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THE DEPUTY GOVERNOR

FOREIGN EXCHANGE AND GOLD MARKETS

Tuesday, 17th August 1982

The conflicting influences on the direction of the dollar were again starkly apparent on the exchanges today. Rumours that AEG would file for liquidation tomorrow weakened the deutschemark and kept the dollar very firm during the morning. These fears were, however, outweighed in the afternoon by news that Henry Kaufman - for so long pessimistic about the prospects for lower long-term US rates - had revised his views and was now predicting further sharp declines over the next twelve months. The dollar gave up its gains on these reports and ended lower in all centres. Sterling saw some good two-way business, mainly in the morning when some sizeable commercial selling was absorbed without difficulty. The base rate cuts had no adverse effect and the ERI closed unchanged at 91.1.

Sterling closed quietly in New York yesterday at 1.7035. As the dollar strengthened in the Far East the rate opened at 1.70 and initially moved lower to 1.6957 in the face of some modest selling from Germany. When the dollar eased on lower Eurodollar rates, sterling recovered to trade around the 1.70 level for the remainder of the morning. The large commercial seller seen yesterday was again active but was counterbalanced by some useful demand on oil company account. Speculation about AEG's demise caused the dollar to strengthen again in late morning and sterling fell back below 1.70 for a time but with the commercial seller having apparently largely completed his business, the rate regained lost ground against the continental currencies. Kaufman's views made for a very strong opening in the US bond market and the dollar again began to ease in Europe, enabling sterling to move steadily higher. The rate reached 1.7063 shortly before closing at 1.7050. Three-month Eurodollars fell another $\frac{1}{2}\%$ to 11 $\frac{1}{16}\%$ and with sterling inter-bank rates falling to 11%, the forward premium for sterling was $\frac{3}{8}\%$.

The pound was a little easier in Europe, losing $\frac{3}{8}\%$ in Germany (4.27 $\frac{1}{2}$), $\frac{1}{2}\%$ in France (11.88 $\frac{1}{2}$) and $\frac{1}{8}\%$ in Switzerland (3.66 $\frac{1}{2}$). The dollar lost $\frac{3}{8}\%$ in each of the first two centres, to 2.5060 and 6.9725 respectively, but was little changed against a weak Swiss franc (2.1492). The French franc regained top position in EMS, 1 $\frac{13}{16}\%$ above the deutschemark which, in turn, was 3 $\frac{3}{8}\%$ from the lira (1401.50). The Italians bought \$37mn., the Irish \$4mn. and the Dutch deutschemarks worth \$4mn. The yen closed at a five-year low of 265.35 in Tokyo but recovered to 263.90 in London.

Gold could not hold yesterday afternoon's gains despite the lower financing costs. Fixings were at \$338 and \$337.75.

Operations:	Market	+ \$22mn.
	Sundries	- 1
		<u> </u>
		+ \$21mn.
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17th August 1982.
TRS

US BOND AND MONEY MARKETS

Tuesday, 17th August 1982

Federal Funds

Opening: 10%
Range: 9-10%
Close: 9%

US Governments (NY closing bids)

2-year: 102½ (+1½) 11 5/8%
5-year: 105½ (+2½) 12 1/4%
10-year: 107¾ (+3¾) 12 7/16%
30-year: 113¾ (+4¾) 12 1/4%

Euro-dollars (Today's opening
London bid)

7-day: 9 9/16%
1-month: 9 13/16%
3-months: 10 1/8%
6-months: 11 1/16%

Federal Reserve Operations:

\$1bn. customer repurchase agreements
with Fed.Funds at 9¾%.
Stop rate 9.10%.

Indicators

US housing starts rose 33.7% in July (c.f. -15.3% in June).
Citibank and Chemical prime rates to 14% from 14½%.

Comment:

An amazing day. The market opened firm with rumours that Kaufman had become bullish. When it was confirmed that he saw Fed.Funds declining to 6-7% and the yield on the long bond to 9-10%, the market bolted, closing at its highs.

18th August 1982.
TRS