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FOREIGN EXCHANGE AND GOLD MARKETS

Mr Bisnend

Week ending 13th January 1982

Concerns over US interest rates again dominated both the exchange and gold markets. Although the US economy continued to show signs of weakness, rising Euro-dollar rates helped the dollar to firm in all centres. Sterling suffered more than the other major currencies as dealers focussed on the industrial unrest in the UK. The ERI fell 1.2 to 90.3.

A sharp increase in Euro-dollar rates was not matched by any similar rise in sterling interest rates and the uncovered differential in favour of London narrowed. At the same time the commencement of industrial action on the railways and the threat of a strike in the mines also brought some pressure on sterling and widespread selling was seen in the latter part of the week. After closing in New York on Wednesday night at 1.9182, sterling opened in London on Thursday at 1.9157 and traded actively less than half a cent either side of this level throughout the day against a slowly strengthening dollar. Temporarily lower Euro-dollar rates, and a sharp increase in US unemployment, caused the dollar to weaken on Friday and sterling moved up to touch 1.9255 before closing at 1.9230. The disappointingly modest decline in the US monetary aggregates made for a much firmer dollar on Monday and sterling opened two cents lower and traded around 1.90 for much of the day. However, some sizeable selling commenced during the afternoon and continued on Tuesday when, following a weak performance by the US bond market, Euro-dollar rates moved up another ½%. With industrial problems adding to the softer appearance of sterling, the rate fell back, touching 1.8725 in late business that day. Softer Euro-dollar rates on Wednesday served to ease the pressure and sterling traded quietly, if a little nervously, around the 1.87½ level, before ending the period at 1.8760, five cents lower over the week. The pound lost ground on the Continent as well, falling ⅞% in Germany (4.28⅜) and France 10.87⅞) but closed unchanged in Switzerland (3.47¼). Against the ECU sterling's premium on its notional central rate fell to 5⅛%. Three-month Euro-dollars ended the week ½% firmer at 13 15/16%, after 14 7/16% on Tuesday. Sterling's forward discount narrowed to 1⅛% and the intrinsic premium to 5/16%.

Markets were only briefly impressed by another sharp rise in US unemployment and were much more concerned by the continued buoyancy of the money supply. The Bundesbank again provided only nominal support for the deutschemark which fell 2% to close at 2.2836. In EMS, the guilder (2.4975) replaced the French franc (5.7987) at the top; the Bank of France sold $45mn. The Belgian franc (38.86) remained at the bottom but the band was only 1 9/16% wide and the Belgian National Bank provided $70mn. in support. The Italians sold $160mn. Elsewhere, the Swiss franc (1.8512) weakened further against the deutschemark, closing at 0.81⅛. The yen was also weak and closed 2% lower at 223.87, despite sales of $210mn. from the Bank of Japan. The Riksbank continued to support the Swedish crown, selling $140mn.

Gold was an active but weak market and the price fell to its lowest level since November 1979. All of the fall occurred after the weekend as formerly firm holders, dismayed at the renewed rise in Euro-dollars, sought to liquidate positions. The final fixing at $380 represented a fall of $21.50 over the week.

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p.p. TRS