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Prime Minister

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I asked for this
report for you.

Treasury Chambers, Parliament Street, SW1P 3AG
01-233 3000

MUS 13/4

13 April 1983

Michael Scholar Esq
10 Downing Street
LONDON SW1

Dear Michael,

You might like an account of developments today in the money markets.

Volcker's remarks on the desirability of lower interest rates in the US got the day off to a helpful start; and the exchange rate reached 82.8 by noon, compared with 82.0 at the close yesterday. Interbank rates were initially little changed, having eased significantly earlier in the week.

As agreed, the Bank in its operations in the money markets has been seeking to facilitate the cut of ½ per cent in base rates which the market has been anticipating over the past few days. Faced with an expected shortage of £300 million, the Bank this morning invited offers of bills for outright purchase. It bought £130 million at rates representing a cut of ¼ per cent in Bands 1-3 and ½ per cent in Band 4. In the afternoon, with the shortage revised up to £350 million, the Bank provided a further £183 million of assistance, mostly in the form of repo's, the rates on which were also cut by ¼ per cent. This provided the market with sufficient liquidity for additional lending facilities not to be activated.

In response to these moves, interbank rates eased by about 1/16. The 3 month interbank rate now stands at about 10½ per cent. Though market comment described the Bank's actions "as an endorsement of the recent falls, paving the way for lower base rates", no change in the latter has yet been announced.

Tomorrow the market is likely to expect a further cut in dealing rates, such as to produce a total fall over two days of around ½ per cent. If the bills offered show that pattern, the Bank

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expects to make a further $\frac{1}{4}$ per cent reduction in its dealing rates in most bands and certainly in the shorter ones. By making two $\frac{1}{4}$ per cent reductions, the Bank feel that the immediate objective of a $\frac{1}{2}$ per cent cut in base rates can be achieved without generating excessive expectations about the timing of the next move.

In the afternoon the higher CGBR announcement had no impact on short term rates; and the initial impact on the gilts market was limited, though prices eased $\frac{1}{8}$ to $\frac{1}{4}$ per cent in late trading. It is possible, however, that there could be some reaction and profit taking in the morning.

The effective exchange rate was unchanged - at 82.8 - at the close.

Yours ever,
J O Kerr
J O KERR

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