International financial developments

- *There was a slowdown in international bank lending in the first quarter of 1982. It appears that lenders have subsequently become more cautious and selective.*
- *The supply of funds from the oil exporting countries continued to decline in the first quarter.*

International balance of payments developments

The world current account

The declining surplus of the oil exporters has been a principal feature of world payments balances during the past twelve months. But so far, the counterpart to this decline has not been fully identified (see box on page 356): there have been significant improvements in a number of individual countries, but not in the overall current account position of any of the principal country groups.

Among the major industrial countries, a deterioration in the UK current account through 1981 offset much of the improvement elsewhere. The minor OECD countries registered only a small improvement over this period, and this was concentrated chiefly in the Netherlands, Norway and Switzerland. Other countries in this group remained in substantial deficit.

For the non-oil developing countries, there was no apparent improvement until the final quarter of last year when there does appear to have been some narrowing in their deficit. This improvement appears to have been sustained in the first half of 1982.

Current account summary

$ billions; *seasonally adjusted*

	1980	1981			1982
	Year	Year	H1	H2	H1(a)
Total OECD	- 69	- 33	- 18	- 15	- 10
of which:					
Major countries(b)	*- 34*	*- 4*	*- 2*	*- 2*	*2*
Other	*- 35*	*- 29*	*- 16*	*- 13*	*- 12*
Oil exporting countries	112	67	46	21	2
of which:					
Capital exporters(c)	*90*	*83*	*49*	*34*	*18*
Other	*22*	*- 16*	*- 3*	*- 13*	*- 16*
Other developing countries	- 66	- 77	- 40	- 37	- 34
Other countries(d)	- 1	- 5	- 2	- 3	- 3
World discrepancy(e)	- 24	- 48	- 14	- 34	- 45

(a) Includes Bank estimates/forecasts.
(b) United States, Canada, France, Italy, Japan, United Kingdom and West Germany.
(c) Kuwait, Libya, Oman, Qatar, Saudi Arabia and the UAE.
(d) South Africa and the centrally planned economies.
(e) This item reflects errors and omissions arising from incomplete country coverage, timing differences and other statistical deficiencies.

Major overseas economies

In the first quarter of 1982, the earlier steady improvement in the combined current account position of the major overseas economies received a setback, although this was mainly concentrated in two countries. In Italy, the ending of its import deposit scheme coincided with a sharp rise in domestic demand, while in Germany, earlier strong export growth tailed off as export markets faltered. In the second quarter, however, current accounts improved in every country apart from France, the only one remaining in deficit. The main factor behind the general improvement elsewhere appears to have been gains in the terms of trade, reflecting in part the weakness of raw material prices. In the case of Italy, receipts from tourism were also a positive factor.

Major countries: current balances

$ billions; *seasonally adjusted*

	1981			1982	
	Year	Q3	Q4	Q1	Q2(a)
United States	4.5	0.8	-0.9	1.1	2.1
Canada	- 5.4	-2.1	-0.5	0.3	1.2
France	- 4.8	-1.3	-2.1	-2.0	-3.2
Italy	- 8.0	-0.6	-0.9	-4.0	0.6
Japan	4.7	2.5	1.1	0.9	2.5
West Germany	- 7.8	-2.1	1.4	-0.8	0.1
Six major overseas countries	-16.8	-2.8	-1.9	-4.5	3.3
United Kingdom	12.8	0.4(b)	2.8	1.4	1.6

(a) Includes Bank estimates.
(b) CSO estimate.

United Kingdom

The visible trade balance deteriorated further in the second quarter of 1982: the visible surplus totalled £0.1 billion, compared with £0.4 billion in the previous quarter and £1.1 billion in the second quarter of 1981. With the surplus on oil trade broadly unchanged at £0.9 billion, the deterioration in the visible trade balance since the second quarter of 1981 has been in the non-oil account.

First estimates suggest that the surplus on invisibles recovered from the sharp fall in the first quarter. The interest, profits and dividends account swung back into surplus, of £0.4 billion, after a deficit of £0.2 billion in the first quarter, mainly because of a recovery in the net interest earned by UK banks on their foreign currency transactions and in the direct investment earnings overseas of companies outside the oil sector. The deficit on transfers widened, however; the deficit with the European Community increased by £0.2 billion.

Seasonally adjusted, the overall current account surplus was little changed at £0.9 billion in the second quarter after a surplus of £0.8 billion in the previous quarter.

The world current account discrepancy

Description and analysis of world balance of payments developments is being hindered by the marked widening of the world current account discrepancy. Bank estimates of the current account balances of the country groups for the first half of 1982 imply a negative discrepancy of $90 billion at an annual rate, compared with $48 billion for 1981 as a whole. This wider discrepancy continues into the future in most recent forecasts (eg those of the IMF and OECD, which show discrepancies for 1982 of –$76 billion and –$95 billion respectively).

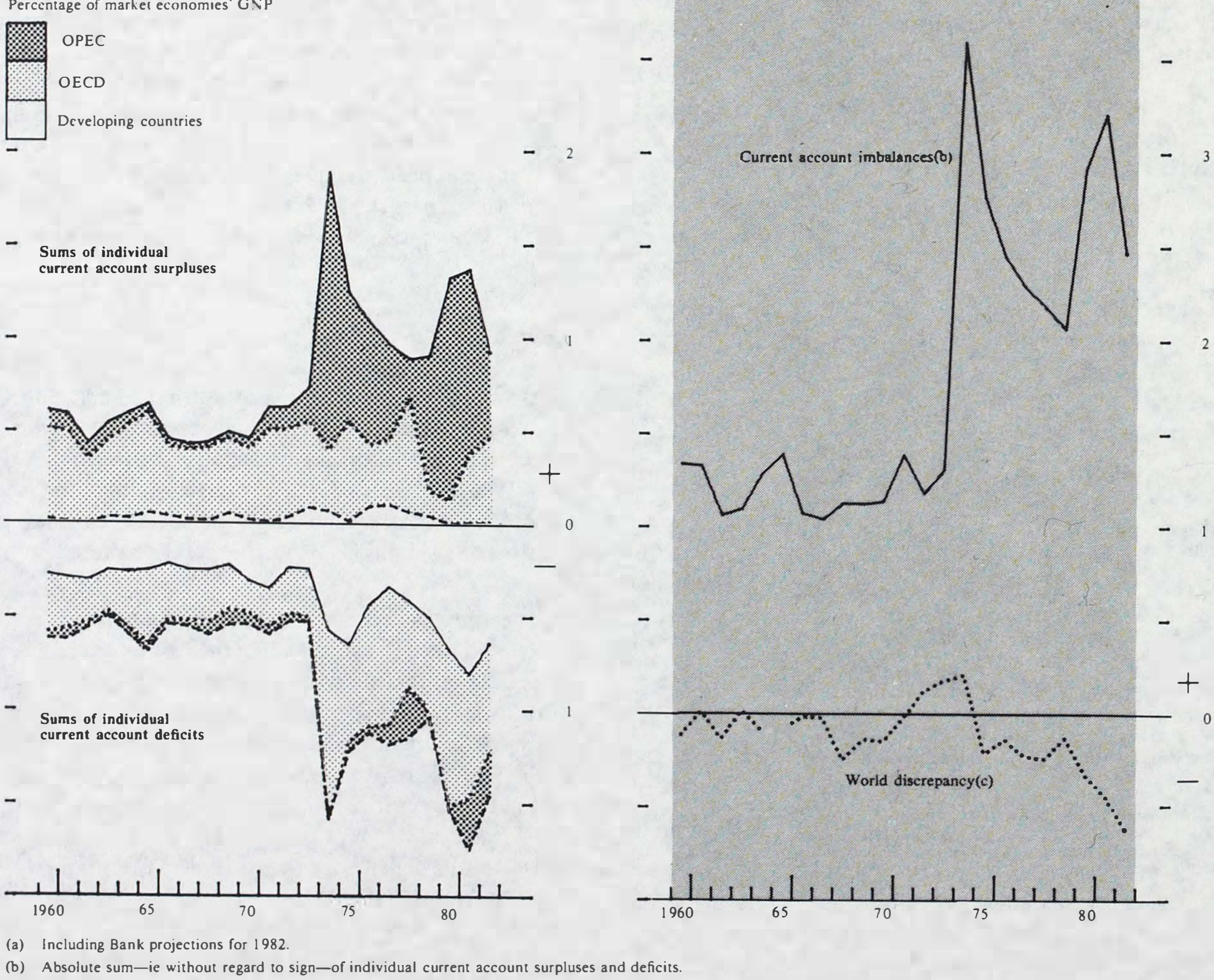
Perhaps surprisingly, this is a new problem. Although there has always been a statistical discrepancy in the aggregation of world current account data, it has generally been small enough not to cast doubt on the general pattern of balance of payments estimates. The discrepancy now, however (expressed as a proportion of world imports), is larger than at any time since at least 1950. The charts below show the pattern and distribution of current account imbalances since 1960, and incorporate projections for 1982, which highlight the apparently much more rapid decline in individual surpluses than deficits.

A recently published OECD study ('The world current account discrepancy', by Edwin Veil, *OECD Economic Outlook Occasional Studies*, June 1982) has indicated various possible sources of the discrepancy, and this can be used to derive some tentative estimates of the 'true' current account positions of the major country groups. Important sources of the discrepancy have traditionally included the asymmetric recording of reinvested earnings derived from foreign direct investments, and recording problems associated with exports of ships to, and the shipping earnings of, flags of convenience countries.

The rapid increase in the discrepancy during the past two years appears, however, to be largely related to two other factors. One is a marked decline in the 'normal' world surplus on trade, which arises when trade is growing because exports are recorded before imports. World trade has been particularly sluggish in the last two years; indeed, its dollar value fell in 1981. The second is an apparently systematic under-recording of investment income by financial asset holders, especially in oil exporting countries.

Rough allowance for these and other identifiable sources of error suggests that the aggregate current account position of OECD countries was probably some $11 billion better than recorded in 1981, and that of the oil exporters some $14 billion better.

The distribution of global current account balances, 1960–82[a]



(a) Including Bank projections for 1982.

(b) Absolute sum—ie without regard to sign—of individual current account surpluses and deficits.

(c) Sum of recorded surpluses and deficits (with regard to sign). Deviations from zero reflect measurement errors and omissions.

UK balance of payments

£ billions; *not seasonally adjusted*

	1981				1982	
	Q1	Q2	Q3	Q4	Q1	Q2
Current account	**2.4**	**1.5**	**0.5**(a)	**1.7**	**1.0**	**0.3**
Outward portfolio investment	-1.3	-1.0	-0.7	-1.1	-1.6	-1.1
Net direct investment (non-oil)	-1.5	-0.3	-1.2	-1.2	-0.5	-0.6
Banks' net external lending in foreign currencies	-0.6	-0.8	0.1	2.6	1.6	0.5
Banks' sterling lending overseas	-1.2	-0.4	-0.8	-0.5	-1.1	0.2
Sterling balances(b)	0.4	1.1	1.2	0.1	1.6	1.3
Other flows	0.2	-0.5	0.3	-0.2	-0.1	-0.3
Total identified capital flows	**-4.0**	**-1.9**	**-1.1**	**-0.3**	**-0.1**	—
Official financing	-0.3	0.2	0.7	0.1	—	0.7
Balancing item	1.8	0.2	-0.1	-1.6	-0.9	-1.0

(a) CSO estimate.

(b) Exchange reserves and other external banking and money market liabilities in sterling.

Identified net capital flows are at present estimated to have been flat in the second quarter, but information at this stage is incomplete: after including unidentified transactions, there was a net outflow of £1 billion which was matched by some official intervention in support of sterling and a modest current account surplus. Among identified capital flows, outward portfolio investment was over £1 billion: figures for the first half-year suggest no slackening in the pace of adjustment of portfolios in the wake of the abolition of exchange control. The latest quarter's figures provide further evidence of a reduction in direct investment outflows from the exceptional level in the latter part of last year. Banks' sterling lending overseas was lower in the second quarter with a reduction in acceptance lending after two quarters of strong growth. Heavy net external borrowing in foreign currencies by banks at the turn of the year subsided in the second quarter, partly because substantial net borrowing in foreign currencies by the UK private sector, which may have been to finance delayed tax payments, came to an end.

Developing countries

Borrowing by the developing countries from the international banking and capital markets was low early in 1981, partly for seasonal reasons. It revived strongly thereafter, especially in the Latin American countries.

Developing countries' balance of payments

$ billions; *not seasonally adjusted*

	1981					1982
	Year	Q1	Q2	Q3	Q4	Q1(a)
Current account	-77	-19	-18	-20	-20	-17
Capital account	73	15	15	21	22	14
Concessionary flows and other official flows	*19*	*4*	*5*	*5*	*5*	*5*
Direct investment	*10*	*2*	*2*	*3*	*3*	*3*
Capital market finance(b)	*45*	*5*	*10*	*12*	*18*	*4*
Other	*-1*	*4*	*-2*	*1*	*-4*	*2*
Official financing balance	-4	-4	-3	1	2	-3
financed by:						
Borrowing from IMF	*5*	—	*2*	*1*	*2*	*1*
SDR allocations	*1*	*1*	—	—	—	—
Reserves (increase -)	*-2*	*3*	*1*	*-2*	*-4*	*2*

(a) Forecasts and estimates

(b) Adjusted to exclude valuation effects.

Borrowing from the IMF doubled to nearly $5 billion in the year as a whole, despite the large number of IMF arrangements which were suspended in countries that failed to meet performance criteria. Reserves fell sharply in the first half of 1981, but then recovered as borrowing increased. Nevertheless, reserves throughout the year were equivalent to less than three months' imports, a lower proportion even than in 1975. Despite the narrowing of the current account deficit in the first quarter of 1982, reserves fell as new bank borrowing totalled only $3.1 billion compared to $16.9 billion in the previous quarter. This reduction in bank borrowing appears to be only partly explained by seasonal factors.

Oil exporting countries

Recent data for oil exporters' deposits with, and borrowing from, the BIS reporting banks serve to emphasise how small the net flow of funds from these countries to the international banks has been compared with their recorded current account surplus (which may itself be a significant underestimate of the true figure). Indeed, in the second half of last year, oil exporting countries, while still in substantial, if diminishing, surplus, were net borrowers of new funds from the international banks (see Table 13 in the statistical annex). Gross withdrawals of deposits by the non-Middle Eastern oil exporting countries (principally Venezuela, Nigeria and Indonesia) totalled $3.5 billion in 1981, and as much as $3.8 billion in the first quarter of 1982 alone.

In so far as oil exporters are financing the deterioration in their current balances in this way rather than through increased borrowing from the banks, they are contributing to a slowdown in the growth of international banking business on both sides of the balance sheet. But the growth of international banking business seems likely to be constrained rather more by debt servicing problems and concerns about banks' exposure than by short-term changes in the pattern of current account imbalances.

Deployment of oil money

In the first quarter of 1982, the surplus available for investment showed a further small decline, to $12 billion.

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

$ billions

	1980	1981		1982	
	Year	Year	H2	Q1	Q2(a)
Exports	309	281	132	61	54
Imports	136	158	83	42	42
Merchandise trade	173	123	49	19	12
Net invisibles	-61	-56	-28	-14	-15
of which, official transfers	*-4*	*-4*	*-2*	*-1*	*-1*
Current balance	**112**	**67**	**21**	**5**	-3
Net movements in external borrowing etc(b)	9	4	11	7	..
Surplus available for investment	**121**	**71**	**32**	**12**	..

.. not available.

(a) Provisional.

(b) For definitions, see footnote (a) to following table.

Identified deployment of oil exporters' surpluses[a]

$ billions

	1980	1981		1982	
	Year	Year	H2	Q1	Q2(b)
United Kingdom:					
Sterling bank deposits	1.4	0.5	-0.1	0.5	0.2
Eurocurrency bank deposits	14.8	7.9	3.0	-0.9	-5.5
British government stocks	1.9	1.0	0.4	0.1	0.2
Treasury bills	- 0.1	—	-0.2	-0.1	—
Other sterling placements	0.1	0.2	—	-0.1	-0.1
Other foreign currency placements	- 0.5	- 0.6	-0.1	—	—
	17.6	9.0	3.0	-0.5	-5.2
United States:					
Bank deposits	- 1.1	- 2.1	-1.5	1.5	4.9
Treasury bonds and notes	8.2	10.9	5.4	2.6	2.7
Treasury bills	1.4	- 0.6	-0.7	0.8	-1.5
Other portfolio investment	4.7	4.6	1.9	0.1	0.3
Other	0.9	3.3	3.6	—	..
	14.1	16.1	8.7	5.0	6.4
Bank deposits in other industrialised countries	26.2	- 2.6	-4.5	-2.0	..
Other investment in other industrialised countries(c)	17.0	21.7	8.4	1.0	..
IMF and IBRD(d)	4.9	2.5	1.2	0.6	..
Loans to developing countries	6.7	7.2	3.2	1.2	..
Total identified deployed net cash surplus	**86.5**	**53.9**	**20.0**	**5.3**	..
Residual of unidentified items(e)	34.5	17.1	12.0	6.7	..
Total net cash surplus derived from current account (as shown in the previous table)	**121**	**71**	**32**	**12**	..

.. not available.

(a) The additional notes to Table 16.1 in the statistical annex in the March *Bulletin* give a list of oil exporting countries. This table excludes liabilities arising from net borrowings and inward direct investment and also, on the assets side, changes in credit given for oil exports. These items are shown as net movements in external borrowing etc, in the previous table.

(b) Provisional.

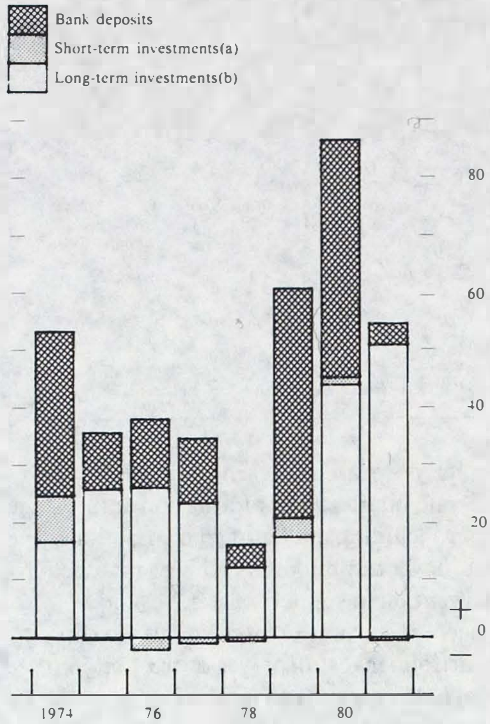
(c) Mainly loans and holdings of equities.

(d) Includes holdings of gold.

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

Identified disposition of oil exporters' surpluses

$ billions



(a) Short-term investments comprise UK and US Treasury bills.

(b) Long-term investments comprise other placements in the public and private sectors, and loans to developing countries and international organisations.

Identified investments totalled $5 billion, over half of which was placed in US government securities. Bank deposits in industrialised countries fell by about $1 billion.

In the second quarter, there were new placements in the United States and withdrawals from the United Kingdom reflecting a transfer of Venezuelan bank deposits between the two financial centres during the Falklands crisis.

The chart shows the identified disposition of oil exporters' surpluses during the years 1974–81, distinguishing bank deposits, short and long-term investments. Changes in the size of the identified deployed surplus have tended to be reflected first in bank deposits. In 1974, over 50% of the large surplus was placed with banks. The proportion then stabilised around 30% in the following four years, despite the markedly smaller surplus in 1978.

In 1979, nearly 70% of a much larger surplus went into bank deposits, and in 1981—when oil exporters' current account positions were deteriorating—the proportion declined to only 7%. Despite the decline in the surplus, long-term investments in that year were over $50 billion.

International banking and eurocurrency markets[1]

International developments (first quarter of 1982)

Outstanding lending by banks in the main financial centres[2] to non-residents grew by $39 billion in the first quarter of 1982. This rise represented a slower rate of growth than that in the fourth quarter of 1981 (+$115 billion). The slowdown reflected largely the unwinding of end-year positions, but the increase was only half as much as in the first quarter of 1981, suggesting that other factors may also have been responsible. During the year to end-March 1982, lending rose by 19%, rather less than the growth rate which has prevailed in recent years. Lending, excluding inter-bank transactions, grew by only $20 billion in the first quarter of 1982—a slower rate than during any quarter in 1981—and recent indications that banks are becoming more selective in their lending support the tentative conclusion that the first quarter could mark the beginning of a period of slower market growth.

The slowdown in international bank lending was greatest for banks in the European area whose external foreign currency assets grew by less than $5 billion. Within this group, however, assets of UK banks grew by $16 billion, while those of banks in Italy and France fell—largely for seasonal reasons—by $10 billion and $3 billion respectively.

(1) All transactions data in this section exclude the estimated effects of exchange rate fluctuations and hence may not correspond with the differences between amounts outstanding.

(2) Including estimates for offshore banks which do not contribute to the BIS quarterly statistics.

External business of banks in the BIS reporting area and offshore centres[(a)]

$ billions; changes exclude estimated exchange rate effects

	1981 Q1	1981 Year	1982 Q1	Outstanding end-March 1982
Deposits from non-residents				
Total	**+ 55**	**+299**	**+ 39**	**1,764**
Placed with banks in:				
Reporting European area	+ 28	+128	+ 3	991
of which, United Kingdom	*+ 23*	*+ 79*	*+ 19*	*459*
United States	− 6	+ 38	+ 27	203
Canada and Japan	+ 12	+ 40	+ 11	171
Offshore centres:				
US banks	+ 7	+ 33	− 2	174
Non-reporting banks	+ 14	+ 60	—	244
Source				
Outside reporting area				
Developed countries	—	+ 3	—	50
Eastern Europe	− 4	—	− 3	11
Oil exporting countries	+ 5	+ 3	− 1	152
Non-oil developing countries	− 1	+ 10	− 1	96
of which, Latin America	—	*+ 6*	—	*39*
Sub-total	—	+ 17	− 5	309
Inside reporting area(b)				
Banks(c)	+ 24	+158	+ 38	1,078
Non-banks	+ 10	+ 41	+ 2	113
Unallocated(d)	+ 21	+ 83	+ 4	264
Lending to non-residents				
Total	**+ 69**	**+329**	**+ 39**	**1,793**
Lent by banks in:				
Reporting European area	+ 32	+136	+ 5	976
of which, United Kingdom	*+ 26*	*+ 80*	*+ 16*	*441*
United States	+ 7	+ 76	+ 28	283
Canada and Japan	+ 9	+ 24	+ 9	129
Offshore centres:				
US banks	+ 6	+ 32	− 3	168
Non-reporting banks	+ 15	+ 61	—	236
Direction				
Outside reporting area				
Developed countries	+ 4	+ 17	+ 5	101
Eastern Europe	+ 1	+ 5	− 3	56
Oil exporting countries	− 2	+ 4	+ 1	72
Non-oil developing countries	+ 5	+ 42	+ 3	230
of which, Latin America	*+ 5*	*+ 33*	*+ 4*	*162*
Sub-total	+ 8	+ 68	+ 6	459
Inside reporting area(b)				
Banks	+ 33	+152	+ 26	920
Non-banks	+ 7	+ 31	+ 1	149
Unallocated(d)	+ 21	+ 78	+ 6	265

Source: Bank for International Settlements.

.. not available.

(a) The coverage of this table is as in Table 13 in the statistical annex plus an estimate for non-reporting banks in certain offshore centres (those listed in footnote (b) to Table 13 plus Bahrain and the Netherlands Antilles). A longer run of figures was provided in an article in the March *Bulletin*.

(b) Includes business with the offshore centres: the split between banks and non-banks is partly estimated.

(c) Includes liabilities to banks' trustee accounts (which may originate from non-banks).

(d) Mainly the positions of non-reporting banks in offshore centres.

Over 70% ($28 billion) of the growth in lending in the March quarter was accounted for by business channelled through the International Banking Facilities (IBFs) in the USA. Lending by banks in the United States other than IBFs ($0.3 billion) and by US banks' offshore branches ($3.5 billion) fell, suggesting that some of the increased IBF business reflected a change of location of existing loans; lending by banks in Europe may also have been affected to some extent.

New borrowing by non-oil developing countries was lower at $3 billion than seasonal factors alone would suggest; Latin American countries absorbed $4 billion of new funds, with other countries in this group reducing their outstanding borrowing by just over $1 billion. Despite some drawing on deposits by the developing countries, the net supply of funds to them from the international banking system was smaller than during any quarter in 1981. Eastern European countries were modest net takers of new funds in the March quarter, after being suppliers in the previous quarter; for although the banks reduced their lending to Eastern Europe, these countries drew down their deposits even more.

Oil producing countries once again increased their borrowing while at the same time reducing deposits, although to a lesser extent than in the previous two quarters.

Eurosterling

In the first quarter of 1982, the market declined slightly in size, but UK banks' lending to, and borrowing from, the market showed a small increase.

Eurosterling market[(a)]

£ billions

	1980 31 Dec.	1981 31 Mar.	1981 30 June	1981 30 Sept.(b)	1981 31 Dec.	1982 31 Mar.
Deposits by:						
UK banks	2.6	3.0	3.2	3.3	3.3	3.6
UK non-banks	1.1	1.0	1.0	1.0	1.0	0.9
Other Western Europe	5.1	4.9	4.5	5.4	5.5	5.6
Oil exporting countries	1.0	1.0	1.0	1.0	0.8	0.9
Other	1.5	1.5	1.4	1.5	1.7	1.2
Total	**11.3**	**11.4**	**11.1**	**12.2**	**12.3**	**12.2**
Of which, CMIs	*0.9*	*0.8*	*0.7*	*0.7*	*0.6*	*0.4*
Lending to:						
UK banks	2.3	2.6	3.0	3.2	3.4	3.6
UK non-banks	0.7	0.7	0.6	0.7	0.7	0.6
Other Western Europe	3.7	3.7	3.9	5.3	5.0	5.1
Other	0.6	0.7	1.1	1.4	1.2	0.9
Total	**7.3**	**7.7**	**8.6**	**10.6**	**10.3**	**10.2**

Source: Bank for International Settlements.

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

(b) From 30 September 1981 the coverage improved, resulting in an increase of around £0.8 billion in both liabilities and assets *vis-à-vis* 'Other Western Europe' at that date.

BIS half-yearly maturity analysis of lending to individual countries (second half of 1981)[(1)]

The analysis for the six months to end-December 1981 showed that international bank lending to countries outside the BIS reporting area grew by $46 billion compared to $32 billion in the first half of 1981. The stronger growth in the second half may be due to seasonal factors rather than any underlying rise in bank lending. The overall maturity profile continued to show a concentration of lending at the short end of the market; claims with a remaining maturity of one year or less accounted for 47% of the total compared to 45.5% a year earlier. Undisbursed credit commitments expressed as a percentage of total claims fell from 23.3% to 21%.

(1) The major part of the UK contribution to the half-yearly analysis, which sets out by maturity the claims of banks in the Group of Ten countries, Austria, Denmark, the Republic of Ireland and Switzerland, and a number of their affiliates domiciled in other countries, is contained in Table 14.3 in the statistical annex.

At end-June 1981, 54% of outstanding lending to countries in Latin America had a remaining maturity of two years or less; this increased during the period to over 55% (Mexico from 54.5% to 57.0%).

Lending to countries in Eastern Europe reflected the general trend of shortening maturities. The hardening in lenders' attitudes may also have been reflected in the decrease in undisbursed credit commitments as countries (especially Poland) drew on credit lines which were not replaced.

London market (second quarter 1982)

Foreign currency

In the second quarter of 1982, the London eurocurrency market, as measured by gross foreign currency liabilities of UK banks, fell by $18 billion. A reduction, probably seasonal, in Japanese banks' activity in the London inter-bank market accounted for three-quarters of this decline. Furthermore, uncertainties—subsequently clarified—about the Budget proposal to change the basis of giving double taxation relief to banks in respect of their overseas lending may have led to a temporary slowing in new business. Summary figures up to mid-August indicate some renewed growth.

UK banks' foreign currency liabilities and assets by customer(a)

$ billions

	1981				1982	
	30 June	30 Sept.	31 Dec.		31 Mar.	30 June
Foreign currency liabilities of UK banks to:						
Other UK banks	129.0	139.4	141.3	143.1	158.6	141.0
Other UK residents	16.6	19.8	18.4	19.2	18.8	19.9
Overseas central monetary institutions	54.3	53.0	53.1	53.4	51.0	48.1
Other banks overseas	238.6	249.8	266.6	270.2	282.7	284.0
Other non-residents	75.9	86.2	94.8	93.3	94.0	89.8
Other liabilities(b)	3.6	3.9	3.4	10.4	10.3	9.9
Total liabilities	**518.0**	**552.1**	**577.6**	**589.6**	**615.4**	**592.8**
Foreign currency assets of UK banks with:						
Other UK banks	127.1	137.5	135.2	140.4	156.5	138.3
Other UK residents	21.2	22.8	27.0	23.6	24.6	25.4
Banks overseas	264.1	277.4	291.3	293.7	301.8	294.9
Other non-residents	96.2	105.3	113.0	114.2	114.1	115.5
Other assets(b)	8.8	9.6	11.4	17.9	17.9	18.3
Total assets	**517.4**	**552.6**	**577.9**	**589.8**	**614.9**	**592.4**

(a) The reporting population is broader than the UK monetary sector (see additional notes to Table 14.1). The split between 'UK banks' and 'Other UK residents' in the Table is consistent with this broader definition.

(b) Mainly capital and other internal funds on the liabilities side and investments on the assets side. Additional unallocated items are included from end-December 1981 for both assets and liabilities.

The net position of UK banks *vis-à-vis* other countries within the BIS reporting area remained static during the June quarter. However, within this group, the United States (+$4 billion) and Japan (+$2 billion) were net depositors of funds, while European countries increased their net borrowings by an equal amount. Outside the reporting area, oil exporting countries reduced their outstanding net deposits in London by $6 billion to a level only slightly higher than it had been two years earlier, principally owing to the large transfer of funds by Venezuela mentioned above (see page 358). Claims on non-oil developing countries fell by $1.3 billion. This was more than accounted for by a fall in claims on Argentina from $5.8 billion to $3.6 billion largely due to the transfer abroad by non-British banks of their loan books, probably to ensure continued receipt of debt service payments. UK banks' liabilities to Argentina fell by $0.5 billion reflecting the withdrawal of deposits before the freeze of 3 April on Argentine assets.

UK banks' net foreign currency liabilities and claims by country or area(a)

$ billions

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

	1981				1982	
	30 June	30 Sept.	31 Dec.		31 Mar.	30 June
BIS reporting area:						
European area	—	+ 3.2	+ 2.7	+ 1.8	+ 2.5	+ 8.8
Canada	+ 2.9	+ 3.0	+ 1.5	+ 1.5	+ 1.8	+ 1.7
Japan	+14.7	+15.2	+16.7	+16.6	+17.0	+14.9
United States	−26.2	−32.9	−34.5	−34.6	−41.0	−47.5
Offshore banking centres	+12.2	+12.2	+ 9.7	+ 9.5	+10.7	+ 6.1
Other Western Europe	+ 9.8	+10.1	+11.1	+11.6	+11.8	+12.0
Australia, New Zealand and South Africa	+ 4.4	+ 5.6	+ 6.5	+ 6.7	+ 7.5	+ 8.6
Eastern Europe	+11.6	+11.2	+11.5	+11.3	+10.2	+10.3
Oil exporting countries	−42.1	−44.2	−43.0	−42.8	−41.1	−34.5
Non-oil developing countries	+18.5	+21.5	+22.8	+22.5	+23.2	+22.0
Others(b)	−14.1	−12.6	−17.3	−15.1	−16.2	−17.5
Total	**− 8.3**	**− 7.7**	**−12.3**	**−11.0**	**−13.6**	**−15.1**

(a) Liabilities and claims are shown separately in Table 14.1 in the statistical annex.

(b) Includes international organisations and certain unallocated items.

The maturity analysis of UK banks' foreign currency claims and liabilities at mid-May 1982 is shown in Table 14.2 in the annex. The figures suggest that British banks' maturity mismatching remained stable between mid-February and mid-May: their short-term (up to six months) net liability position (expressed as a proportion of total claims) remained unchanged at 24.6%. The consortium banks' short-term net liability position increased from 42.7% to 45.9%.

Sterling

UK banks' sterling liabilities to overseas residents continued to grow strongly in the second quarter of 1982,

UK banks' external sterling liabilities and assets analysed by customer(a)

£ billions

	1981			1982	
	30 Sept.	31 Dec.		31 Mar.	30 June
UK banks' sterling liabilities to:					
Overseas central monetary institutions(b)	1.4	1.2	1.2	1.5	1.3
Other banks overseas	5.4	5.7	6.0	6.4	7.4
Other non-residents	7.1	7.2	7.4	8.2	8.7
Total liabilities	**13.9**	**14.1**	**14.6**	**16.1**	**17.4**
UK banks' sterling assets:					
Loans and advances to:					
Banks overseas	4.1	3.9	4.2	4.3	3.8
Other non-residents	1.8	1.6	1.7	2.0	2.4
Bills	5.0	5.1	5.0	5.2	5.2
Acceptances	0.6	1.5	1.5	2.1	1.9
Total assets	**11.6**	**12.1**	**12.5**	**13.6**	**13.4**

(a) The reporting population is broader than the UK monetary sector (see additional notes to Tables 16.1 and 16.2 in the March 1982 *Bulletin*).

(b) Includes international organisations.

increasing by £1.3 billion—slightly less than in the first quarter. Unlike the first quarter, most of the increase in the second quarter reflected deposits from banks overseas, though deposits from non-banks also continued to grow. After particularly strong growth in acceptance lending in the six months to March 1982, acceptances outstanding fell by £0.3 billion in the second quarter, leading to a similar fall in total sterling claims.

International capital markets

In the face of a changed environment accompanied by lower profitability, lenders are beginning to behave more cautiously; this may reduce their willingness to intermediate, and, in particular, to maintain the rate of new international lending of recent years. Rescheduling of debt by some major international borrowers and the failure of one or two minor banks have led to an atmosphere of uncertainty in international markets, even though the collapse of those banks was brought about mainly by internal weaknesses. Banks have also experienced increasing losses on domestic loans.

The present stagnation in the world economy has depressed commodity prices and constrained the growth of exports from developing countries. This, together with high international interest rates until recently, has increased the resources which deficit countries have had to devote to debt servicing; consequently, a greater degree of adjustment of domestic economic policies has been required than was planned when much of the debt was contracted. The recent decline in eurodollar interest rates (the six-month eurodollar rate fell from $15\frac{7}{8}\%$ at end-June to $12\frac{3}{16}\%$ at end-August) provided some relief, particularly to borrowers whose outstanding debts are at floating rates. It remains to be seen whether this alleviation is durable—it may be partly offset by depressed export growth.

Some deceleration in the rate of growth of international lending has been projected. The IMF recently forecast an increase this year of 16%–17% compared with 21% last year. It is not clear how official support for Mexico, the resumption of some lending to Hungary, and possibly reschedulings of debt by Argentina and Cuba, will affect market sentiment over the next few months. In judging individual creditworthiness lenders will need to differentiate between different classes of risk in order to minimize disruption to the international markets.

Mean spreads over LIBOR and mean maturities of public sector and state-guaranteed loans

	1980	1981	1982 Q1	1982 Q2
Means spreads over LIBOR				
Percentages				
Major OECD	0.56	0.49	0.49	0.53
Minor OECD	0.69	0.60	0.49	0.51
Developing countries	0.90	1.20	1.35	1.35
Mean maturities(a)				
Years				
Major OECD	8.0	7.5	6.7	7.3
Minor OECD	8.0	8.4	8.5	10.7(b)
Developing Countries	8.6	7.9	6.2	7.0

(a) Weighted by size of loans.
(b) This lengthening of maturity is attributable mainly to a large loan to a New Zealand borrower with an exceptionally long maturity.

Announced medium-term eurocurrency credits
Although the overall pace of gross new lending through the publicised medium-term eurocurrency credit and international bond markets taken together remains strong, the aggregate figures should be seen against the background of the problems being faced by a few individual borrowers.

Announced new medium-term eurocurrency credits(a)
$ billions

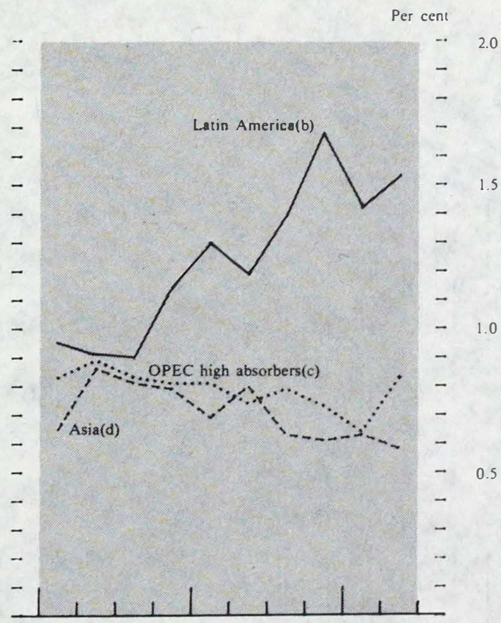
	1980	1981	1982 Q1	1982 Q2	1982 July	1982 Aug.
Total	**73.3**	**126.0(b)**	**21.7**	**21.6**	**7.7**	**4.4**
of which:						
OECD countries	*38.0*	*83.7(b)*	*11.0*	*10.2*	*4.4*	*1.9*
Developing countries	*24.6*	*33.7*	*8.3*	*10.1*	*1.7*	*1.3*

(a) Original maturities of three years and over.
(b) $41 billion of this total is related to takeover activity in North America.

In the first eight months of 1982, new credits were announced at much the same rate as in 1981 (after allowance for issues in 1981 related to takeover activity in North America). The aggregate statistics conceal distributional changes which have occurred over the last two months. Developing countries, which had been taking almost half (by value) of the market, took only around a quarter in July and August.

Of the Latin American countries, Argentina has not borrowed medium and long-term since the Falklands crisis;

Spreads paid by borrowers from developing countries(a)



(a) Loans with an original maturity of three years or more to public sector borrowers, sovereign borrowers, and those with a state guarantee.
(b) Excluding Venezuela.
(c) Indonesia, Venezuela, Nigeria and Algeria.
(d) Excluding Indonesia.

announced credits for Mexico were sharply lower in both June and July; and Brazil has also been borrowing less recently in the form of announced credits.

International bonds and notes

The value of international bond issues has been maintained at a high level this year ($17 billion per quarter since the fourth quarter of 1981, compared to below $9 billion per quarter on average over the previous three years). A marked increase in the pace of issuing activity has been evident since the fourth quarter of 1981, particularly in dollar securities between February and May as interest rates fell and there was widespread expectation of further falls. Demand for dollar paper, particularly from Swiss investors, was so strong during April that a number of highly rated US companies successfully placed issues yielding less than comparable US Treasury paper.

By mid-May, there were signs that investor demand had weakened, and this was underlined in June by the reception of Canada's jumbo issue of a record $750 million, at $14\frac{3}{8}\%$, and a change in US interest-rate expectations. Borrowing by US entities in the first half of 1982 totalled $9.5 billion compared to $7.1 billion in the whole of 1981. Heavy government borrowing in the US domestic bond market may have encouraged corporations to turn to other markets.

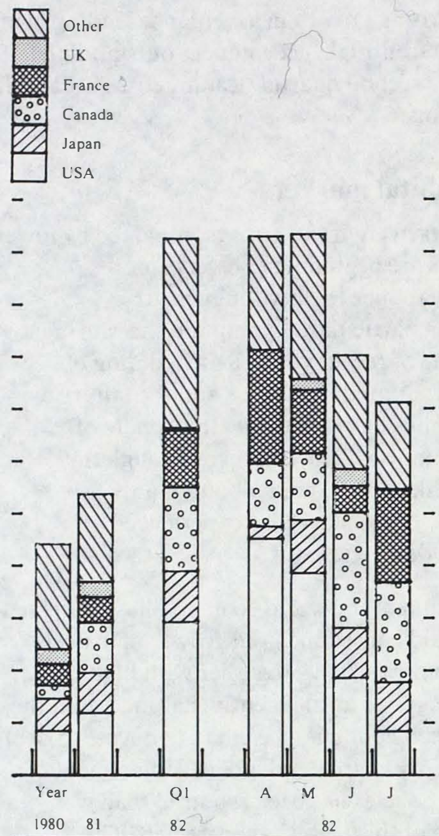
There is evidence of some resistance to issuers whose creditworthiness has weakened. Thus in July, Mexico paid record coupons ($18\frac{3}{8}$–$18\frac{1}{2}\%$) on two eurodollar bond issues. It is reported that these Mexican issues are being held, somewhat unusually, by banks, and that these holdings appear to be deliberate rather than the result of unsold underwriting commitments. Redemption options effectively give these bonds a three-year maturity. Banks may have begun to hold them not only because of the high return over the period but also in the expectation of more favourable treatment than lenders in syndicated loans in event of debt rescheduling.

The use of deals which include special features, some designed to reduce the cost of borrowing, or to mask it, continued. The option of speculating on a downward trend in interest rates (provided by issues bearing warrants to subscribe to further bonds) proved particularly popular during April and May. There were seventeen issues with warrants attached in the second quarter compared to four in the first. However, convertible issues declined following a weakening of the Japanese equity market. There were only three zero coupon bond issues in the second quarter because of continuing uncertainty surrounding the tax treatment of these bonds in some countries.

Though currency swaps have been used in the market for some time, during June and July a number of actual and prospective deals were announced whereby fixed rate debt is exchanged for floating rate debt, allowing the borrowers to benefit from market imperfections. There was also considerable growth throughout the first half of 1982 in the use of the ECU in the international markets, but the

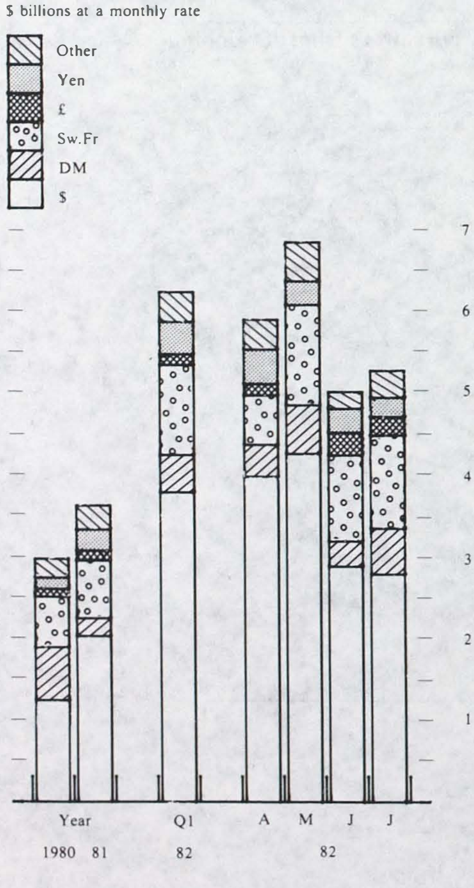
Euro and foreign bond issues, and floating rate notes: breakdown of major OECD borrowers by countries

$ billions at a monthly rate



Euro and foreign bond issues, and floating rate notes: currency analysis

$ billions at a monthly rate



unit still accounts for less than 1% of total publicised international bond and credit finance.

Foreign exchange and gold markets

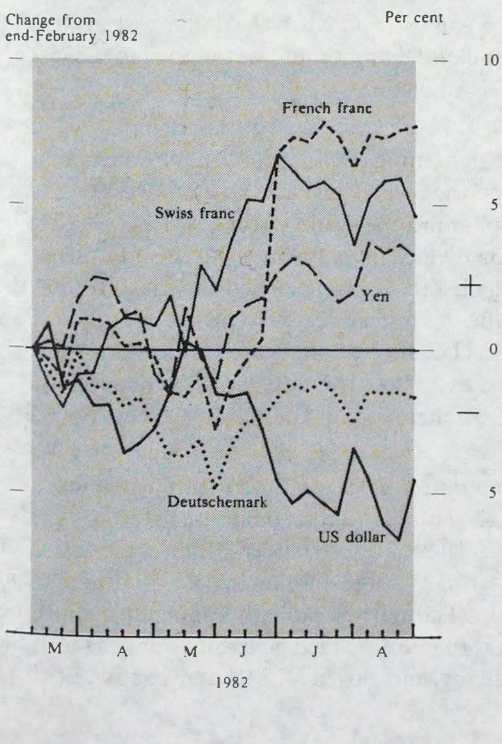
(End-May to end-August)

The foreign exchange markets began June much influenced by expectations of an imminent realignment of the currencies within the EMS and the continuing campaign to recapture the Falklands. By the middle of the month these matters had been resolved, and subsequent developments affecting US interest rates and the dollar once more became of central interest as the US currency rose to new heights in early July. Though US interest rates eased in July and August, the dollar continued to be strong.

Sterling

Sterling opened June at $1.7950, DM4.19$\frac{3}{4}$ and 90.2 in effective terms, and in the early part of the month was affected by news from the Falklands. Even though UK interest rates eased, sterling strengthened and had risen to 90.9 in effective terms by 9 June, despite declining against a strong dollar to $1.7759, partly boosted by encouraging wholesale price and trade figures. On 10 June, sterling fell to 90.4 in effective terms, $1.7635 and DM 4.25. The EMS was realigned over the weekend of 12/13 June, with the French franc and lira falling substantially and a small decline in the rates for the other EMS currencies. This caused sterling's effective index to rise sharply, to 91.5 on 14 June, and it reacted erratically to the news of the Argentine surrender, rising in the Far East on 15 June to $1.7805, and in London to an effective rate of 92.2. Subsequently heavy selling pressure developed and the rate closed at $1.7615 and 91.4, little changed from the previous day. Thereafter, it traded stably, and ended June at $1.7430, DM 4.27$\frac{1}{2}$ and 91.3 in effective terms.

Sterling against selected foreign currencies



Some encouraging economic news, including on retail prices, continued in July; sterling remained largely unchanged in effective terms, despite a further easing of UK interest rates, but reached a low against the dollar of $1.7035 on 7 July. Cuts in the clearing banks' rates, on 13 July and 30 July, appeared to have been discounted by the time of their announcement, and sterling closed July at $1.7405, DM 4.28 and 91.5.

In August, sterling continued to trade generally stably in effective terms, edging up on 25 August to its highest for a year, at 92.3, and against the continental currencies, as growth of the monetary aggregates continued within the target range and there was further good news on inflation and the balance of payments. Further cuts in banks' base rates on 17 August and 27 August again appeared to have been fully discounted. Against the volatile dollar, sterling fell to a five-year low of $1.6870 on 9 August. It subsequently fluctuated against the dollar, but was stable against the continental currencies and closed at DM 4.28$\frac{3}{4}$ and 91.7 on 27 August.

Official reserves

Borrowing under the exchange cover scheme brought in a net $151 million during June and July. The underlying change in reserves was $8 million.

Changes in UK official reserves

$ millions

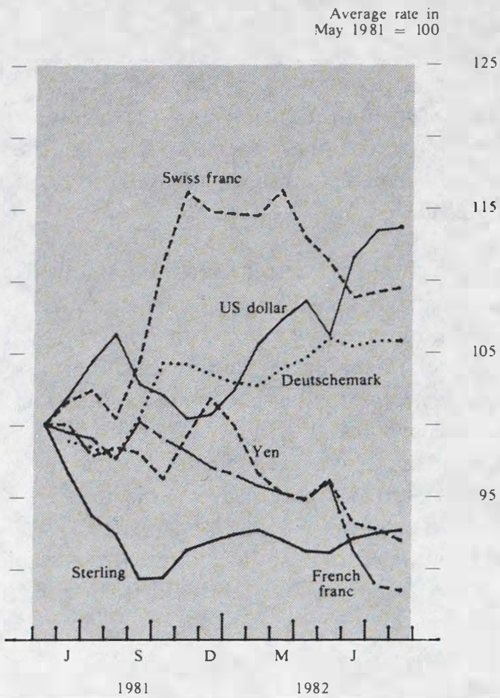
	1982 June	1982 July
IMF oil facility repayment	—	− 57
Other HMG capital repayments	− 13	—
EMCF swap valuation	—	+ 34
Exchange cover scheme:		
Borrowing	+ 73	+123
Repayments	− 26	− 19
Other (underlying changes in reserves)	−151	+159
Total change in reserves (including valuation change)	**−117**	**+240**
Level of reserves (end of period)	**17,703**	**17,943**

US dollar

US interest rates rose steadily for most of June, influenced in part by concern at a possible bulge in the money supply in July, and suggestions that the US economy might be moving out of recession. The dollar opened the month at DM 2.3387 and 115.4 and rose to DM 2.4095 and 117.2 by 10 June. The EMS realignment over the weekend of 12/13 June saw the dollar climb further—to DM 2.4200 and 118.7 by the close on 14 June. Rising interest rates in the second half of the month helped the US currency to continue to strengthen, and it touched DM 2.4875 and 121.8 by the close on 28 June before easing to end the month at DM 2.4525 and 120.5.

The dollar strengthened again in the first week of July to reach DM 2.5170 and 122.7 on 7 July. Subsequently, it seemed more likely that the money supply, despite the expected seasonal bulge, would not again move above its target range in the near term, and US interest rates eased back, the dollar falling with them to DM 2.4035 and 118.3 by the close on 23 July. Discount rate was reduced from 12% to 11$\frac{1}{2}$% on 20 July. However, towards the end of the

Indices of effective exchange rates



month, concern over the US Federal Government's funding programme increased, interest rates rose again slightly, and the dollar rose to DM 2.4590 and 120.5 by the close on 30 July.

The dollar continued to be strong in the first half of August as US interest rates stabilised following a further cut in discount rate, effective on 2 August. Record levels were achieved against a number of currencies, including the French franc and lira. Against the deutschemark, it reached a high of DM 2.5365. The announcement of a new set of tax measures contributed to a further fall in US interest rates and a dramatic surge in the bond market in mid-month; another contributory factor was market analysts' realisation that the economy was weaker than previously thought. Discount rate was again cut, on 16 August, and the dollar weakened, reaching a low of DM 2.4155 and an effective level of 118.5 on 25 August. Towards the end of the month, US interest rates edged up, although discount rate was again cut (on 27 August), and the dollar strengthened to DM 2.4640 and 120.4 in effective terms by 27 August, little changed over the month despite the substantial fall in US interest rates.

Other currencies

The EMS began June under considerable pressure, with the deutschemark exceeding −75 on its divergence indicator on a number of occasions. When the expected realignment took place during the weekend of 12/13 June, central rates of the French franc and the lira were devalued by 5.75% and 2.75%, respectively, and the deutschemark and Dutch guilder were both revalued by 4.25%. The Danish krone then rose to the top of the EMS, but was supplanted the following day by the French franc. The deutschemark fell to the bottom, where it was replaced towards the end of the month by the Dutch guilder. EMS currencies depreciated considerably against the dollar over the month.

During July, EMS currencies fluctuated, but ended little changed against the dollar. The deutschemark and Dutch guilder alternated at the bottom of the system, and the French franc, Danish krone and Irish pound took turns at the top. There was little pressure on the system.

These conditions continued for much of August. Towards the end of the month, the French franc came under pressure and slipped briefly to fourth in the narrow band. The Belgian discount and Lombard rates were cut to 13% and 14% respectively with effect from 19 August, and reductions in the German discount and Lombard rate (to 7% and 8%) and the Dutch discount rate (to 7%) were announced on 26 August.

The lira, which began June below the currencies in the narrow band, rose to almost three per cent above the deutschemark after the realignment. There was a limited relaxation of Italian exchange controls. In the first half of July, it strengthened further to over three and a half per cent above the deutschemark, but fell back in the second half of the month to trade nearer three per cent above the bottom currency of the narrow band.

The lira strengthened again early in August and traded some three and a half per cent above the deutschemark for the first half of the month. In the second half it eased back; discount rate was cut to 18% on 25 August, and by 27 August the lira was only about $2\frac{1}{2}$% above the deutschemark, which was at the bottom of the system.

Changes in the exchange rate of the yen against the dollar broadly reflected variations in interest differentials. The yen weakened against the dollar in June from ¥241.42 to ¥254.37 and fell to a low of ¥259.55 on 7 July, before recovering to ¥249.30 on 23 July. It dropped to ¥256.90 by the end of the month. On 17 August, it fell to a five-year low of ¥265.35. As the dollar weakened it strengthened to ¥250.40 on 25 August, and when the dollar rose again towards the end of the month, the yen slipped to ¥256.22 by the close on 27 August.

Despite some tightening of conditions in the domestic money market, the Swiss franc continued to weaken against the dollar in June, falling from Sw. Fcs 1.9880 to Sw. Fcs 2.0935 by the end of the month. The interest differential against the dollar widened early in July, and the franc fell further, to Sw. Fcs 2.1510, on 7 July. It then strengthened as US interest rates eased, and ended the month at Sw. Fcs 2.0860. It fluctuated only moderately against the deutschemark, and closed July at Sw. Fcs $0.84\frac{3}{4}$.

The dollar fluctuated in August, and the franc fell to a low of Sw. Fcs 2.1547 on 12 August, then rose to Sw. Fcs 2.0370 on 25 August, before falling again to Sw. Fcs 2.0860 on 27 August following cuts in discount and Lombard rates. Though occasionally edging up against the deutschemark, the franc traded generally stably against the German currency, and closed on 27 August at Sw. Fcs $0.84\frac{5}{8}$.

The Norwegian krone strengthened in effective terms in June even though it weakened against the dollar. In July, it fell both against the dollar and in effective terms. The Swedish krona, on the other hand, was stable in effective terms in June, despite depreciating against the dollar, and in July it strengthened in effective terms and, slightly, against the dollar.

In early August, there was a change in the weightings given to the currencies in the basket used by the Norwegian authorities. The krone was effectively devalued by around 3%, and closed on 27 August lower than at end-July both in effective and dollar terms. The Swedish krona eased back slightly against the dollar, but closed on 27 August unchanged in effective terms compared with end-July.

The Canadian dollar fell sharply against the US dollar early in June, reaching a low of Can $1.3032 on 23 June, before recovering substantially in late June and July, ending the period up both on the dollar and in effective terms. In August it continued to strengthen against the US dollar.

Gold

Gold fell further in the first half of June, to a new two-year low of $296.75 on 21 June. However, support emerged around this level, and, with only moderate producer selling, the price recovered to $317.50 by the end of the month. In July, the price moved in broadly opposite directions to the US dollar; it fell to $306.75 on 7 July as the dollar appreciated, it rose to $363.75 on 23 July as US interest rates and the dollar declined, and fell to $342.90 by the end of the month as the dollar rose again.

Gold traded stably in the first half of August, but rose sharply towards the end of the month, partly in response to lower interest rates, but also reflecting increased anxiety about the stability of the financial system. The price rose to $418 by the close on 27 August.

London gold price