Financial review

Introduction

The review describes developments in various markets, mainly during the period February to April.

In these three months, there was a marked turn-round in sentiment, and financial confidence weakened. This weakening contrasted with the distinct signs of revival which became apparent in the real economy. Concern grew over the difficulties actual and potential facing domestic monetary policy, and, with sterling weakening as the dollar recovered and US interest rates rose, there were widespread fears that interest rates in London would have to rise.

In the latter part of the period, interest rates did rise sharply. The Bank of England's minimum lending rate rose in stages, by 2½% to 9%, in April and early May. Yields rose and turnover dropped in the gilt-edged market, and sales of stock by the authorities in the March quarter were only a little over half what they had been in the previous three months. Sterling's effective exchange rate index stood at 61.4 at the end of April compared with 66.5 at the end of January.

The review concludes with the usual accounts of international banking and the euro-currency markets (page 177), oil money movements (page 179) and the commodity markets (page 179).

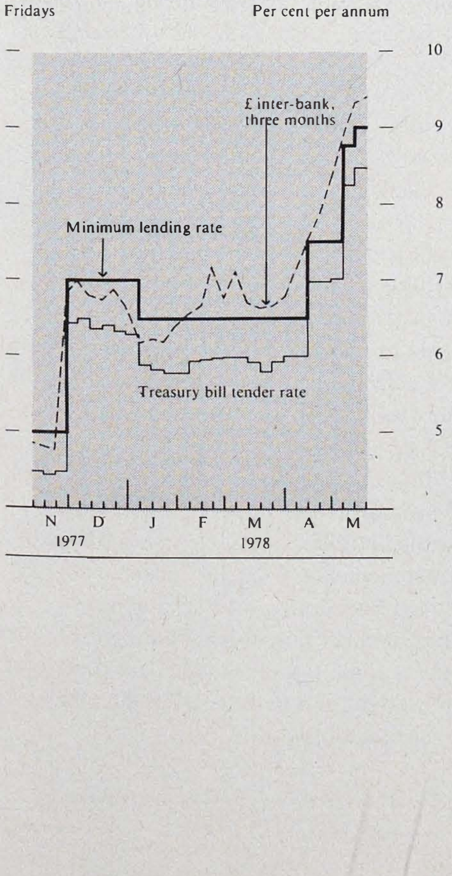
The money market

Summary

Unease over domestic monetary conditions and increasing pressure on sterling brought about a general rise in money-market rates towards the end of the period under review. The Bank of England's minimum lending rate was raised from 6½% to 7½% on 11th April: the Chancellor of the Exchequer announced the increase in his Budget statement, explaining that sterling short-term interest rates were 'on the low side, both in relation to controlling the domestic money supply and by comparison with United States and euro-dollar rates, given recent developments in the exchange markets'.[1] Continued uncertainty about both domestic and external monetary developments led to further increases in minimum lending rate, to 8¾% after the tender on 5th May, and to 9% the following week.[2]

Short-term interest rates in London

Rates rose quite sharply during April and May.



Details of developments during February to April

In January, with sterling strengthening and with financial confidence continuing to run fairly high, the Bank had been leaning against pressure for a further fall in rates (see the March *Bulletin*, page 23). In February, however, there was a change in market sentiment, first because of concern as to whether the Government's pay guidelines would continue to be observed, later because of disappointing trade and money supply figures and some easing of sterling in foreign exchange markets. The discount houses bid less aggressively for Treasury bills at the weekly tender, and the average rate of discount gradually increased. Although money was short on most days, conditions in the market were less tight than in January. The Bank gave assistance as necessary by purchasing Treasury and local authority bills, and without resorting to lending at minimum lending rate; this kept down the discount houses' average cost of money and thus helped to resist the tendency for interest rates to rise.

There was some recovery of confidence in the first half of March, largely because the banking figures suggested that the growth in the money supply had slackened: there was increased competition for Treasury bills at the tender and the average rate of discount fell back. Later

[1] Hansard 11th April 1978. Col. 1192.
[2] See also below, page 173

in the month, however, as sterling declined further, fears of a rise in interest rates again came to the fore: the tender rate finished the month more or less where it had begun and a gap between short-term and longer-term money-market rates, which had begun to appear in February, again became a feature. It was clear that the market was expecting a rise in Treasury bill rates before long. The Bank continued to relieve shortages in the market, principally in the normal way by the purchase of bills.[1]

On 11th April, minimum lending rate was raised from $6\frac{1}{2}$% to $7\frac{1}{2}$%, as described above. The normal formula was suspended until such time as the Treasury bill rate should come into line;[2] this happened on the following Friday and the formula therefore became operative again.

Despite this rise in minimum lending rate, the market remained nervous after the Budget, partly because of concern about the high projected public sector borrowing requirement for 1978/79, which seemed to require substantial sales of gilt-edged stocks if the money supply were to be kept within the target range; and partly also because of the continued pressure on sterling and further signs of an upturn in interest rates in the United States. A general increase in bank base rates by 1% to $7\frac{1}{2}$%, announced on 19th April,[3] steadied the market for a short period but expectations of a further rise in interest rates quickly returned, with even greater intensity than before. Inter-bank, certificate of deposit and other rates began to indicate a rise in minimum lending rate to between $8\frac{1}{2}$% and 9%. For a while the Bank attempted to moderate these pressures by their tactics in the money market, but on 4th May the Bank lent to a number of discount houses for a week at minimum lending rate, making it clear that they would not seek to prevent the restoration of a more normal relationship between domestic money rates generally and the Treasury bill and minimum lending rates. At the tender on the following day, minimum lending rate moved up to $8\frac{3}{4}$%; and it rose further to 9% at the tender on the 12th.[4]

During April, day-to-day conditions in the market were mixed: the Bank continued to help by buying bills, sometimes for resale, and, as in February and March, the occasional surplus was relieved by the sale of Treasury bills.

Reserve assets and eligible liabilities

A feature of the period was the emergence of a two-tier interest-rate structure, particularly around the banks' mid-month make-up days, with secured loans by banks to discount houses being made at rates significantly lower than inter-bank loans. This seems to have been because the shortage of Treasury bills mentioned earlier created a shortage of reserve assets, and banks needed to increase their call money with the discount market to keep their reserve ratios above the minimum $12\frac{1}{2}$%.[5] Much of the money was effectively returned to the banks by the discount houses through the inter-bank or certificate of deposit markets, thus increasing eligible liabilities as well as reserve assets. (Such transactions would have had no direct effect on sterling M_3, from which transactions within the banking system are excluded.) To discourage banks from increasing their eligible liabilities in an attempt to forestall any future reintroduction of the supplementary special deposits scheme, the Government made it clear, in a written reply to a Parliamentary question, that there was no immediate intention of reactivating the scheme, but that if this were done at some future date the base period for interest-bearing eligible liabilities might be a period earlier than that immediately preceding the announcement.[6]

[1] The Bank from time to time, at the end of February and subsequently, also gave assistance by purchasing Treasury, local authority and commercial bills from the discount houses for subsequent resale to them at fixed later dates. Such transactions, which had been entered into by the Bank on a number of occasions in earlier years, were intended to relieve a shortage of Treasury bills in the market, which had developed as a result of the Government's reduced need for short-term finance because of heavy receipts of tax in January and February.

[2] See the additional notes to Table 9 in the statistical annex.

[3] Deposit rates were also raised by 1%, to 4%.

[4] In the second week of May, base rates rose to 9% and deposit rates to 6%.

[5] See the additional notes to Table 3 in the statistical annex.

[6] Hansard 21st February 1978, Col.617.

New financing instruments

In a notice to banks on 22nd March, the Bank stated that, provided exchange control requirements were met, they would not object to the issue by banks of variable rate sterling certificates of deposit and would not normally object to the issue by banks of fixed or variable rate medium or long-term sterling securities, with a term to maturity of over five years. Issues of the latter securities would not be classified as eligible liabilities and would not therefore be subject to reserve asset ratio, special deposit or supplementary special deposit requirements; however, the Bank reserved the right for the future to request that banks should refrain for the time being from further issues, if this became necessary for the purpose of monetary control.

Minimum lending rate

On Thursday, 25th May, the Bank issued the following press notice:

> On the proposal of the Bank of England, the Chancellor of the Exchequer has agreed that the arrangements for determining minimum lending rate described in the Bank's notice of 9th October 1972 should be terminated. For the future the level of minimum lending rate will be determined by administrative decision and any change will normally be announced to the market at 12.30 p.m. on a Thursday. It has been decided that minimum lending rate shall remain at its present level of 9% until further notice. No further announcement will be made until it is decided to change the rate. It is intended that minimum lending rate will continue to be adjusted flexibly, taking account of market developments.

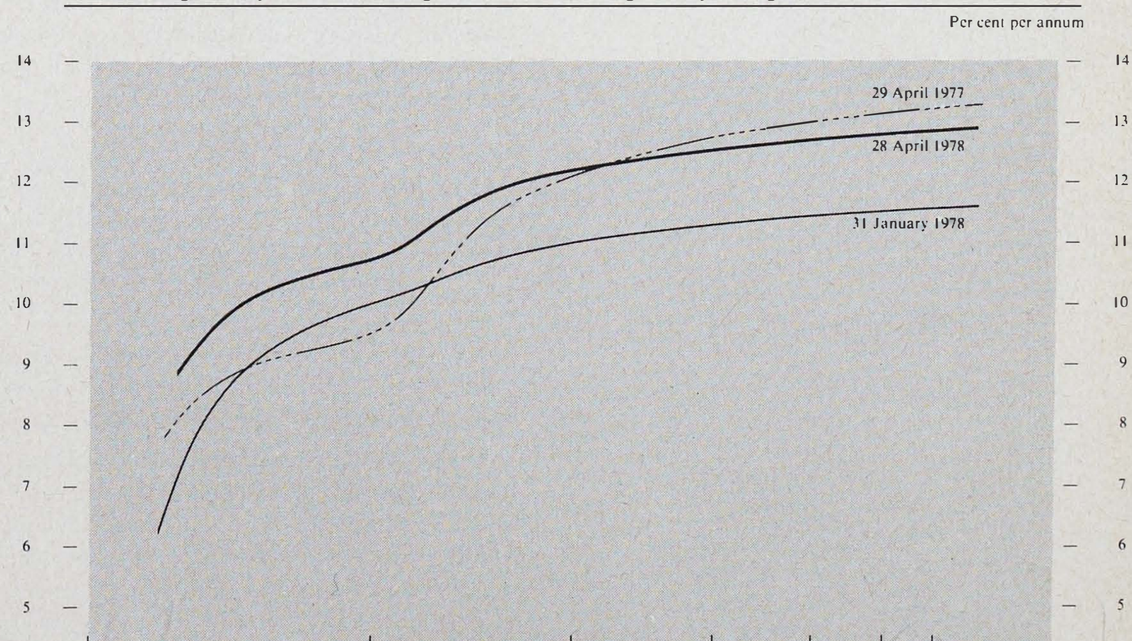
Capital markets

The gilt-edged market

In the gilt-edged market, yields rose during the period, while turnover dropped (in both March and April, to only a little over half last year's peak figure in September).

Time/yield curves of British government stocks[a]

Yields rose generally, but at the long end were not as high as a year ago.

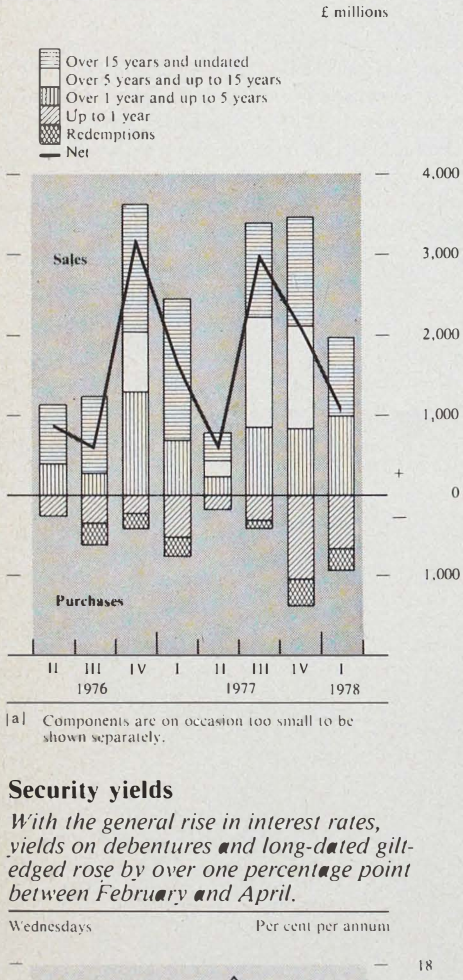


[a] The lines measure the nominal rate of interest which a stock at each maturity should bear if issued at par. The curve runs from the shortest-dated stock with a life of more than one year to the longest-dated stock. A revision to the construction of these curves was described in the June 1976 *Bulletin* (page 212). The relevant computer program is available from the Economic Intelligence Department of the Bank at the address given on the reverse of the contents page.

The market was affected at the beginning of February by financial uncertainties and worries about industrial wage claims, but the miners' acceptance of a pay settlement within the Government's guidelines improved sentiment, and substantial sales were made of the long-dated

Official transactions in gilt-edged stocks by maturity [a]

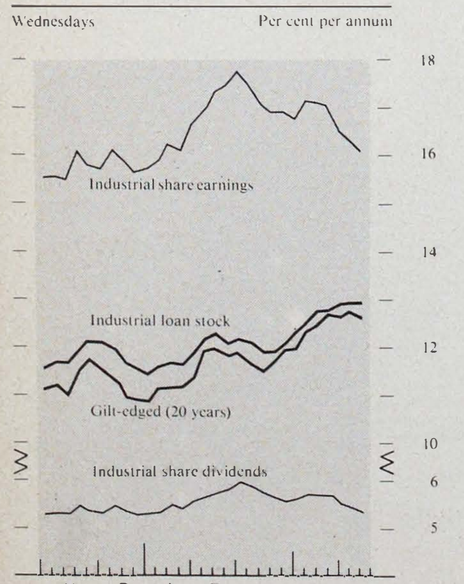
During the March quarter, the authorities sold over £1,000 million net of stock, considerably less than in the previous two quarters.



[a] Components are on occasion too small to be shown separately.

Security yields

With the general rise in interest rates, yields on debentures and long-dated gilt-edged rose by over one percentage point between February and April.



tap stock, 10¼% Exchequer Stock 1995 (which had been issued on 12th January, but of which little had previously been sold). There was some uneasiness ahead of the mid-February announcements of the trade and money supply figures for January, and the size of the trade deficit when it finally came to be announced caused a further set-back, but by 24th February the market had steadied sufficiently for the Bank to announce an issue of £600 million 8¾% Exchequer Stock 1983 at £96.50 per cent. [1]

The issue was made on 2nd March and at first only moderate amounts were sold, but more encouraging financial and external trade statistics during the first half of March strengthened the market and led to large sales of both tap stocks. In the second half of the month and in April, however, the decline in the exchange rate and renewed anxieties about the money supply led to fears of rises in interest rates which undermined the market. After the Budget, in particular, there was uneasiness about the size of the funding programme facing the authorities. There was some steadying in the third week of April, when the raising of banks' base rates was taken as a gesture of confidence, and there was substantial demand for stock: the 1983 stock was exhausted on 19th April (the day of the banks' announcements) and the 1995 stock the day after, and a new long-dated stock, £800 million 12% Exchequer Stock 1998 at £96.00 per cent, was announced on the 21st.[2] By the day of issue (the 27th), however, the market had moved lower as sterling weakened, and initial sales of the new stock were very small.[3]

During the March quarter, the authorities sold £1,050 million net of stock.[4] Net sales of long-dated stocks amounted to £980 million, and of stocks within one to five years of maturity to £1,000 million. One stock matured during the quarter — 9% Treasury Stock 1978 on 15th March, with only £245 million in market hands; [5] the major portion of the £675 million net of stocks within one year of maturity which was bought by the authorities during the quarter represented purchases of this stock in advance of its redemption.

Total net sales of stock by the authorities in the financial year 1977/78 as a whole amounted to £6,685 million, after £6,290 million in the preceding financial year. National savings during 1977/78 brought in £1,165 million, compared with just under £1,000 million in the preceding year and £500 million the year before that.

Other markets

Local authorities were raising little new money by stock and bond issues at the end of their financial year, and there were net redemptions of such issues of £40 million during February to April. Over the financial year as a whole, however, local authorities raised nearly £180 million net by these issues.

Turnover in the debenture market was a little lower in February to April, and yields rose during the period. Redemptions by companies again exceeded new money raised by way of loan capital and preference shares.

The equity market was affected by economic and financial uncertainties and the FT-Actuaries industrial (500) share price index, which stood at 220 at the end of January, fell to 205 in early March, after the adverse external trade figures announced in February and some disappointing company results; however, it recovered to finish April slightly up over the period, at 225. Trading was very thin and turnover fell further after its sharp decline in the preceding three months.

New money raised by issues of equity capital fell to about £115 million (nearly all in February), from around £215 million in November to January.

[1] As with several recent issues, a further £200 million was reserved for the National Debt Commissioners, for public funds under their management.

[2] £30 was payable on application, £35 on 15th May and £31 on 7th June.

[3] A new short-dated issue, a second tranche of £800 million 9¼% Exchequer Stock 1982 at £94.75 per cent, was announced on 12th May.

[4] The figures are cash values and for partly-paid stocks, therefore, incorporate only instalments actually paid.

[5] The outstanding amounts of British Transport 4% Stock 1972/77, totalling over £10 million, were also presented for redemption during the period (see the March *Bulletin*, page 24).

A new feature in the period was the opening of a London market in traded options. Dealings in traded options began on the stock exchange on 21st April: call options on a limited number of underlying UK securities are listed.[1]

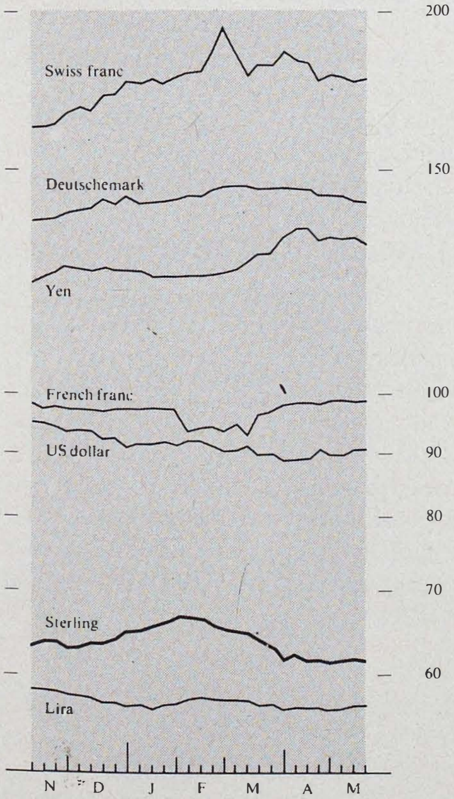
Net sales of unit trust units again rose sharply, to £97 million, or £44 million more than in the previous three months. There were particularly heavy sales in March and April, reflecting investment in specialised American funds.

The Council for the Securities Industry
The Bank announced on 30th March that general agreement had been reached for the setting-up of a new self-regulatory body for the securities industry, to be called the Council for the Securities Industry (CSI). The Council is under the chairmanship of Mr Patrick Neill, QC, and its work will be built around the existing regulatory machinery of the stock exchange and of the City Panel on Take-overs and Mergers. Details of its constitution, objectives and basis of operation are given on page 250.

Foreign exchange and gold markets

Indices of effective exchange rates
Sterling weakened during the period; the US dollar became steadier in April.

Logarithmic scale
Fridays
21 December 1971 = 100



Summary
During February to April, the US dollar remained the centre of attention in foreign exchange markets. Until early April its weakness continued to make for very nervous and at times disorderly markets, despite heavy intervention by the authorities in a number of centres. From mid-April a recovery took place. Sterling also weakened markedly over the period, and the effective rate index fell from 66.5 at the end of January to 61.4 at the end of April — somewhat below its level before 31st October 1977, when the authorities ended their policy of intervening to prevent a rise in effective terms. At times large amounts of sterling were on offer, and official intervention was substantial; it was designed to moderate the effect on the rate of the re-export of some of the more volatile inflows of last year. There was also some intervention in the short-dated swap markets on occasion, to increase the potential cost of running short speculative positions against sterling.

Sterling
During February, disappointing trade and money supply figures, and a reassessment by the market of its earlier euphoric view of North Sea oil prospects, caused sterling to weaken somewhat against the dollar, which was itself falling against the yen and most European currencies. The sterling/dollar rate eased from \$1.9481 on 1st February to \$1.9365 at the end of the month, although it touched \$1.9585 on 20th February when the dollar was particularly weak. The effective rate index fell from 66.5 to 65.2.

The rate steadied in the early part of March and the trade and money supply figures published in March were encouraging, but doubts about sterling in the medium term, and nervousness ahead of the Budget, gave rise to considerable selling pressure in the second half of the month. The sterling/dollar rate weakened further, passing through \$1.90 on 21st March and reaching \$1.8680 in thin markets just before Easter. Further selling developed over the end of the month following the publication of some gloomy reports on the prospects for the UK economy, and substantial official support was given to maintain orderly conditions.

The sterling/dollar rate steadied again on 5th April, closing at \$1.8735 (effective rate index: 62.2), and sterling traded quietly until shortly after the Budget on the 11th. Rumours of further tax reductions in the summer and market uncertainty about the financing of the public sector borrowing

[1] An option may be a call option (an entitlement to buy shares at a fixed price at any time before the expiry date of the contract) or a put option (an entitlement to sell). Only call options are being traded on the new London market. A traded options market is one in which a clearing organisation exists to register and guarantee contracts for buying or selling options. The contracts are on standardised terms so far as the underlying security, the price at which the option may be exercised and the expiry date of the contract are concerned; the price at which the options change hands is determined by supply and demand.

requirement then led to renewed selling pressure, which became strong as the dollar began to grow firmer and disappointing UK trade figures were announced. Appreciable official support was again provided, enabling some reversal of last year's volatile inflows into sterling to take place as the dollar showed signs of recovery. Sterling ended the month at $1.8267, with an effective rate index of 61.4. But such was the strengthening of the dollar against the yen, the deutschemark and other major European currencies in April that sterling, too, had made up some of the ground it lost against them in February and March.

Over the three months, the reserves fell by $3,830 million, after net repayments of public sector borrowing under the exchange cover scheme of $726 million and the repayment of $943 million to the International Monetary Fund in April ahead of time.

The US dollar

Having ended January at DM 2.1062, the dollar enjoyed a brief period of stability in early February before the market's fears about inadequate progress on the US energy import bill, compounded by the US miners' strike, brought a severe weakening in the second half of the month: it reached DM 2.0280 by the 20th.

The weakness continued into March, and at times market conditions were disorderly despite substantial official support in some centres. The rate dipped briefly below DM 2.00 at the beginning of the month, and demand for the yen became very strong. The dollar recovered a little on the later news of discussions between the governments of the United States and Western Germany. A joint communiqué was issued on 13th March, announcing that swap facilities between the Federal Reserve and the Deutsche Bundesbank were to be doubled to $4 billion, that the US Treasury was prepared to sell SDR 600 million to the Bundesbank for deutschemarks, and that the United States would draw on its reserve position with the IMF to buy additional foreign exchange if necessary. This, however, failed to meet expectations in the market, and the dollar fell back again. Following the announcement of a record monthly US trade deficit of $4.5 billion on 31st March, it dipped briefly below DM 2.00 once more.

In early April some stability was restored. President Carter's statement on the 11th about anti-inflation policies evidently did not entirely satisfy the market's previous hopes, but the dollar nevertheless began to recover, and strengthened markedly on the announcement on the 19th of official US gold sales, reaching DM 2.0788 on the 20th. Thereafter rising US interest rates, news of the proposed deregulation of the price of natural gas in the United States, and further commitments undertaken by the US authorities in the battle against inflation helped to consolidate the dollar's recovery. It ended April a little weaker on profit-taking at DM 2.0688, but regained most of this ground in early May.

Other currencies

The margins between the 'snake' currencies came under some pressure again in early February before the Norwegian krone was devalued by 8% over the week-end of 11th–12th February, but these currencies then remained comfortably within the limits for the rest of the period. For most of the time the deutschemark was at the top of the 'snake', and the Danish krone spent the longest period at the bottom, although the other three currencies all took that position at various times. Intervention in 'snake' currencies was light, except for purchases made to repay currencies borrowed for intervention in earlier periods. The mid-point of the 'snake' rose from a premium of $23\frac{1}{16}$% against the dollar at the end of January and reached $29\frac{3}{16}$% on 3rd April before settling back to $25\frac{13}{16}$% at the end of the month.

The Japanese yen was in extremely strong demand in the second half of February and in March. By 28th March it had appreciated by $7\frac{1}{2}$% against the dollar since the beginning of February, despite very substantial intervention. When the Bank of Japan then stopped intervening for domestic monetary reasons, the yen at first continued to appreciate, but it fell back as the dollar strengthened, and ended April close to the level at which intervention ceased.

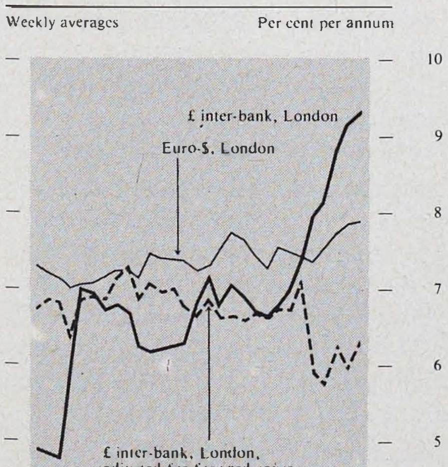
As in previous periods, the Swiss franc's movements were especially volatile. It stood at SW.Fr.1.9850 against the dollar at the beginning of February and had appreciated against that currency by no less than 11% by the 24th, when it was announced that controls on inflows would be tightened. Nearly all this appreciation was reversed in early March, but the rate strengthened once more towards the end of the month before falling back to Sw.Fr.1.9320 at the end of April.

The French franc came under strong pressure before the French elections, reaching a low point of F. Fr.4.9525 against the dollar on 6th February, but it recovered strongly when the results were known and ended April at F.Fr.4.6100, despite the recovery of the dollar. The French authorities gave substantial support to the franc in February, but both they and the Italian authorities bought dollars for their reserves in March and April.

The Canadian dollar remained weak for most of the period. It fell fairly steadily from US$0.9034 at the beginning of February to reach a low point of US$0.8669 on 14th April. It then shared in the US dollar's recovery, and was helped by news that the Canadian authorities were arranging further foreign borrowing. It ended the period at US$0.8824.

UK and US three-month interest rates

With the recovery of the dollar, the covered differential against sterling widened in April; the uncovered differential, however, moved in favour of sterling as interest rates in London rose.



Interest rates and differentials

The three-month sterling inter-bank rate rose from $6\frac{7}{16}$% to $6\frac{15}{16}$% in February, but fell back to around $6\frac{3}{4}$% during March. It became somewhat firmer in early April, rose sharply to $8\frac{1}{8}$% following the rise in minimum lending rate on the 11th, and finished the month at $8\frac{7}{16}$%. The upward movement continued into May and the rate reached $9\frac{1}{8}$% after the two further increases in minimum lending rate on 5th and 12th May. The three months' euro-dollar rate rose from $7\frac{5}{16}$% to $7\frac{1}{2}$% during February and remained around that level for most of March and April, before firming, as US short-term interest rates rose, to end April at $7\frac{11}{16}$% and to reach 8% in mid-May. The uncovered differential, which had favoured the dollar for most of the period, moved to the advantage of sterling after the rise in minimum lending rate in April and reached $1\frac{1}{2}$% in mid-May. Three months' forward dollars moved to a premium early in February as sterling weakened, and the premium was maintained throughout the period, except for a few days of particular dollar weakness in mid-March. The premium was generally well below $\frac{1}{2}$% until mid-April, but then rose sharply to reach $2\frac{3}{4}$% before the end of April and over 3% after the first few days of May. The covered differential against sterling, which was about $\frac{1}{2}$% at the beginning of February, widened slightly during March before jumping to over $1\frac{1}{2}$% near the end of April.

Gold

The gold price became firmer during February, largely because of the weakness of the dollar, and reached $190 per fine ounce (the highest since the record of $197.50 in December 1974) on 8th March. It then fell back as the market came round to the view that gold had been overbought and became nervous on rumours of gold sales by the US authorities. Sentiment deteriorated further when modest selling was followed by the announcement of Indian gold sales, and the price stood at $181.60 at the end of March. As the dollar strengthened in the second half of April the gold price weakened further, and fell to $168.55 on the 20th following the announcement of US gold sales. It ended the month at $170.85.

International banking and euro-currency markets

Figures published by the Bank for International Settlements show that international bank activity[1] expanded very rapidly in the fourth quarter

[1] Defined as the domestic and foreign currency business of banks in the Group of Ten countries and Switzerland and of branches of US banks in certain off-shore centres — the widest available measure.

of 1977. The gross external assets of reporting banks rose by $65 billion during the quarter. This, however, overstates the underlying increase for two reasons. First, the purely statistical effects of changes in the value of the US dollar account for about $15 billion of the increase. Secondly, some $25 billion was attributable to the seasonal build-up of end-year positions between banks within the area. Thus, new international bank credit to non-bank residents of the reporting area and to countries outside the area probably amounted to some $25 billion during the quarter, compared with an average of about $15 billion for the first three quarters of the year. Over 1977 as a whole, some $70 billion of new international bank credit was made available.

Of the recorded increase in gross assets in the fourth quarter, $47 billion was within the reporting area itself. The remaining $18 billion was well spread amongst other geographical areas, all of which redeposited large proportions of the funds borrowed. Developed countries outside the Group of Ten and Switzerland borrowed $\$5\frac{3}{4}$ billion and deposited $\$4\frac{1}{2}$ billion; non-oil developing countries, especially Brazil and Argentina, took $\$5\frac{3}{4}$ billion and this group as a whole deposited $\$4\frac{3}{4}$ billion; and the oil-exporting countries borrowed $\$3\frac{1}{2}$ billion and deposited $\$4\frac{1}{2}$ billion (or $3 billion after adjustment for currency valuation changes, the deposits being largely in currencies other than US dollars).

Over 1977 as a whole, developed countries outside the Group of Ten and Switzerland were the largest users of funds, taking $\$9\frac{1}{2}$ billion net. Eastern Europe also received nearly $4 billion net. Non-oil developing countries, on the other hand, in contrast with previous years, deposited a net $\$1\frac{1}{2}$ billion. The net deposits of the oil-exporting countries amounted to only just over $2 billion.

Only limited data are yet available for the first quarter of 1978. The volume of newly-announced medium-term euro-currency bank credits (which show up in the BIS figures only when taken up and only to the extent that they are not replacing maturing debt) amounted to nearly $12 billion, much the same as in the previous three months. During the quarter the average size of announced medium-term credits rose and the average maturity lengthened; the downward pressure on spreads continued.[1] Completed new foreign and international bond issues fell slightly to $\$7\frac{1}{4}$ billion, after $\$7\frac{3}{4}$ billion in the fourth quarter of 1977.

Provisional figures suggest that the size of the London euro-currency market, measured by the total foreign currency liabilities of reporting institutions, increased by some $\$5\frac{1}{2}$ billion in the first quarter of 1978, after $\$12\frac{1}{2}$ billion in the last quarter of 1977. However, after allowing for the statistical effects of currency valuation changes and the unwinding in the first quarter of end-year positions built up in the previous three months, the underlying growth of the market in the first quarter was probably only slightly slower than in the fourth.

The regular analysis of external positions by country or area was not available at the time of going to press.

A quarterly maturity analysis of the foreign currency liabilities and assets of reporting institutions was completed as at 15th February (see Table 21 in the statistical annex). Gross foreign currency liabilities rose by some $\$7\frac{1}{4}$ billion, although after adjustment for currency valuation changes the real rise was probably about $4 billion. Net liabilities up to one year dipped slightly and there was some lengthening of maturities: thus, net borrowing at less than eight days fell by $\$\frac{1}{2}$ billion, and at eight days to less than three months by $\$1\frac{1}{2}$ billion, while, in contrast, net borrowing at three months to less than one year rose by nearly $2 billion, from 14% to 18% of the up to one-year category. This overall lengthening of maturities was probably associated with the steepening of the euro-dollar yield curve, which may have encouraged depositors to place funds at longer term. In addition, the switching of short-term currency deposits into sterling, which partly accounted for a shortening of

[1] The 'spread' is the amount by which the interest rate is to exceed LIBOR.

UK banks' liabilities and assets by customer[a]

The underlying growth of the London euro-currency market was probably slightly slower in the first quarter of 1978 than in the fourth quarter of 1977 (see text).

$ billions

	1977				1978
	31 Mar.	30 June	30 Sept.	31 Dec.	31 Mar. [b]
Foreign currency liabilities of UK banks to:					
Other UK banks	48.0	48.4	50.1	51.2	53.5
Other UK residents	6.3	6.8	6.6	7.1	7.8
Overseas central monetary institutions	36.5	37.0	38.9	41.0	149.8
Other banks overseas	93.8	97.3	100.7	108.6	
Other non-residents	20.7	22.2	23.5	24.5	26.4
Other liabilities [c]	1.3	1.6	1.5	1.5	1.9
Total liabilities	**206.6**	**213.3**	**221.3**	**233.9**	**239.4**
Foreign currency assets of UK banks with:					
Other UK banks	47.6	48.5	51.3	53.2	55.7
Other UK residents	18.5	18.4	18.3	19.0	19.4
Banks overseas	102.3	107.1	110.2	116.6	117.7
Other non-residents	36.7	38.3	39.8	43.3	44.6
Other assets [c]	2.2	2.4	2.5	2.8	2.9
Total assets	**207.3**	**214.7**	**222.1**	**234.9**	**240.3**

[a] Figures differ from those in Table 6 in the statistical annex (see additional notes to Tables 20 and 21).

[b] Provisional.

[c] Mainly capital and other internal funds denominated in foreign currencies.

Maturity structure of UK banks' net foreign currency position

In the up to one-year category, there was some lengthening of net maturities between mid-November 1977 and mid-February 1978.

$ billions

Net liabilities −/net assets +

	1977	1978
	mid-Nov.	mid-Feb.
Less than 8 days [a]	−13.6	−13.0
	− 9.9	*− 9.5*
8 days to less than 3 months	−20.1	−18.5
3 months to less than 1 year	− 5.3	− 7.2
Net borrowing up to 1 year	−39.0	−38.7
Net lending at 1 year and over	+38.3	+38.8
	− 0.7	+ 0.1

[a] Figures in *italics* include all holdings of London dollar certificates of deposit, regardless of maturity, as these are immediately realisable assets for the holding bank.

Estimated oil revenues of exporting countries

Oil revenues in the first quarter were marginally lower than in the fourth quarter of 1977.

$ billions

1976	1977				1978
Year	Year	1st half	3rd qtr	4th qtr	1st qtr
113.2	129.1	64.5	32.3	32.3	32.1

Estimated deployment of oil exporters' surpluses [a]

The total surplus in the first quarter was significantly lower than in the fourth quarter of 1977.

$ billions

	1976	1977				1978
	Year	Year	1st half	3rd qtr	4th qtr	1st qtr [b]
United Kingdom						
British government stocks	0.2	—	−0.2	0.1	0.1	—
Treasury bills	−1.2	−0.2	−0.1	0.2	−0.3	—
Sterling deposits	−1.4	0.3	0.5	−0.2	—	0.2
Other sterling investments [c]	0.5	0.4	0.2	0.1	0.1	—
British government foreign currency bonds	—	0.2	0.2	—	—	—
Foreign currency deposits	5.6	3.4	3.4	0.5	−0.5	1.0
Other foreign currency borrowing	0.8	—	—	—	—	—
	4.5	4.1	4.0	0.7	−0.6	1.2
United States						
Treasury bonds and notes	4.2	4.3	2.0	0.7	1.6	−0.1
Treasury bills	−1.0	−0.8	0.5	0.2	−1.5	0.3
Bank deposits	1.6	0.4	—	0.1	0.3	0.5
Other [c]	7.2	5.3	2.9	1.3	1.1	1.1
	12.0	9.2	5.4	2.3	1.5	1.8
Other countries						
Bank deposits	7.0	8.5	5.5	0.5	2.5	1.5
Special bilateral facilities and other investments [c] [d]	10.3	11.7	6.1	2.6	3.0	0.9
	17.3	20.2	11.6	3.1	5.5	2.4
International organisations	2.0	0.3	0.2	0.1	—	—
Total	**35.8**	**33.8**	**21.2**	**6.2**	**6.4**	**5.4**

[a] This table excludes liabilities arising from net borrowing and inward direct investment and also, on the assets side, changes in credit given for oil exports. A table reconciling the figures with the estimates for current account surpluses is given below.

[b] Provisional.

[c] Includes holdings of equities, property, etc.

[d] Includes loans to less developed countries.

Reconciliation between 'deployment' table and current account surpluses

$ billions

	1975	1976	1977 [a]
Current account surpluses	31	36	36
Net borrowing	3	7	7
Oil sector capital transactions [b]	1	−6	−2
Cash surpluses available for investment	35	37	41
Deployment table estimates	35	36	34
Errors and omissions	—	1	7

[a] The figures for 1977 are likely to be revised as fuller information becomes available.

[b] Includes credit given for oil exports and oil companies' investment/disinvestment in oil-exporting countries.

maturities between mid-August and mid-November 1977 (see the March *Bulletin,* page 28), was reversed in the period under review.

A maturity analysis of banks' issues and holdings of US certificates of deposit (and small amounts of other negotiable paper) is again included in the additional notes to Table 21 in the annex. In the period to mid-February, issues fell by some $500 million; the fall was mainly concentrated in the shorter maturities and was more than accounted for by lower issues by the American banks.

All central banks in the BIS reporting area [1] are now conducting half-yearly surveys of the external positions of banks in their territories and submitting aggregated data to the BIS, which will consolidate and publish the results in due course. The contribution of banks in the United Kingdom to the end-December 1977 analysis appears as Table 22 in the statistical annex in this issue.

Oil money movements

Total estimated oil revenues of oil-exporting countries fell very slightly in the first quarter, a rise in the volume of exports in November and December being offset by some shading of prices. The higher demand for oil was due partly to higher consumption, accentuated by the particularly severe US winter, and partly to stockpiling in anticipation of a possible price rise. In January, the volume of exports fell back sharply, reflecting a large reduction in oil stocks in importing countries and the impact of rising non-OPEC production, particularly in the North Sea and Alaska.

The volume of oil exports in February and March was at a rate only slightly above the depressed level recorded in January and revenues in the second quarter are likely to fall further.

Oil exporters' net borrowings [2] remained high in the first quarter, but with the marginal fall in revenues and a further increase in imports of goods and services, the cash surplus available for investment abroad, for government loans and for additions to financial reserves was markedly lower than in the fourth quarter. With revenues likely to be lower in the second quarter, the outlook is for a further fall in the cash surplus.

Sterling holdings were once again little changed. However, foreign currency deposits with UK banks rose after falling in the fourth quarter.

Investment in the United States was higher than in the previous quarter and accounted for a third of the total cash surplus, a higher proportion than in most of 1977.

Bank deposits in other countries continued to rise, but less strongly than in the previous quarter. The diversification into currencies other than the US dollar which had been of some significance in the third quarter was less noticeable in the fourth, and it seems likely that little further diversification occurred in the first quarter.

Commodity markets

Trading remained generally quiet during February to April. Turnover on the principal London futures markets was little changed from the previous three months and substantially lower than in the corresponding period of 1977; nevertheless, some prices moved quite sharply, in response to exchange rate movements as well as to world market conditions. The depreciation of sterling was largely responsible for a rise in commodity prices of 11%.[3]

In the terminal markets, there was a large increase in cocoa prices after the lowest point for eighteen months was reached in mid-February; the rise was due to revised estimates of both crops and consumption. Soyabean meal prices also rose sharply, when it became clear that the Brazilian crop would be smaller than had previously been estimated.

[1] For this purpose, this includes the Group of Ten countries, Austria, Denmark, Republic of Ireland and Switzerland.

[2] See footnote [a] to the second table.

[3] As measured by *The Economist* sterling index.

These increases were partly offset by a renewed fall in coffee prices after three months of relative stability. Sugar was again depressed by the continuing world surplus.

Price movements on the London Metal Exchange were also mixed. Copper fell at the end of February to its lowest for two years, but then recovered (partly because of announcements by the major exporting countries of their intention to restrict supplies), so that by mid-April cash copper was at its highest during the period; LME stocks of copper, which had reached a peak in mid-January, declined throughout February to April. Zinc prices also rose; both tin and lead, on the other hand, remained weak, with tin being affected by uncertainty over the prospect of releases from the US stockpile.