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FOREIGN EXCHANGE AND GOLD MARKETSWeek ending 19th January 1983

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The earlier rise in base rates and the Prime Minister's firm statements on Government policy following her return from the Falklands, reassured the market and the pound traded comfortably throughout the week. The ERI rose 0.9 to 82.3. In the absence of a cut in the US discount rate, the dollar continued to move higher, as expectations of a reduction in the German Lombard rate, together with concerns over the forthcoming German elections weakened the deutschemark.

Sterling closed in New York on Wednesday at 1.5785 and, after opening unchanged the following day in London, lost ground, as commercial selling developed from Europe, to touch 1.57 in mid-morning. Sterling began to rise towards noon and the pace of the advance accelerated as the purchase of a large speculative position by a US bank caused widespread covering of short positions; the pound reached 1.5837 at best shortly before the close. On Friday with good two-way business in sterling and a further unwinding of short positions, sterling traded around 1.57½ against a stronger dollar and closed at 1.5805 with the ERI improving by 0.3 to 81.6. Following the Prime Minister's television appearance on Sunday, sterling opened on Monday at 1.58½ and on early demand from Europe, moved up to 1.5890 and an ERI of 82.1. Thereafter sterling traded in a narrow range around 1.59 for the balance of the day. With the dollar strengthening sharply in New York, sterling slipped back to close there at 1.5815 but recovered to just below 1.59 in early business in London on Tuesday. However, when a large commercial selling order from Sweden entered the market and with some professional selling from Germany and Italy, sterling began to give ground, but moved down slowly, despite the dollar strengthening further, to close at 1.57½. On Wednesday sterling traded in a range around 1.57 and closed at 1.5718, with the ERI gaining a further 0.3 as other currencies weakened sharply against the dollar. The pound rose by 1½% against the Swiss franc (3.10), by 1½% against its notional central rate against the ECU (to a discount of 8½%) and by 1½% against the deutschemark (3.79½) and French franc (10.75½). Three-month Euro-dollar rose by 1/16% to 8 13/16% and sterling's forward discount narrowed by ½% to 2½%.

Hopes of a reduction, possibly of 1%, in the German Lombard rate, following the ½% reduction by the Dutch on Thursday, and worries that the German elections in March might result in a hung parliament brought the deutschemark under pressure. And with the dollar in demand following the disappointment of market expectations of a ½% reduction in the US discount rate on Friday, the dollar strengthened sharply, gaining 2½% against the deutschemark (2.4140) and French franc (6.8440), 2% against the yen (234.67) and 1½% against the Swiss franc (1.9727). EMS had a quiet week although with the band remaining almost fully stretched at 2 3/16% throughout between the guilder at the top and the Belgian franc and Irish punt at the bottom, regular intervention to support the weak currencies was required. The Irish sold \$200mn., the Belgians \$150mn. (in guilders) and the Dutch bought \$80mn. (of which \$30mn. was in Belgian francs). The lira moved back within the narrow band, with the Bank of Italy buying \$210mn.

Gold strengthened in New York on Wednesday and fixed on Thursday at \$491. With good institutional interest from Europe, the price made several unsuccessful attempts to hold the \$500 level, before closing the week at \$495.50.

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