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SECRET

THE DEPUTY GOVERNOR

FOREIGN EXCHANGE AND GOLD MARKETS

Friday, 21st January 1983

Diminishing hopes of lower US interest rates took the dollar higher in rather sporadic trading on the exchanges. A speech last night by Mr.Volcker which appeared to imply that no further cut in US discount rate was yet likely, together with reports that Henry Kaufman was becoming bearish about prospects for further falls in bond yields, completely outweighed the implications for interest rates of a further sharp fall in US inflation (consumer prices fell 0.3% in December, taking the annual rate of increase to 3.9%). Meanwhile, the relative weakness of the deutschemark meant there were few of the familiar pre-weekend pressures in EMS. Sterling enjoyed a comfortable day benefiting from news late yesterday that the Saudis might cut their oil production to preserve the $34 a barrel price and from the good RPI figures. The ERI closed 0.4 higher at 82.8.

Some good demand carried sterling to 1.5810 by the New York close last night and the rate opened at 1.5835 in London today. Although the dollar initially was easing elsewhere, sterling soon moved back to the 1.58 level as a further tranche of the large commercial selling order against deutschemarks seen yesterday was executed. With an oil company also selling sterling, the rate fell back to 1.5753 in mid-morning but then stabilised around the 1.5765 level. Although the dollar was by then moving higher in Europe, sterling held very steady, with reports of good commercial demand against Swiss francs and yen, and the rate was also helped by the publication of the RPI. From the start of their day, New York bid actively for dollars and the release of the CPI caused only a momentary pause in the dollar's upward progress as reports began to circulate that Kaufman had become bearish and the US bond market took a dive. With Volcker's remarks publicised widely in the US press, the dollar was marked up throughout the afternoon but the volume of real business seemed rather small. Although sterling was marked down, it suffered less than the other European currencies and the rate touched a low of 1.5697 shortly before the close at 1.5715. Three-month Euro-dollars were unchanged at 8 15/16% and the cost of cover narrowed to 2 1/16%.

The pound made further gains in Europe, rising 7/8% in Germany (3.83¼) and France (10.86¼) and 1% in Switzerland (3.12⅞). The dollar rose another ½% in each of these centres (making 3% over the week) to end at 2.4390, 6.9125 and 1.9905 respectively. Although EMS was stretched throughout the day, only modest intervention was needed to hold the band. By the close, however, the Belgian franc (47.70) had fallen 2⅜% below the guilder (2.6710). The Belgians sold guilders worth $4mn., while the Dutch bought Belgian francs worth $4mn. and deutschemarks worth $18mn. The Italians bought $125mn., the French sold $77mn. (of which $56mn. was in deutschemarks), the Irish sold $13mn. and the Danes bought $12mn. The yen was more or less unchanged at 235.87.

After recovering in New York last night, gold slipped back in rather quiet trading in London today. Fixings were at $490.50 and $485.

Operations:	Market	+	$12mn.
	Sundries	+	6
		+	$18mn.

21st January 1983.
TRS

US BOND AND MONEY MARKETS

Friday, 21st January 1983

Federal Funds

Opening: $8\frac{1}{4}$%
Range: 8% - $8\frac{1}{2}$%
Close: $8\frac{1}{2}$%

US Governments (NY closing bids)

2-year:	$99\frac{1}{2}$	$(-\frac{1}{2})$	$9\frac{1}{2}$%
5-year:	$99\frac{1}{2}$	$(-1\frac{1}{8})$	$10\frac{1}{4}$%
10-year:	$99\frac{1}{8}$	$(-1\frac{3}{8})$	$10\frac{5}{8}$%
30-year:	96	$(-1\frac{5}{8})$	10 13/16%

Euro-dollars (Today's opening London bid)

7-day: $9\frac{1}{8}$%
1-month: 9 3/16%
3-months: 9 5/16%
6-months: $9\frac{1}{2}$%

Federal Reserve Operations:

3-month Treasury Bills	$8\frac{1}{8}$%
3-month US bank CDs	$8\frac{1}{2}$%
Differential	$\frac{3}{8}$%

Indicators

Consumer prices -0.3% in December (c.f. +0.1% in November)
Durable goods orders +12% in December (c.f. +0.1% in November)
M1 +\$6.9bn. (last week's M2 revised down by \$3bn. to \$11bn.)

Comment:

The market weakened during the morning following a report that Kaufman had turned bearish and, again, lack of retail interest. The sharp rise in durable goods orders dealt it a further blow and the final nail in the coffin was the money supply. The market closed at its lows.

24th January 1983.

TRS