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MR COLEBY *h.c.*  
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MONEY MARKETS DURING WEEK ENDED 11 NOVEMBER

General Features

The last two weeks have seen quite a significant change in market sentiment. With the three-month inter-bank rate briefly trading at 17% on Monday, 26 October and the market talking of higher base rates, news such as Tuesday's EM3 figures would probably have proved the last straw. Much of the recovery in sentiment is, of course, attributable to developments in the US while Monday's cut in base rates and the BL settlement last week have undoubtedly helped to improve market confidence. Thus, the disappointing M3 figures have been virtually shrugged off even though many people had been looking for a good figure. In fact the impression yesterday morning was that the slight hardening of rates was not so much due to the money supply figures as to the strengthening of the dollar. In the event the market, while quieter and steadier yesterday, moved slightly ahead over the day.

The cut in base rates, from 15 1/2%-15%, undoubtedly took the market by surprise on Monday morning, and helped to fuel the strong bull market that day, particularly in the gilt-edged market where the long tap was sold out.

Over the week the period inter-bank rates have eased by 9/16/5/8% - up to a full point at one stage in the three-month rate. The houses' overnight secured money rate has dropped from 15 1/4% to 14 3/4% in the last three days.

The discount houses have shown greater confidence than of late but being conscious of the volatility of rates in the last two months are not lengthening their books by very much. Their inclination is to be prepared to sell longer assets at very short notice and

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to take short-term profits. However, their general expectation is that rates are unlikely to move up again in the near future.

#### Daily Money Conditions

The most significant event of the last week took place on Monday when a large swing against the market (mostly because of backlog tax) left the clearing banks' operational balances some £280 mn below their target figure of around £200 mn - and three of the big four were overdrawn. While the Bank did not become aware of this very large swing till late in the day - by which time it was too late to provide any form of assistance, the banking system appeared to be equally unaware of the likely outcome on the day. When we undertook operations after lunch to relieve the shortage as then known to us, the discount market itself was not very short and, indeed, was able to pick up money fairly easily. The inter-bank market tightened in the last half-hour to close at 30-20%.

The shortages over the last week have almost entirely been relieved by outright purchases of bills which have totalled just over £1 bn. Most of these purchases took place on Tuesday when we were required to deal with a market shortage of £650 mn (caused by heavy gilt sales on Monday and the need for the banks to replenish their operational balances). It was indeed a very successful outcome that with a shortage of that size the houses were able to mobilise sufficient paper in Bands 1 and 2 to sell to us. Some £78 mn was provided by means of a repo till next week, while one house required a small amount of (unpublicised) assistance at 2.45 pm.

While market rates were moving down last week, the opportunity had not appeared for the Bank to lower its 'stop' rate in its operations with the market until Friday when we were able to move down by  $1/16$  to  $15 \frac{1}{16}$  and  $15 \frac{3}{16}$  in Bands 1 and 2 respectively. On Monday following the  $1/2\%$  fall in base rates, our stop rate for both Bands 1 and 2 became  $14 \frac{5}{8}\%$  which was interpreted by the market as going along with the trend, and this, in fact, was the rate at which all the bills were purchased on Tuesday.

Treasury Bill Tender

The discount market obtained all the bills allotted last Friday when the pro rata price rose by 19p to £96.28 (equivalent to a discount rate of 14 15/16%). By Monday afternoon these were trading at around 14 1/4%, while the tender for £35 mn GLC bills on Monday afternoon produced a pro rata price of £96.425, 14 1/2p higher than the Treasury Bill outcome. The rate has remained at around this level since then, so bids in the region of £96.45 are likely tomorrow.

Other Points

Three discount houses, Secombes, King & Shaxson and Cater Ryder, have made interim statements following their half-years. The first two named have reported small profits, but Cater Ryder (whose offer for Allen Harvey & Ross has now become unconditional following an EGM) made no comment on their situation except to say that results had been disappointing.

The discount houses have responded to the Select Committee regarding the EEC proposed directive on disclosure of reserves.

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Money Markets Division  
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