Financial review

The main points in financial markets in the three months to mid-May:

- *There were severe cash shortages in the money markets earlier in the period, but these conditions subsequently eased, largely because of the temporary effects of the Civil Service dispute.*
- *The authorities maintained the momentum of the funding programme in the first three months of the new target period for sterling M_3, with heavy sales of gilt-edged stocks (including the first index-linked stock) and national savings.*
- *A number of other domestic capital markets showed greater activity. There was a sharp rise—later partially reversed—in equity prices.*
- *In the foreign exchange market, currencies responded mainly to developments in interest rates. Sterling weakened against a generally stronger dollar, but maintained its position against European currencies and in effective terms.*

This review generally covers the calendar months of March and April but, because official actions in the money and gilt-edged markets are tied closely to banking months, the sections on these markets cover the three banking months from 19 February to 20 May.(1)

In addition to the sections commented upon above, the review also contains the usual sections on international banking and the eurocurrency markets, oil money movements, and the commodity markets.

Money markets

There was an acute cash shortage in the money markets in the first half of March and the pattern of interest rate expectations which built up ahead of the Budget made it particularly difficult for the authorities to relieve the pressure. Heavy sales of gilt-edged stocks immediately after the Budget temporarily increased the pressure. But with uncertainty about short-term interest rates largely resolved by the Budget, and with increasing delays to government revenue from mid-March onwards because of the Civil Service dispute, the position then eased considerably. Nevertheless, periods of substantial cash shortage recurred on occasion to the end of April. The banks' minimum reserve asset ratio was set at 8% for nearly all of March and April, but was restored to 10% on 30 April. There were further developments in official techniques for managing the markets.

(1) Unless otherwise stated, all subsequent references are to calendar months.

Management of the market

It became obvious during February that, following a heavy call on 12% Exchequer Convertible Stock 1985 on 27 February and the payment of some £1,300 million of petroleum revenue tax on 2 March, the cash position of the money markets during early March would be very tight. To ease the problem, the Bank announced on 24 February that the banks' minimum reserve asset requirement would be reduced from 10% to 8% of eligible liabilities between 2 and 10 March, thereby releasing assets which could be sold to the Bank.

In the event, the pressure was more severe and lasted longer than had been expected. In part, this was because net government receipts in the first half of March were higher than had been forecast. Also, the Budget stimulated rapid and heavy demand for gilt-edged stocks (see below), causing another very substantial cash drain from the market on 12 March.

The pressure was also more difficult to relieve than might have been expected, mainly because of the pattern of interest rate expectations which formed ahead of the Budget. By the end of February, private sector borrowers had come to expect a large reduction in minimum lending rate (MLR) on 10 March (Budget day) and, until the size of the cut was known, many wished to borrow only short-term money. Thus demand for funds was concentrated at the very short end of the market. Similarly, as commercial bills matured,[1] they were replaced, if at all, by new bills of very short maturity.

These pre-Budget expectations, together with an underlying cash position which was very tight and rather uncertain from day to day, led to very high shorter-term interest rates throughout the period from end-February to 13 March and a pattern of rates which made 'round-tripping',[2] in various forms, profitable (see the section below on interest rates).

During this period, the Bank sought to provide cash by a variety of means to offset the forecast shortages. It bought bills outright every day (mostly eligible bank bills because these formed the bulk of the available supply) and it also bought a large number of bills on a purchase and resale basis (see the section below on developments in techniques). The Bank also lent 'through the discount window' on three occasions when the shortages were clearly the result of the authorities' own actions and were too large to be met by open-market operations alone—2 March (when petroleum revenue tax was paid), 10 March, and 12 March (after heavy gilt sales). On the first two occasions the lending was at MLR, but on the third occasion it was above MLR. In addition, the Bank again reduced the banks' minimum reserve asset ratio, from 10% of eligible liabilities to 8%, for the period 12 March to 30 April.

Conditions eased on 13 March, to the extent that the structure of interest rates returned to a more normal pattern. But in the following week there were three days of heavy shortage and the Bank, in addition to buying bills outright and by purchase and resale agreement, lent through the discount window. On each occasion, the Bank charged a rate above MLR to discourage reliance upon this source of funds. The terms of the Bank's lending were not, however, intended to be heavily penal, in recognition of the uncertainties in the cash position each day generated by the Civil Service dispute.

(1) Many of these bills were in the Bank's hands as a result of earlier open-market operations; their maturity was often a major—although foreseeable—factor behind cash shortages in the market.

(2) Borrowing either by drawing short-term bills or on overdraft and redepositing the money in the inter-bank market.

Thereafter, in the month to mid-April, heavy shortages tended to appear once or twice a week, usually as a result of sales of, or calls on, gilt-edged stocks (as on 27 March and 10 April), the maturity of large amounts of eligible bank bills held by the Bank, and the unwinding of earlier purchase and resale agreements. For similar reasons, moderate shortages appeared most days after Easter until 1 May. But in the following week, with the Bank making significant purchases of gilt-edged stocks close to maturity (see below), conditions were considerably easier; the cash position of the market then tightened again but open-market operations on a modest scale were sufficient to relieve the shortages and to avoid any undue upward pressure on shorter-term interest rates.

From around the middle of March, the cash position was eased significantly on a number of days by the effects of the Civil Service dispute, which began to produce shortfalls in net government receipts. The Government estimated that, because of the dispute, there had been a cumulative shortfall of gross receipts of around £750–1,000 million by end-March; during April, there was a further shortfall of £1,250 million and delay to receipts continued during the first half of May. The effects of the strike were, not surprisingly, difficult to predict and uncertainty in the market was often considerable. On a number of days, a cash surplus appeared unexpectedly in the market towards the end of business, after the Bank had injected funds to meet an apparent shortage.

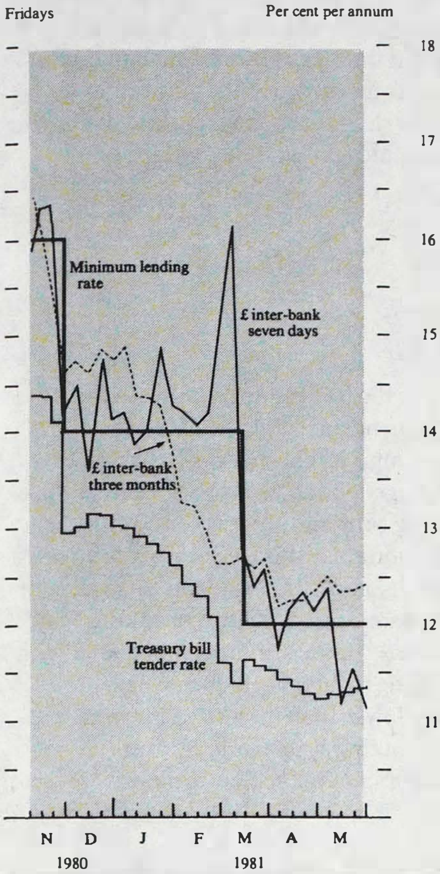
When intervention by the Bank was required, it was again provided, until the end of March, by outright purchases of bills and by purchase and resale agreements, and thereafter by outright purchases only. In this, the Bank was helped by an increase in the supply of longer-term bills, as borrowers returned to a more normal pattern of financing once the Budget had clarified the outlook for interest rates. The Bank was required to absorb cash surpluses on three days early in April by selling Treasury bills overnight; when conditions eased again in the first week of May, the Bank again sold Treasury bills, mostly of eight or nine days' maturity as there seemed no immediate likelihood of renewed cash shortages on a large scale. In general, however, the quantity of Treasury bills in the hands of the market continued to fall during the period under review, and the adverse effects on exchequer financing of the Civil Service dispute were reflected primarily in a net reduction in the Bank's holdings of commercial bills.

Interest rates

By the end of February, interest rates for three months and over had fallen to the point where they fully discounted a fall of two percentage points in MLR. When MLR was actually reduced from 14% to 12% on 10 March, these rates did not fall further; indeed, some rose slightly. They then showed little change until early April, when speculation about an imminent cut in MLR caused further declines—of half a percentage point in the case of three-month rates. When MLR remained unchanged, there was a slight reaction, and rates edged up a little further during the rest of April. The further rise in US rates early in May led to a modest increase in longer-term UK rates and the three-month inter-bank rate ended banking May only marginally lower than it had been at the end of February when MLR was still 14%.

Interest rates at the very short end moved considerably more. From the end of February to around 13 March, they reflected the cash pressure in the money markets, with overnight rates climbing to

Short-term interest rates in London



40% late on 9 March, the seven-day inter-bank rate reaching a peak of around 17% on 2 March, and the one-month rate staying at around 13½% for two days after the cut in MLR and the subsequent fall in banks' base rates. As a result, it was profitable for much of this period for borrowers to round-trip. Once the structure of interest rates had returned to a more normal pattern, this round-tripping began to unwind. But a considerable amount was probably still outstanding on 18 March (the make-up day for banking March) and this may not have been fully unwound until after the end of banking April.

In the second half of March, interest rates up to one month remained virtually unchanged. They then fell, reflecting a significant temporary easing in the cash position of the money markets, but rebounded in the second week of April as shortages reappeared. They showed no obvious trend until the end of April, but very short rates then eased as cash surpluses began to appear in the market.

When MLR was reduced to 12%, banks' base rates were also cut to 12%, and their deposit rates were lowered by 2½ percentage points, to 9%.

Developments in techniques

During March and April, the authorities continued the process of changing their operating techniques along the lines set out in the Bank's Background Note of 24 November, 'Methods of monetary control'. Considerable changes had already been made by the end of February. In the following two months the pace of change was slower, in part because of the unusual conditions in the money markets, but also because of the need to await the outcome of consultations on the proposals contained in the Bank's paper *Monetary control: next steps* which was published on 12 March.(1) However, several changes were made.

First, from the end of February, on days when it seemed that the cash shortage might be too great to be relieved by outright purchases of bills, the Bank renewed the practice used extensively between 1978 and 1980 of offering to buy eligible bills from the discount houses for resale at specified future dates. In doing this, the Bank sought to extend the range of available options for providing cash temporarily against an asset (a longer-term bill) which the holder might not wish to sell outright (because he expected interest rates to fall). As with outright transactions (and in contrast to previous occasions on which this technique had been used), houses wishing to use this facility have to bid a rate of interest at which they will enter a resale agreement; the Bank retains complete freedom as to which, if any, bids it accepts.

Second, from the end of March, the Bank abandoned completely the practice of quoting prices at which it would buy or sell bills. (Since January, the Bank had quoted prices only for bills of under one month to maturity.)(2) The Bank thus became free over the whole range of maturities to choose which, if any, offers it would accept. At the same time, the Bank started to ask those offering bills with under a month to maturity to quote separate prices for bills with fourteen days or less to maturity. This was done to increase the role of market forces in determining the structure of interest rates on bills of very short maturity.

(1) The Background Note was reproduced in the December 1980 *Bulletin*, page 428, and *Monetary control: next steps* in the March 1981 *Bulletin*, page 38.

(2) See the March *Bulletin*, page 24.

Finally, from early May, the Bank allowed the discount houses to increase their maximum holdings of undefined assets[1] from twenty to twenty-five times their capital and reserves and thus to raise their potential holdings of eligible bank bills which the Bank could buy if necessary. This step was taken in the face of increasing liquidity in the banking system and a prospective need for the authorities to provide very large amounts of cash to the money markets (by buying bills) when the Civil Service dispute ends and the backlog of government receipts is made up.

Capital markets

The gilt-edged market

A strong demand for stock after the Budget, together with the issue of the first index-linked government stock at the end of March, ensured very large sales in banking March and April, the first two months of the new monetary target period, and provided assurance of considerable funds in banking May and June as well. With substantial inflows also into national savings (see below), total sales of central government debt to UK non-bank residents were a major factor restraining the growth of sterling M_3. During banking May, however, market conditions were generally more difficult and, with the Bank buying in large quantities of stocks that were near maturity, net official sales were lower than in the two previous banking months. Sales by the banking system and by overseas holders, however, meant that net sales to the non-bank private sector were well maintained.

The authorities began March with one tap stock—12¼% Exchequer Stock 1999 'B' (issued on 7 January); and a low coupon stock—3% Treasury Stock 1986—was issued on 4 March. Gross receipts of around £900 million for the banking month were already assured as a result of earlier sales of the partly-paid 12% Treasury Stock 1986, on which a further call was due on 13 March, and from the final instalment on 12% Exchequer Convertible Stock 1985. Nevertheless, the authorities were looking to make further sales to give a sound start to the funding programme for the new monetary target period.

Ahead of the Budget, investors in the gilt-edged market were cautious; prices in general moved little and turnover was modest. There were few tenders for the low-coupon stock on 4 March. The Budget was well received by the market, and early the following morning (11 March) demand for 12¼% Exchequer Stock 1999 'B' was well in excess of the very large amount still held by the Bank. The authorities chose to meet this demand at a price of £90¾ per cent, £⅝ above the previous official price, but still leaving the prospect of some further short-term rise in prices and, consequently, encouraging suitable conditions for selling stock quickly. Sizable amounts of the low-coupon tap were also sold.

Prices on all medium and long-dated stocks rose significantly over the day (with gains of £2 at the longer end). In the afternoon, the authorities announced an issue direct to the Bank[2] of £1,000 million of 12½% Exchequer Stock 1990 for sale to the public from the following day. The stock was partly paid with only £15 per cent

(1) See the additional notes to Table 2 in the statistical annex.

(2) This technique had previously been used for the issue of 13¾% Treasury Stock 2000/03 'A' in November 1979 and for the issue of three small tranches of existing stocks in December 1980.

Issues of gilt-edged stock (19 February to 20 May)

Stock	Amount issued (£ millions) Total	of which to NDC(a)	Date announced	Date issued	Date exhausted	Minimum price per £100 stock (£)	Payable per £100 stock: On tender (£)	Second instalment (£)	Third instalment (£)	Redemption yield (per cent)
3% Treasury Stock 1986	500	—	27/2	4/3		69.50	In full	—	—	10.80
2% Index-Linked Treasury Stock 1996	1,000	—	10/3	27/3	27/3	(b)	35	30 on 1/5	35 on 26/5	(b)
12½% Exchequer Stock 1990	1,000	—	11/3	11/3	23/3	(b)	15	25 on 3/4	55 on 15/5	13.49
11½% Treasury Stock 1985	1,100	*100*	27/3	1/4		96.50	15	15 on 8/5	66.50 on 12/6	12.60

(a) National Debt Commissioners.
(b) See text.

payable initially (because funding needs for banking March had now been fully met); a further £25 was payable in banking April and a final £55 late in banking May (when no receipts were yet assured).

Roughly one third of the new tap stock was sold on 12 March as prices, particularly of longer-dated stocks, rose again. Further sizable sales were made over the next three days (up to 17 March) at prices up to £15$\frac{5}{16}$. Despite occasional setbacks on profit-taking, the market remained firm, and between 17 and 23 March prices on longer-dated stocks rose further.

Sentiment was helped by reasonably encouraging wage and earnings statistics released on 18 March, while the money supply data published the following day were much as expected. On 23 March, further demand exhausted the tap stock and attention switched to the tender on 27 March for the 2% Index-Linked Treasury Stock 1996. Prices of conventional stocks fell back a little in the three days ahead of the tender.

The Government's purpose in issuing an index-linked stock—the first of its kind—was to increase the flexibility of its funding programme by adding an instrument significantly different from those already available. The stock carries a 2% coupon, with both the value of the principal on repayment and of each half-yearly interest payment related to the increase in the retail price index, subject to a lag of eight months.(1) Eligible holders of the stock are confined essentially to approved pension schemes or funds and, in respect of their UK pension business, to life insurance companies and registered friendly societies. With the stock confined to institutions paying little or no income tax or capital gains tax, problems do not arise as to its treatment for taxation purposes. At the same time, the possibility was avoided of upward pressure on the exchange rate which might have resulted had the stock been generally available to foreign buyers.

To give time for eligible holders to assess the unusual features of the stock, twelve full working days were allowed between the issue of the prospectus and the date for tenders, instead of the normal two or three days. The issue was by tender with no minimum price although, as with other stocks, the authorities reserved the right to reject any tender or to allot a smaller amount than that for which tenders had been received. All successful tenders were to be allotted at the lowest price accepted (as with conventional gilt-edged stocks) and not, for example, at the price bid, as in the weekly Treasury bill tender. The stock was partly paid, reflecting the substantial receipts already assured for banking April, with £35 per cent payable on tender, £30 in banking May and the balance in banking June.

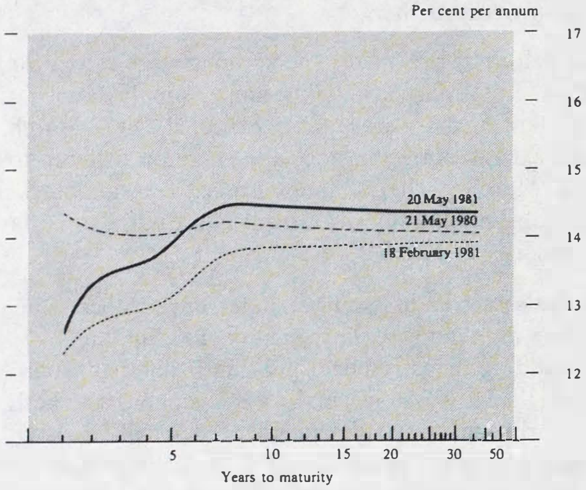
(1) A lag of some months was inevitable in order to allow each interest payment to be calculated in time to make payment on the due date. The choice of an eight-month lag permits the Bank to announce the amount of each forthcoming interest payment before the start of the relevant interest period and would also allow effect to be given to the early redemption provisions, should that be necessary.

Tenders for 2% Index-Linked Treasury Stock 1996

Price tendered per £100 stock(a) (£)	Percentage of tenders received	Percentage of total value of tenders
130 or more	0.3	0.1
120 - 129.75	1.5	1.3
110 - 119.75	24.8	18.5
100 - 109.75	55.0	43.4
90 - 99.75	15.7	29.1
80 - 89.75	2.7	7.6

(a) Bids had to be in multiples of 25 pence.

Time/yield curves of British government stocks[a]



(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 program is available from the Bank at the address given on the reverse of the contents page.

Tenders for the stock on 27 March showed a wide range of bid prices (see table). In the event, the stock was issued at par.[1]

With the index-linked stock duly launched, the authorities felt able to create another conventional stock immediately, and on the same day announced 11½% Treasury Stock 1985. With funding needs in banking April now assured and with substantial calls due in banking May, the stock was partly paid, with over two thirds of the price not due until banking June.

Prices of most stocks fell back immediately and applications for the new stock on 1 April were minimal. A little of the stock was sold the following day at a premium of £$\frac{1}{16}$, but prices then eased again. There were further losses, of up to one point for medium and long-dated stocks, when rather higher-than-expected provisional sterling M_3 figures for March were published on 7 April. There was a similar fall in prices on 13 April after news that a stockbroking firm was in default as a result of transactions involving its gilt-edged department and that some US banks had raised their prime rates. Although prices recovered modestly before Easter, the market was very quiet.

Trading remained subdued after Easter, and in the final week of April prices fell back after press comment that there was no prospect of an early cut in MLR. On 1 May, the Bank bought in large amounts of 8¼% Exchequer Stock 1981 (due to mature on 12 June).[2] On 5 May, after the bank holiday, prices fell heavily (with losses of up to £2½ in some medium and long-dated stocks) following sharp increases in US short-term interest rates. The Bank made further large purchases of stocks close to maturity. There was a small rally on 7 and 8 May, and when the Bank did not announce a new stock, demand was strong enough on 11 May to permit the Bank to sell some of the 1985 tap stock for the first time since 2 April; modest sales were made at £27⅜ per cent, with the stock £30 per cent paid. Sentiment remained a little stronger and further modest sales were made at £27$\frac{7}{16}$ on 19 May.

Over the three banking months to mid-May, yields on gilt-edged stocks rose by around half a point on long-dated stocks and by up to three quarters of a point on short-dated stocks.

Throughout April, the index-linked stock was traded in only very modest amounts on the Stock Exchange, initially at a discount of up to half a point, but later at a modest premium. There was thus no sign of those who had bid well above par at the tender going into the secondary market to bid aggressively for the stock at a lower price. When prices on conventional stocks fell back early in May, the price of the index-linked stock declined as well.

Issues of non-marketable gilt-edged stocks to the National Debt Commissioners

On 16 April, arrangements were introduced to allow for the issue of non-marketable stocks from time to time to the National Debt Commissioners, to reduce the possibility of conflict between the freedom of the Commissioners to invest the public funds under their management and the Bank's objectives in managing the gilt-edged

(1) All applications above par were allotted in full. Applications at par for amounts up to £1 million were also allotted in full; but those for between £1 million and £2 million were awarded £1 million, and applications for £2 million and over were alloted 55% of the amount sought.

(2) The Bank stands ready to buy all stock maturing within three months at known prices related to Treasury bill rates. For tax and technical reasons, holders of a stock close to maturity often prefer to sell it to the Bank rather than await redemption.

market. In the past, when the Commissioners had significant amounts to invest (or reinvest), they would often buy stock which was available from the Issue Department of the Bank in order not to complicate the Bank's market management. Since 1977, as an extension of this practice, the Bank has been prepared to reserve a tranche of appropriate new issues for the Commissioners. Even so, these arrangements could not ensure that the Commissioners could obtain precisely those stocks which they required at times of their choosing, without the possibility of conflict with the Bank's own operations for the purposes of monetary control. Now, the Commissioners will, if they choose, have access to special non-marketable stocks of the coupon and maturity they need, when required, without affecting the market. The intended effect of the new arrangements, therefore, is to increase the investment flexibility of the Commissioners; it does not mean that the market will face significantly less demand from them since their purchases have in any case for some years been largely channelled through the Bank.

Other capital markets and national savings

£ millions; *not seasonally adjusted*
Net cash raised +

	Calendar months	May 80–July 80	Aug. 80–Oct. 80	Nov. 80–Jan. 81	Feb. 81–Apr. 81(a)
A	**National savings**(b)				
	Inflow	+208	+194	+928	+1,459
	of which index-linked certificates	*+204*	*+126*	*+694*	*+ 425*
B	**Local authorities**				
	Stocks	− 22	− 90	− 84	− 8
	Negotiable bonds	+ 4	+ 4	+ 16	− 39
C	**Private sector**				
	Loan capital and preference shares(c)	− 16	+ 57	− 75	− 22
	Equity capital(c)	+301	+289	+439	+ 215
	Unit trusts	+ 26	+ 42	+ 80	+ 175

(a) Provisional.
(b) Includes National Savings Bank investment accounts from January 1981; inflows were £156 million in January and £420 million between February and April.
(c) Net issues by listed UK public companies.

National savings

Net receipts from national savings continued to be very substantial in the three months to end-April (see table). Conditions were favourable for the sale of a number of instruments. Some £420 million was added to National Savings Bank investment accounts, where, until 1 May, a particularly competitive interest rate prevailed, following the cut in MLR on 10 March.[1] A similar amount was raised from index-linked certificates, which began to benefit in April from the reduction in the minimum age of eligible holders (from 60 to 50) announced in the Budget. There were also very large net sales of conventional savings certificates, particularly following the announcement on 17 March that the nineteenth issue would be replaced from 11 May with a new issue (the twenty-first) offering a net yield more in line with competing rates.[2]

Over the 1980/81 financial year, net receipts from national savings were £2,200 million.[3] For the present financial year, the Government has set a target of £3,000 million.

Other capital markets (three months to end-April)

There has been a distinct revival of activity in several sectors of the domestic capital market, with attention concentrated on various forms of fixed-interest debt. New equity capital raised was considerably lower than in recent quarters but, with the equity market generally strong, a significant number of rights issues were announced in the first half of May.

Among the local authority markets, the most notable feature was the stock issue of £50 million by the City of Leeds— the first issue by an authority since 1979. It was also the first since 1967 with a maturity of over twenty years. The stock, issued on 26 March, was oversubscribed and allotted on terms giving a gross redemption yield of 13.82%, roughly 0.6 points above an equivalent gilt-edged stock. In April, the City of Swansea placed £7 million of stock of a similar maturity on a redemption yield on 14.23%. As a result of these issues, net redemptions of stock in the period were much smaller than in recent quarters.

(1) Interest on these accounts is calculated on a calendar month basis and can be changed only upon one month's notice. The rate was reduced from 15% to 13% from 1 May.
(2) 9.02% per annum if held to maturity, against 10.33% on the nineteenth issue.
(3) Including National Savings Bank investment accounts from 1 January.

There was also increased activity in the domestic bulldog[1] market for foreign borrowers in sterling. Following the earlier placings by Denmark in July 1980 and by Iceland in January this year, there were three further issues in March and April: in March, Sweden raised £50 million with a maturity of five years by way of an offer for sale, and Pemex[2] placed £50 million with a maturity of twenty-five years; in April, the IBRD[3] offered for sale £100 million of stock with a maturity of five years.

In other parts of the fixed-interest market, there were fewer signs of renewed interest by borrowers, with net redemptions of local authority negotiable bonds and, as in previous quarters, of private sector loan capital and preference shares.

Nevertheless, the possible flow of new stock issues by both domestic and foreign borrowers has increased. The cut in MLR to 12% announced at the time of the Budget has stimulated a fairly large number of prospective borrowers to come forward, either into the new issues queue, or onto the waiting list recently established by the Bank for prospective borrowers not ready to set a firm date.[4]

Droplock arrangements

In recent months, there has been renewed interest in sterling droplock arrangements. The droplock is a technique which has been used intermittently in the international bond markets and a number of local authorities have negotiated sterling facilities incorporating it over the past two years. There is now evidence of interest among corporate borrowers in utilising the technique as a means of securing long-term financing in the capital market.

The droplock facilities so far arranged have typically taken one of two forms.

The droplock loan is a medium-term floating-rate bank facility (usually provided by a syndicate of banks), with a built-in trigger mechanism which operates if long-term interest rates fall to a pre-determined level during the life of the loan or if the borrower exercises an option to convert at some higher level. When the trigger operates, the bank loan is automatically refinanced by a placing of fixed-rate long-term stock with a group of institutions. Droplock option agreements take the form of a similar commitment to a placing of fixed-rate long-term stock if interest rates fall to a pre-determined level, but without the initial bank loan. Some of these options have no specific trigger level but, instead, give the borrower the right to place stock in a given time period at a specified margin over one or more gilt-edged stocks.

Arrangements of this type offer the prospect of a useful expansion in the facilities available in the capital market, and the Bank has accordingly worked closely with the various parties involved in developing them. Since the placings of stock have an impact on the new issues queue, intending borrowers are asked—before entering into droplock commitments—to notify the Government Broker of the main details of the transaction, and should at that stage seek timing consent under the Control of Borrowing Order for the ultimate placing of the stock. It is not felt necessary at present to institute queuing arrangements for droplock facilities, but the Bank will continue to monitor the volume of droplock transactions and will, if necessary, take steps to ensure that they do not disturb

(1) The term generally applied to stock issues by foreign borrowers in the domestic sterling market.
(2) The national oil company of Mexico.
(3) The International Bank for Reconstruction and Development, often referred to as the 'World Bank'.
(4) See the March 1981 *Bulletin*, page 30.

Outstanding stock placings with droplock arrangements

Trigger level (a)	Amounts committed as at mid-May (£ millions)
11% up to 11½%	8
10½% „ 11%	31
10% „ 10½%	30
9½% „ 10%	48
9% „ 9½%	5
No specified level	26

(a) Usually set with reference to the yield on high coupon, long-dated gilt-edged stocks.

conditions in the new issues market. To this end, it will clearly be useful for the market to be aware of the size of stock placings associated with particular interest-rate trigger levels. The table sets out the position at mid-May on the basis of droplock arrangements known to the Bank.

Equity market

The equity market remained firm during February and early March in the face of several disappointing results from major companies, but weakened just ahead of the Budget. Immediately after the Budget, prices fell sharply, but they recovered quickly and, in the last two full weeks in March, the FT Actuaries all-share index rose by 5%, aided by hopes of a recovery in domestic activity later in 1981 and by the strength of share prices in the United States (the main Wall Street index reaching its highest level for eight years on 25 March). In early April, there was a further jump in UK share prices—with the all-share index reaching a record level—partly on hopes of an early cut in MLR. When these hopes were disappointed, there was a temporary setback, but prices rose further just before and after Easter, ending the month on a firm note after a little profit-taking, with the all-share index at 332.1, just under 10% higher than at the end of February. (In May, this gain was partially reversed.)

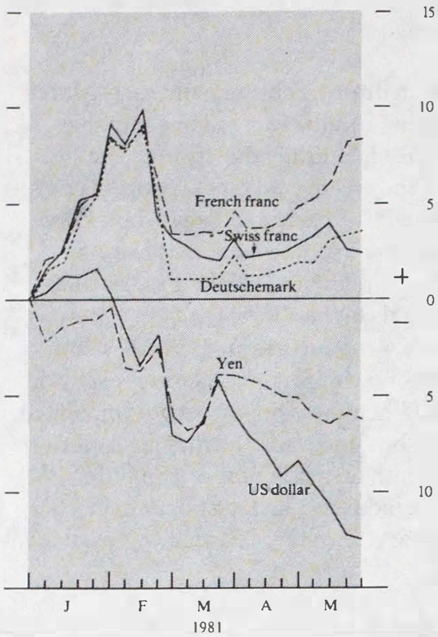
After allowing for inflation, current share prices are still significantly lower than ten years ago: in real terms they have halved since 1970, while GDP in real terms has risen modestly. Over a shorter period, share prices at the end of April were only slightly higher in real terms than four or six years ago.

Foreign exchange and gold markets

Summary

Exchange markets were very active for most of March and April, reflecting sharp movements in interest rates and reacting nervously to political news. After a firm beginning, the dollar weakened towards mid-March as interest rates fell in the face of apparent evidence of a slowdown in economic activity; but later indicators suggested that the US economy was still buoyant and the dollar surged ahead, supported by firmer interest rates and also by capital inflows prompted by concern over developments in Poland. In the United Kingdom, the widely anticipated reduction in MLR had little further effect on sterling; it weakened against the dollar, but remained stable against European currencies, and in effective terms, sustained by a continuing trade surplus and further falls in the rate of inflation and in the growth of average earnings. Interest rates in West Germany remained close to the high levels reached in February and the deutschemark rose to the top of the European Monetary System (EMS), giving rise to increasing pressures within the exchange rate mechanism. The lira was devalued by 6% in March, and in Belgium official interest rates were raised substantially to ease pressure on the Belgian franc at the bottom of the 2¼% band. France and the Netherlands also increased official interest rates, and by the end of April strains within the EMS had eased considerably. The yen remained firm despite a cut in rediscount rate. The gold market was volatile, moving sharply in response both to political developments and to movements in interest rates.

Sterling against selected foreign currencies
Change from end-October 1980



Changes in UK official reserves
$ millions

	1981			
	Jan.	Feb.	Mar.	Apr.
Change in reserves including revaluation	**+918**	**+ 40**	**−222**	**−146**
IMF oil facility repayment	− 78	—	—	− 77
Other HMG capital repayments	—	—	—	—
SDR allocation	+373	—	—	—
EMCF swap valuation gain	+266	—	—	+229
Annual revaluation of reserves	—	—	−257	—
Exchange cover scheme:				
Borrowing	+213	+100	+160	+100
Repayments	−164	− 56	−176	−372
Underlying change in reserves	**+308**	**− 4**	**+ 51**	**− 26**
Level of reserves (end of period)	28,394	28,434	28,212	28,066

Sterling

On 2 March, sterling opened at $2.1660, nearly four cents lower than the closing rate at end-February; this followed heavy selling over the previous weekend from the Middle and Far East, prompted by expectations of a large reduction in MLR. But sterling quickly recovered as interest rates rose in advance of petroleum revenue tax payments; thereafter it traded in the $2.19–2.20 range in an active two-way market before moving higher just before the Budget on a growing belief that the reduction in MLR would be smaller than had earlier been forecast. There was little immediate market reaction to the Budget itself, but the pound continued to strengthen on regular commercial demand against a background of falling interest rates in the United States and Japan. Publication of another trade surplus in February, albeit a somewhat smaller one, and a further fall in the rate of growth of average earnings, added to the firmer trend, and sterling rose to $2.30 on 19 March. Towards the end of the month it began to weaken against the dollar, but remained stable against continental currencies and closed the month at DM 4.70 and $2.2420, with the effective index (ERI) at 100.1.

In April, sterling continued to ease against a strengthening dollar amid some speculation about a further cut in MLR and reached $2.1670 on 6 April, but it soon recovered with the publication of a larger-than-expected increase in sterling M_3 for banking March. In the week before Easter sterling again fell against the dollar, reaching $2.1460 on 16 April, but maintained its position against continental currencies. Over Easter, however, the pound was in demand in US markets, and this continued after the holiday, pushing the rate to $2.1855 before it dropped back, despite steady commercial demand, to close the month at $2.1450. Sterling strengthened slightly against European currencies over April, closing at DM 4.73½, Sw. Fcs. 4.32½ and Fr. Fcs. 11.23. The ERI was 98.9.

During March and April, the UK reserves fell by a total of $368 million, to $28,066 million. The annual revaluation of the reserves at the end of March[1] resulted in a net reduction of $257 million (comprising a valuation increase of $272 million on gold holdings and a decrease of $529 million in SDRs, ECUs and non-dollar currencies), while the EMCF swap in April added $229 million. After allowing for these revaluation effects, a further oil facility repayment to the IMF and net repayments under the exchange cover scheme, the reserves showed an underlying increase of $25 million. On 11 March, the Government said that it would repay in 1981 the whole of the $2.5 billion eurodollar loan raised in 1974 and originally due for repayment between 1981 and 1984. At the same time it was announced that the official exchange cover scheme would in future be limited to borrowings from institutions of the European Community.

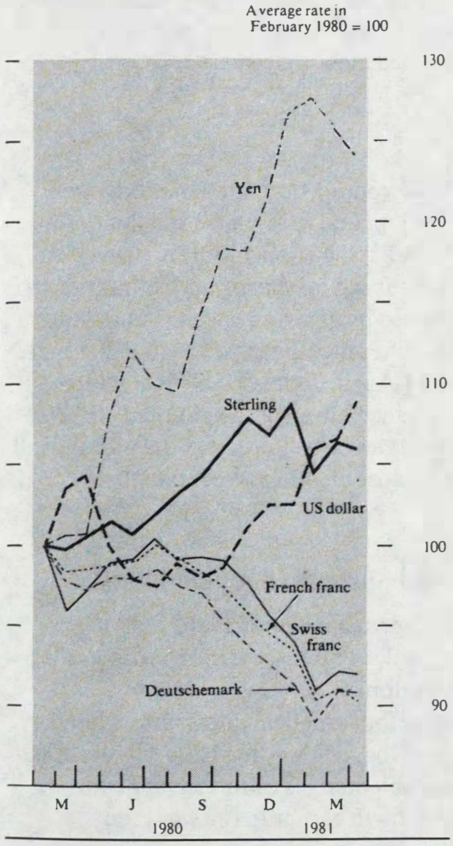
US dollar

The dollar began March very firm, boosted by a sharp increase in eurodollar interest rates reflecting an unexpectedly large rise in the US monetary aggregates at the end of February. But interest rates soon began to ease as indicators suggested a slowdown in economic activity; the Federal funds rate fell to around 13% and prime rates were gradually reduced to 17%. By 19 March, the dollar had fallen by over 4% against sterling, to $2.28, and by 3% in effective terms, to 98.3. But the probability of higher interest rates following the publication of a large increase in the money supply, combined with

(1) See the additional notes to Table 17 in the statistical annex.

increasing tensions in Poland in late March, reversed the decline. The upward trend was briefly interrupted by reaction to the attempted assassination of President Reagan, but the Federal Reserve intervened to steady the market and the dollar continued to strengthen. The rise was further underpinned by the publication of indicators suggesting a buoyant economy, with GNP up 8.4% (at an annual rate) in the first quarter, and on 16 April the dollar reached DM 2.1883, and 103.0 in effective terms. These levels were sustained over the Easter period and exceeded towards the end of the month when the trade figures revealed a much smaller deficit, and the Federal funds rate reached $18\frac{1}{2}$%. The dollar rose to new recent peaks against a number of European currencies, including the French franc, and at Fr. Fcs. 5.26 reached its highest since the Smithsonian realignment in December 1971. The dollar closed the period at DM 2.2071, Fr. Fcs. 5.2362 and 103.3 in effective terms, a rise of over five points in the effective index since mid-March. Apart from the day on which the President was wounded, there was no official intervention by the Federal Reserve; this was in line with the authorities' new policy of intervening only to counter disorderly market conditions.

Indices of effective exchange rates

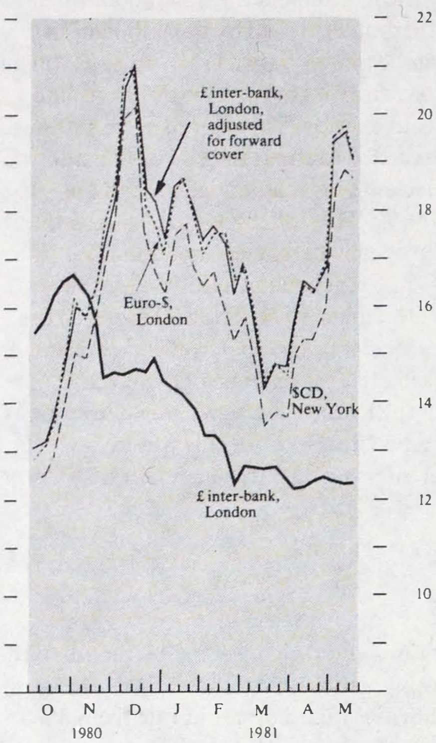


Other currencies

High West German interest rates and the consequent strength of the deutschemark caused increasing tensions within the EMS in March. On 3 March, the Dutch authorities raised discount rate from 8% to 9%, and the guilder briefly rose to the top of the grid, but it was soon replaced by the deutschemark. The Belgian franc, at the bottom of the $2\frac{1}{4}$% band, was under constant pressure and frequently reached its intervention limit against the deutschemark. The lira also suffered, and by 20 March had fallen to over 5% below the deutschemark despite substantial official support. The Italian authorities responded with a package of measures, including a 6% downwards adjustment of the bilateral central rates of the lira against other EMS currencies and an increase in discount rate from $16\frac{1}{2}$% to 19%. Thereafter the lira remained comfortably in the upper half of the system (although it continued to weaken against the dollar) and attention once again focused on the Belgian franc. Increases on 26 March in Bank and Lombard rates to 13% and 15% respectively had little effect, and on 31 March the Belgian authorities increased both rates by a further three percentage points and introduced a temporary price freeze. Pressures within the system began to ease in April; the Belgian authorities were able to reduce Bank and Lombard rates in the second half of April and by the end of the month the margin between the weakest and strongest currencies had fallen to $1\frac{5}{8}$%. Although remaining comfortably in second place for most of the period, the French franc weakened during the first round of the Presidential election despite regular official support in the preceding weeks and precautionary increases in official interest rates. (The French franc subsequently fell very sharply after the second round of the Presidential elections on 10 May, reaching its intervention limit against the deutschemark and the lowest-ever level against the US dollar of Fr. Fcs. $5.61\frac{1}{2}$ on 21 May. The franc required substantial official support, and the authorities introduced certain exchange control measures and increased their money-market intervention rate to a record 22%.) The Danish krone weakened over the two-month period, and the Irish pound also came under pressure, falling very close to the bottom of the system at times and requiring regular support as the balance of payments continued to deteriorate.

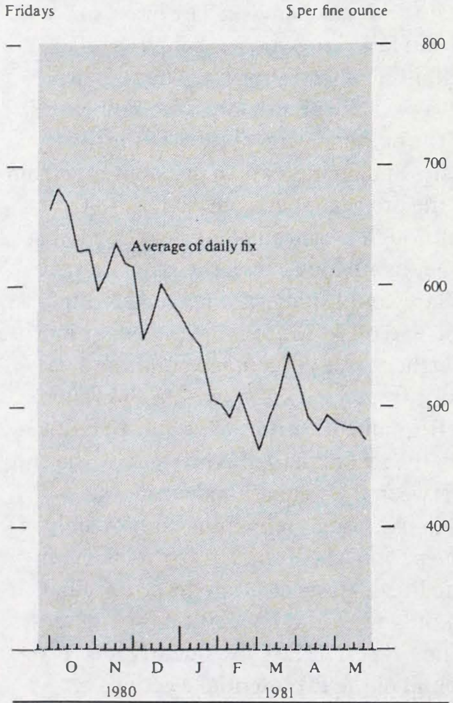
UK and US three-month interest rates

Weekly averages	Per cent per annum



London gold price

Fridays	$ per fine ounce



The Swedish krona was firm for most of the period, reflecting the continued improvement in Sweden's external position, but weakened temporarily towards the end of April as the coalition government showed signs of breaking up. The Norwegian krone was in strong demand for oil tax payments and its effective index rose. The Swiss franc was weak at times, but benefited from some pre-election capital flows out of the French franc and ended a little stronger against the deutschemark at Sw. Fcs. 0.91$\frac{3}{8}$. The yen weakened only slightly following a long-expected cut in the Bank of Japan's rediscount rate to 6$\frac{1}{4}$% on 18 March, but fell further as the dollar strengthened in April, touching ¥218.20 just after Easter, before recovering sharply on strong Middle East demand to reach ¥211.97 on 27 April. It closed a little easier at ¥215.55. The Canadian dollar strengthened over the period as short-term interest rates reached record levels and the premium over US interest rates was firmly re-established.

Interest rates and differentials

The three-month eurodollar rate began the period at 17%, but fell back steadily during March and reached 14$\frac{1}{4}$% by the beginning of April. It then picked up in the face of large increases in the US monetary aggregates and remained above 16% throughout the second half of April, closing at 16$\frac{15}{16}$%. After opening March at 12$\frac{15}{16}$%, the three-month inter-bank sterling rate remained very steady, moving in a narrow range between 12$\frac{3}{16}$% and 12$\frac{13}{16}$%, and closed at 12$\frac{7}{16}$%. Three-month sterling traded consistently at a premium in forward markets, falling from a peak of 4$\frac{13}{16}$% on 3 March to 1$\frac{3}{8}$% on 19 March, before rising again to close at 4$\frac{5}{16}$%. The covered differential remained close to interest-rate parity throughout the period.

Gold

The gold market was active and volatile during the period, once again being dominated by developments in Poland and fluctuations in US interest rates. The price fell to $457 on 5 March, the lowest fixing for fifteen months, but it turned up sharply as US interest rates weakened and was later sustained by growing tensions in Poland, reaching 547\frac{1}{4}$ on 27 March. After moving in the $510–530 range, the price fell below $500 in mid-April, depressed by firmer interest rates in the United States and cancellation of the national strike in Poland. Markets became quieter towards the end of the month, and the price eased back further to close at 482\frac{3}{4}$, a net fall of only 6\frac{1}{4}$ since the end of February.

International banking and eurocurrency markets

International developments (fourth quarter of 1980)

The gross external claims of banks within the BIS reporting area grew by some $75 billion in the fourth quarter of 1980, to $1,325 billion.(1) After allowing for statistical distortions caused by exchange rate fluctuations, and for redepositing between reporting banks, the underlying growth of lending is estimated at about $50 billion. After fairly slow growth earlier in the year, the international banking market grew by 23% over 1980 as a whole, only a little less than during 1978 and 1979.

External claims of the reporting European banks increased by about $77 billion in the December quarter—a rise four times greater than in the third quarter. A substantial amount of this may have been due to banks' end-year operations; other factors were the unsettled exchange markets, the general revival in the growth of international

(1) Data published by the Bank for International Settlements—see Table 13 in the statistical annex.

bank activity, and less recourse to official reserves to finance deficits. For the third consecutive quarter, banks in the United States were large suppliers of funds to the market ($12 billion). The steady increase in US interest rates appears not to have stemmed the growth of this lending.

The supply of funds from oil-exporting countries ($6½ billion) once again declined; net of borrowing, they provided only $1½ billion.

The developing countries increased their outstanding borrowing by nearly $15 billion, with substantially more than half going to Latin America (mainly Mexico, Brazil and Chile). For 1980 as a whole, net new finance provided by the reporting banks to the non-oil developing countries was $35 billion, nearly 50% more than in 1979, and about equal to the net inflow of funds from the oil-exporting countries. Claims on Eastern European countries rose by $3¾ billion in the fourth quarter.

Countries within the reporting area continued to be net takers of funds, absorbing about $20 billion. In particular, the Japanese banking system took nearly $11 billion net, no doubt partly as a contribution to the financing of the Japanese current account deficit.

Eurosterling

For the second successive quarter, the eurosterling market (as defined in the accompanying table) grew only modestly. This suggests that the strong growth in the first half of 1980 was due primarily to the removal of UK exchange controls in October 1979 and to the continued operation of the 'corset' until mid-June 1980. The increase of £0.3 billion in eurosterling deposits in the December quarter was more than accounted for by deposits from UK banks (+£0.5 billion) and UK non-banks (+£0.3 billion); claims fell by £0.2 billion. Thus the banks' eurosterling liabilities exceeded their claims by £4 billion at end-1980; the size of this 'switch out' is comparatively larger for eurosterling than other eurocurrencies, possibly because non-bank demand for eurosterling loans is still small, and perhaps because non-residents' direct access to sterling borrowing in the United Kingdom has increased.

Eurosterling market[a]

£ billions

	1979		1980			
	Sept.	Dec.	Mar.	June(b)	Sept.	Dec.
Deposits by:						
UK banks	0.6	0.7	1.0	1.7	2.1	2.6
UK non-banks	0.4	0.6	0.9	1.0	0.8	1.1
Other Western Europe	4.5	4.4	5.4	5.7	5.6	5.1
Oil-exporting countries	0.6	0.7	1.1	1.1	1.0	1.0
Other	1.6	1.4	1.6	1.6	1.5	1.5
Total	**7.7**	**7.8**	**10.0**	**11.1**	**11.0**	**11.3**
Of which, central monetary institutions	*0.6*	*0.7*	*1.0*	*1.0*	*0.8*	*0.9*
Claims on:						
UK banks	1.1	1.7	1.6	2.2	2.2	2.3
UK non-banks	0.3	0.9	0.8	0.8	0.6	0.7
Other Western Europe	3.4	3.2	3.8	3.8	4.0	3.7
Other	0.7	0.5	0.6	0.8	0.7	0.6
Total	**5.5**	**6.3**	**6.8**	**7.6**	**7.5**	**7.3**

Source: Bank for International Settlements

(a) The table shows sterling liabilities and claims of banks in the Group of Ten countries (except the United States and—by definition—the United Kingdom), Austria, Denmark, the Republic of Ireland and Switzerland. Apart from this geographical limitation, full data on business with residents of the countries in which the reporting banks are situated are not available for all countries. The table therefore understates the size of the market.

(b) Expansion of coverage between March and June 1980 increased UK banks' deposits by £0.2 billion and UK non-bank deposits, claims on UK banks and claims on UK non-banks each by £0.1 billion.

UK contribution to BIS half-yearly survey of banks' external positions (end-1980)

The contribution of UK banks to the detailed half-yearly surveys of banks' positions *vis-à-vis* countries outside the BIS reporting area, undertaken by all central banks within the area, is set out in Table 14.3 of the statistical annex.

If claims on the offshore banking centres (which are predominantly short-term inter-bank positions) are excluded, there has been a continued and marked movement towards shorter maturities for most groups of borrowers, and in particular for Eastern European and non-oil developing countries. In contrast, Australia, New Zealand and South Africa managed to lengthen the maturity profile of their borrowing.

There was a widespread decline in unused credit facilities of $1.6 billion between end-June and end-December.

UK banks' liabilities and assets by customer[a]

$ billions

	1980				1981
	31 Mar.	30 June	30 Sept.	31 Dec.	31 Mar.
Foreign currency liabilities of UK banks to:					
Other UK banks	96.1	103.7	109.1	118.5	130.2
Other UK residents	11.9	13.5	13.5	13.9	17.0
Overseas central monetary institutions	57.9	61.4	62.8	58.6	58.1
Other banks overseas	186.0	198.6	201.0	222.8	233.3
Other non-residents	55.2	57.4	60.6	67.8	74.7
Other liabilities(b)	3.1	3.5	3.7	3.8	3.9
Total liabilities	**410.2**	**438.1**	**450.7**	**485.4**	**517.2**
Foreign currency assets of UK banks with:					
Other UK banks	92.6	99.4	106.4	116.4	129.0
Other UK residents	22.6	25.6	24.1	22.9	23.5
Banks overseas	216.2	227.1	228.9	249.1	263.0
Other non-residents	73.2	80.6	84.8	88.2	92.3
Other assets(b)	5.9	7.1	7.5	8.4	8.6
Total assets	**410.5**	**439.8**	**451.7**	**485.0**	**516.4**

(a) Figures differ from those in Table 6 in the statistical annex (see additional notes to Table 14.1)

(b) Mainly capital and other internal funds denominated in foreign currency.

UK banks' net liabilities and claims by country or area[a]

$ billions

Net source of funds to London – /net use of London funds +

	1980				1981
	31 Mar.	30 June	30 Sept.	31 Dec.	31 Mar.
BIS reporting area:					
European area	– 7.4	– 3.7	– 1.4	– 7.2	+ 1.4
Canada	– 0.5	– 0.5	– 0.3	+ 0.5	+ 1.8
Japan	+13.5	+16.0	+17.3	+17.9	+15.8
United States	–13.9	–18.7	–17.0	–20.3	–22.1
Offshore banking centres	+14.5	+12.5	+ 9.3	+ 7.6	+ 8.2
Other Western Europe	+ 4.0	+ 4.7	+ 5.3	+ 6.7	+ 8.4
Australia, New Zealand and South Africa	+ 2.1	+ 2.7	+ 3.0	+ 3.3	+ 3.6
Eastern Europe	+10.1	+10.7	+10.4	+10.6	+11.5
Oil-exporting countries	–31.2	–33.1	–37.4	–38.6	–43.9
Non-oil developing countries	+ 7.2	+ 8.4	+10.8	+13.5	+16.5
Others(b)	–11.7	–13.8	–13.1	– 6.9	–12.8
Total	**–13.3**	**–14.0**	**–13.1**	**–13.1**	**–11.6**

(a) The breakdown corresponds to that in Table 14.1 in the statistical annex.

(b) Includes international organisations and certain unallocated items.

Announced new medium-term eurocurrency credits[a]

$ billions

	1979	1980	1981	
	Quarterly rate		Q1	April
Major OECD countries	3.2	4.8	4.8	0.2
Minor OECD countries	3.7	4.7	4.0	1.9
Oil-exporting countries	1.9	1.9	1.4	0.2
Eastern Europe	1.0	0.6	0.9	—
Developing countries	7.6	6.1	10.4	1.8
of which:				
Countries with some degree of oil self-sufficiency	*2.3*	*1.7*	*3.7*	*0.7*
Newly industrialised countries	*2.6*	*2.5*	*3.1*	*0.7*
Other	0.7	0.2	0.1	0.1
Total	18.1	18.3	21.6	4.2

(a) Maturities of three years and over.

London market (first quarter of 1981)

After adjustment for the effects of exchange rate fluctuations, the London eurocurrency market—as measured by the gross foreign currency liabilities of UK banks—grew by $36 billion ($32 billion unadjusted) in the first quarter of 1981. In unadjusted terms, $17 billion of the increase was accounted for by the continued rapid growth of Japanese banks' foreign currency liabilities; while American banks recorded an increase of $5 billion and British banks $3 billion.

There was some acceleration in the growth of foreign currency deposits placed in the London market by overseas residents. The oil exporters, the United States and Japan each increased their deposits by $4 billion, while the deposits of offshore centres rose by $3 billion. Eastern European countries, on the other hand, drew down their holdings by over $1½ billion.

New lending to non-oil developing countries ($3 billion) grew at a similar rate to that in recent quarters; as usual, the greater part was absorbed by Latin American countries.

The maturity analysis of the foreign currency positions of British banks at mid-February appears to show that their short-term net liability positions viewed as a percentage of total claims increased in the period since mid-November. However, this was largely because of a change in the method of compiling the statistics for British banks; the underlying position showed little change. The consortium banks and 'other overseas banks' showed increased mismatches in the up-to-three-months maturity band.

Medium-term eurocurrency credit markets (first four months of 1981)

The medium-term credit markets continued to be active, with developing countries accounting for 48% of total borrowing compared with just over one third in 1980. This may reflect the wish of banks to increase their return on assets in the face of continued low spreads for OECD borrowers, or it may simply be a response to demand. While the average spread for public sector borrowers from the major OECD countries fell below ½% in the first quarter (for the first time since early 1979), spreads for borrowers from developing countries moved above 1%.

In April, total borrowing fell back sharply and was the lowest since September 1980.

International bond markets (first four months of 1981)

The pattern of new issues of bonds and floating-rate notes has been erratic in recent months. After a slight fall in the first quarter (to $7.9 billion) compared with the quarterly average for last year, issues recovered in April and May. There have been various factors at play. First, a decline in the volume of new dollar non-convertible fixed-rate issues was offset by a revival of convertible issues and floating-rate notes. Second, the effect of the moratorium on new issues in the deutschemark sector was partly offset by an expansion of lending in closely related European currencies. Third, there were signs of steady growth in the minor sectors—largely those of the yen, sterling and French franc.

These developments have to some extent been determined by the type of borrower approaching the markets. The recent revival in new issues has been spurred by international institutions seeking to spread their exposure between currencies, while dollar borrowing by OECD countries has tended to decline. Events have also been influenced by interest rate movements. In the dollar sector, yields on non-convertible fixed-rate bonds edged back over 14% after appearing to be moving downward at the beginning of the year, and nearly all issues this year have been priced to yield well over 14%. In May, coupons moved up further, to 15¾%. This was clearly too costly for many borrowers.

Similarly, the rise in West German and Swiss interest rates since March has deterred many potential borrowers, despite the lifting of the moratorium in April in the deutschemark sector. Deutschemark issues are running at about one third of the rate of last year compared with a maximum of one half permitted by the Capital Markets Sub-Committee.

These adverse effects have to some extent been offset by greater recourse to floating-rate notes, which should in principle appeal to borrowers at a time of high interest rates. In addition, borrowing in yen and sterling may have been associated with risk-spreading policies by Scandinavian countries and certain oil exporters.

Identified deployment of oil exporters' surpluses(a)
$ billions

	1979 Year	1980 Year	1980 Q3	1980 Q4	1981 Q1(b)
United Kingdom:					
Sterling bank deposits	1.4	1.4	0.2	−0.1	0.3
Eurocurrency bank deposits	14.8	14.8	5.3	3.5	4.6
British government stocks	0.4	1.9	0.7	—	0.2
Treasury bills	—	−0.1	−0.2	−0.1	0.2
Other sterling placements	0.4	0.1	—	—	—
Other foreign currency placements	0.2	−0.5	—	−0.2	−0.1
	17.2	17.6	6.0	3.1	5.2
United States:					
Bank deposits	5.0	−1.2	−2.0	−1.0	0.3
Treasury bonds and notes	−1.1	8.3	1.6	2.2	3.0
Treasury bills	3.3	1.4	0.7	−0.2	0.1
Other portfolio investment	1.0	4.6	1.9	1.0	1.5
Other	−1.4	1.4	0.5	0.3	..
	6.8	14.5	2.7	2.3	4.9
Bank deposits in other industrialised countries	18.7	26.2	6.9	2.8	..
Other investment in other industrialised countries(c)	8.7	16.7	4.7	3.9	6.1
IMF and IBRD(d)	−0.4	4.9	0.3	1.2	0.2
Loans to developing countries	9.6	6.6	1.8	0.8	0.5
Total identified deployed net cash surplus	**60.6**	**86.5**	**22.4**	**14.1**	..
Residual of unidentified items(e)	10.4	8.5	−2.4	3.9	..
Total net cash surplus derived from current account (as shown in the following table)	**71.0**	**95.0**	**20.0**	**18.0**	..

.. not available.

(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. These items are shown as net external borrowing etc., in the following table.

(b) Provisional

(c) Mainly loans and holdings of equities.

(d) Includes holdings of gold.

(e) The residual may reflect errors in either the current or capital account.

Oil exporters' current account balance and cash surplus available for investment
$ billions

	1979 Year	1980 Year	1980 Q3	1980 Q4	1981 Q1
Exports	223	310	78	74	82
Imports	−111	−150	−39	−41	−46
Merchandise trade	112	160	39	33	36
Net invisibles	− 46	− 54	−14	−14	−14
of which official transfers	*− 3*	*− 4*	*− 1*	*− 1*	*− 1*
Current balance	**66**	**106**	**25**	**19**	**22**
Net external borrowing etc.(a)	5	− 11	− 5	− 1	..
Surplus available for investment	**71**	**95**	**20**	**18**	..

.. not available.

(a) For definitions, see footnote (a) to previous table.

Deployment of oil money

The total identified deployed cash surplus of the oil-exporting countries for the fourth quarter of 1980 was $14.1 billion, bringing the total for the second half of the year to nearly $37 billion compared with $50 billion in the first half. For 1980 as a whole the aggregate current account surplus of the oil-exporting countries is estimated to have been some $106 billion. The disposable cash surplus for the same period is estimated at $95 billion, some $9 billion larger than the deployed surplus identified so far for the year.

During 1980, the proportion of new funds placed in the United Kingdom and the United States fell to some 37% of total identified investments, while the proportion of funds placed in other industrial countries rose to nearly 50%. There is some evidence of a lengthening of the maturity of new placements, particularly in the second half of the year. In the United States, for example, new placements were predominantly in the form of Treasury bonds and notes and other portfolio holdings, while bank deposits in the second half of the year fell by $3 billion.

New longer-term investment in industrialised countries other than the United Kingdom and the United States, notably in West Germany and Japan, was also greater in 1980 than in the previous year.

In the first quarter of 1981, oil-exporting countries' new placements in the United Kingdom were $5.2 billion, predominantly in dollar-denominated bank deposits. Investment in the United States rose by $4.9 billion during the quarter: the movement towards longer-term investments continued with Treasury bonds and notes increasing by $3 billion and other portfolio investment by $1.5 billion.

Commodity markets

In March and April, prices generally moved narrowly, and speculative activity remained modest. The further strengthening of the dollar provided some upward impetus: among the base metals, copper, lead, zinc and nickel prices all rose on balance during the period. The only marked fall was in the price of sugar, reflecting reduced demand.

A London futures contract in gas oil was introduced by the International Petroleum Exchange on 6 April; this attracted considerable business from its inception.