (4.15½), ½% on the Swiss franc (3.53½) and ¾% on the French franc (9.99½). The deutschemark recovered to 2.3190 (after 2.34) but was later quoted around 2.3350 again. The Bundesbank sold \$17mn. The Belgian franc (38.06) finished the full 2¼% adrift in EMS but required no support. The French, however, sold \$120mn. and \$23mn. of deutschemarks, their franc (5.57½) closing less than ¼% from its Belgian counterpart. The Irish sold \$27mn. of exchange, the Italians bought \$15mn. The Swiss franc (1.9725) was very firm as the end-quarter approached but the Swiss swapped in only \$10mn. The Swedes took in another \$68mn. The yen was little changed at 229.50.

Gold recovered in the Far East this morning on the dollar's early weakness and was fixed in London at \$451.75 this morning. Continuing to mirror the dollar, the metal eased somewhat later this morning but turned up to fix at \$450.50 this afternoon. Later, however, the price fell away and was around \$444 as London closed.

Operations:	Market	-	\$42mn.
	Sundries	+	5
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		-	\$37mn.
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	Overnight	-	\$34mn.
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