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SECRET

THE DEPUTY GOVERNOR

FOREIGN EXCHANGE AND GOLD MARKETS

Tuesday, 20th July 1982

The overnight $\frac{1}{2}\%$ cut in the Fed's discount rate took the market by surprise both as to timing and size. It enabled the move towards lower interest rates to be continued today (the Swiss commercial banks were quick to reduce their deposit rates by $\frac{1}{2}-\frac{3}{4}\%$) but markets were nervous, awaiting Volcker's statement on the US monetary targets to the Senate Banking Committee. Although Euro-dollar rates shed a further $\frac{1}{2}\%$, the dollar again weakened only reluctantly. Sterling was depressed by some sizeable official selling orders and the ERI closed 0.3 lower at 91.1.

The discount rate cut came too late in New York yesterday afternoon to have any great impact on the exchanges and sterling closed there at 1.7407. Although earlier than the market had expected, $\frac{1}{2}\%$ was regarded as disappointing and the dollar strengthened in the Far East, taking sterling back to 1.7365 by the London opening. With the dollar tending to ease elsewhere in Europe, sterling was traded actively around the opening level throughout most of the morning but fell to 1.7331 at the low under pressure of selling from a Japanese bank known to be long of sterling, and a US bank. Some modest commercial demand was seen towards noon, by when the rate had recovered to 1.7380 and when Fed Funds opened in New York at $11\frac{1}{2}\%$, it briefly touched 1.7385. However, the advent of some large official selling orders from Europe restrained the rate during the afternoon and it gradually gave ground to close at 1.7340. Three-month Euro-dollars lost another $\frac{1}{2}\%$ to close at $13\frac{3}{4}\%$. Sterling's forward premium fell only slightly to $1\frac{11}{16}\%$ and the covered differential widened to $\frac{3}{8}\%$ in favour of London.

The pound lost yesterday's gains on the Continent, surrendering $\frac{1}{2}\%$ in Germany ($4.27\frac{1}{4}$) and France ($11.88\frac{7}{8}$) and $\frac{1}{8}\%$ in Switzerland ($3.63\frac{3}{8}$). The dollar closed little changed in these centres at 2.4635, 6.8610 and 2.0970 respectively. The Irish punt (1.4010) remained at the top of EMS which widened to $2\frac{3}{16}\%$, with the guilder (2.7235) replacing the deutschemark at the bottom, $3\frac{3}{8}\%$ below the lira (1379.20). There was more intervention than on most recent days: the Italians bought \$69mn. and the Belgians \$50mn., while the Dutch sold \$10mn. and deutschemarks worth \$8mn. and the Germans sold \$3mn. Despite the fall in US rates, the yen was weak, closing at 254.42.

Gold enjoyed an active day. After fixing at \$344.25 in the morning, the price began to rise in the afternoon, helped by the lower Fed Funds rate. The second fixing was at \$347.75 but the price was later quoted up to \$355.

Operations:	Market	+	\$5mn.
	Interest	+	8
	Sundries	+	4
			<hr/>
		+	\$17mn.
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20th July 1982.
TRS

US BOND AND MONEY MARKETS

Tuesday, 20th July 1982

Federal Funds

Opening: 11½%
Range: 10¾% - 11½%
Close: 10¾%

US Governments (NY closing bids)

2-year: 101½ (+½) 13¼%
5-year: 100½ (-) 13 9/16%
10-year: 101¼ (+½) 13½%
30-year: 105½ (+¾) 13¼%

Euro-dollars (Today's opening
London bid)

7-day: 11¾%
1-month: 12 5/16%
3-months: 13 3/16%
6-months: 13¾%

Federal Reserve Operations:

US 3-month Treasury Bills 11%
US bank 3-month CDs 13¾%

Indicators

US personal income up 0.3% in June

Comment:

The market opened higher as a further response to the previous evening's discount rate cut. Prices traded up for a brief period before profit-takers pushed prices down, by the late morning, to around the previous night's close. Volcker's report to Congress had no effect. Towards the latter part of the afternoon, prices moved up again on another flurry of activity, as the Fed Funds rate declined below 11%.

21st July 1982.

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