FE 2/2 4 subs. for copy filed

CONFIDENTIAL

22. 7.82.

Thank you

GOVERNOR'S PRIVATE SECRETARY

Copy to Mr.Sangster

22/7

As requested, I attach a speaking note for the Governor's guidance at Court this morning, describing the foreign exchange and gold markets since the last meeting.

DAHB

22nd July 1982.

DAHB

CONFIDENTIAL

22. 7.82.

CR 22/7

FOREIGN EXCHANGE AND GOLD MARKETS
IN WEEK TO 10.15 A.M., 22ND JULY

The foreign exchange markets have been dominated by interest rate and money supply factors, stemming in particular from last week's American monetary aggregates. A seasonal bulge of +$10bn. in M1 had been generally feared (and thus the maintenance of a tight interest rate policy); although this estimated degree of change was somewhat tempered during Friday, the actual result of +$5.9bn. was at the lower end of expectations. Reaction was swift: the first prime rate cut by a large American bank (Manufacturers Hanover) was announced on Monday, from 16½% to 16%, and the Fed reduced its Discount Rate by ½% to 11½% with effect from Tuesday. These changes brought the rates into line with current market levels, the Fed's action being regarded as a sign that a greater reduction in prime rates would not have been welcomed by the authorities. This easing has enabled us to reduce our dealing rates this week in the money market by up to ¼%. Swiss commercial bank deposit rates have also been reduced, by up to ¾%.

Mr.Volcker's statement to the Senate Banking Committee, including the fact that there would be no relaxation in money growth targets but that temporary bulges would be tolerated when circumstances were exceptional, was in line with market expectations.

Against this background, the Fed Funds rate eased from around 13% to 11¼% on Tuesday (and further to 10¼% yesterday); Euro-dollars for three months have now fallen by about 1¼% to 13⅝% this morning. The dollar itself has eased by just over 2%, declining from 2.49 to 2.43¼ in Germany.

Sterling gained some strength from the calling off of the ASLEF strike but has since been sold for official account (EEC -£125mn. approximately) and will have softened a little by our own reductions in dealing rates. Over the week it has risen by some 1% in dollar terms to 1.74½ but lost some 2% against the deutschemark (4.25¼). The ERI is 0.2 lower at 91.1.

EMS moved out at times to nearly full width and has usually been bordered by the Danish crown and the deutschemark. The Belgians and Italians have recovered some reserves but intervention has been fairly muted.

The Canadian dollar has continued to improve and the Canadians have now recovered this month over half of last month's US$2bn. loss.

Gold has been extremely volatile and very heavily traded, reaching $368.50 yesterday afternoon. Short covering was evident and a number of chart points were successively breached. Silver, too, was firm. But in the last 10 minutes of New York trading yesterday there was a sharp fall. The net gain on the week is $10 to $358¼ ~~(pre-fixing today)~~.

[The Court may be interested to know that the Chancellor will be announcing tomorrow the resumption of bullion half-sovereign production, the first since 1915. The venture is experimental as the coin is hardly likely to compete with the nearest fractional krugerrand. But HMT believe there is a need for a British gold coin, cheaper than a sovereign. The Bank will handle the new coin as part of the EEA's coin operations.]