DM/83/69

INTERNATIONAL MONETARY FUND

Treasurer's Department

Foreign Exchange and Financial Markets in August 1983

Prepared by Mark A. Lumsden and Nobumitsu Hayashi

Approved by Muhammad N. Bhuiyan

September 23, 1983

The main feature of foreign exchange market activity in August was a succession of large swings in the quotations of major currencies against the U.S. dollar. Trading conditions varied from quiet to hectic and were frequently nervous. Interest rate relativities favoring the dollar continued to be a principal factor influencing the market, moderated in part by coordinated central bank intervention in the first two weeks of the month; among other factors were concerns about the international debt situation and escalated fighting in Lebanon. Over the month as a whole, major currencies eased by 1.47-2.79 percent against the U.S. dollar, except for the Canadian dollar which was unchanged; the dollar firmed by 1.65 per cent in effective (MERM) terms and by 1.21 percent against the SDR (see Table 1). The intramonth variations were, however, substantially more marked (see Charts 1, 3, and 4). For example, the U.S. dollar firmed against the Deutsche mark by 3.16 per cent from the end of July to August 11, then reversed the course and eased by 4.05 percent up to August 23 before firming 2.54 percent again to the end of the month.

The strong rise in the dollar in the first two weeks of August was an extension of the trend since mid-June, influenced by the firming of short-term interest rates and fears of a tightening of U.S. monetary policy in reaction to the above-target M1 money supply growth. In this period most major U.S. banks raised their prime lending rate to 11 per cent from 10.5 percent in response to increases in their cost of funds. The dollar continued to firm despite concerted central bank intervention, estimated over the two weeks to be in the range of $2.5-4 billion. The U.S. Federal Reserve was active in the first week of the month for the first time since early October 1982; from July 29 to August 5 the Federal Reserve bought the equivalent of $182.6 million in Deutsche mark and $71.5 million in Japanese yen to counter market turbulence and restore an orderly two-way market. Consistent with this objective, the Federal Reserve offset its dollar sales on the exchange markets by cutting down the availability of Federal funds in the money market. The Bundesbank's intervention in the first two weeks of August, mostly sales of U.S. dollars for Deutsche mark, amounted to over $1 billion. The Deutsche mark appeared to have been especially vulnerable with the Bundesbank remaining reluctant to raise official interest rates despite above-target money stock growth. The Bundesbank's purchases of domestic currency, however, were used to help drain domestic liquidity. The Swiss National Bank's intervention amounted to several hundred million Swiss francs, comprising mainly purchases of Deutsche mark with U.S. dollars and Swiss francs. The Bank of Japan was also an active dollar seller while other somewhat less active participants in the coordinated intervention were the Bank of France, the Bank of Italy, and the National Bank of Austria.

Table 1. Changes in Exchange Rates in August 1983 1/

(In percent)

	Monthly exchange rate changes			
	Against U.S. dollar 2/	Against SDR	Effective exchange rate 3/ (In percent)	Change in effective exchange rate since August 1982 3/
Belgium	-2.39	-1.74	-1.01	-4.2
Denmark	-2.03	-1.36	-0.88	-2.8
France	-1.90	-1.32	-0.73	-7.7
Germany	-1.80	-1.31	+0.20	+0.8
Ireland	-2.40	-1.57	-1.17	-8.6
Italy	-2.79	-1.97	-1.44	-6.3
Netherlands	-2.00	-1.32	-0.68	-1.7
Austria	-2.13	-1.26	-0.80	-1.3
Canada	-0.00	+1.09	+0.76	+3.8
Japan	-1.91	-0.95	-1.03	+12.4
Norway	-1.47	-0.73	-0.28	-3.8
Sweden	-2.17	-1.56	-1.12	-16.9
Switzerland	-2.40	-1.89	-1.40	+3.1
United Kingdom	-1.72	-0.78	-0.20	-7.1
United States	--	+1.21	+1.65	+6.3

1/ Positive sign indicates appreciation of the currency.
2/ Based on New York noon quotations.
3/ Based on the Fund's multilateral exchange rate model (MERM).

A dramatic reversal in sentiment about the exchange rate for the U.S. dollar was sparked at the beginning of the third week of the month as lower than expected producer price inflation and money supply growth allayed fears about a further rise in U.S. interest rates. Central bank intervention subsided to relatively insignificant levels although there were reports of some dollar sales by the Bundesbank, the Netherlands Bank, the Bank of Japan, the Bank of Italy, the Bank of France, and the Swiss National Bank. Between August 11 and August 23 the dollar eased by 2.6 percent in effective (MERM) terms. The Deutsche mark was reported to have received special support vis-a-vis the U.S. dollar during this period from currency flows out of Swiss francs and Japanese yen into the German currency.

Attitude about the prospects for interest rates on U.S. dollar-denominated assets, however, reversed again starting from the time of the August 23-24 monthly U.S. Federal Open Market Committee Meeting on monetary policy, and the U.S. dollar resumed strengthening which continued through the end of the month; a modest but higher than expected rise in the U.S. consumer price index, a widening of the Federal budget deficit in July, estimates that the U.S. M1 money supply may surge in mid-September, the absence of policy tightening by the Bundesbank at its regular fortnightly meeting, Federal Reserve action to temporarily drain domestic liquidity to keep the Federal funds rate from dropping below 9 percent, a smaller than expected drop in the M1 money supply announced late in the month, uncertainties about the world debt situation, and intensified fighting in Lebanon were the contributory factors. Unlike in the first two weeks of August, central bank intervention to stem the rise of the dollar was only occasional and relatively light.

Within the EMS, the Belgian franc replaced the Deutsche mark in the first half of the month as the weakest currency in the narrow band of the parity grid (in the New York market) while the French franc replaced the Irish pound as the strongest currency toward the end of the month. The Belgian franc weakened mainly because of continuing internal political tensions and an unfavorable budget outlook. The National Bank of Belgium and the Central Bank of Ireland conducted relatively small sales of Irish pounds over the middle of the month until the French franc emerged as the strongest currency in the narrow band. In the New York market, the spread in the narrow band frequently exceeded the 2.25 percent maximum spread maintained in EMS member markets (see Charts 1 and 2). Against the U.S. dollar the EMS currencies eased by 1.80-2.79 percent over the month with the Deutsche mark weakening the least and the Italian lira weakening the most. The spread of the Italian lira from the weakest currency in the EMS narrowed from 5.80 percent to 5.21 percent (the lira is permitted a maximum margin of 6 percent in the exchange arrangements).

The variability of exchange rates increased considerably in August. As noted above, most major currencies displayed wide swings against the U.S. dollar and there were only eight trading days between the lows (on or about August 11) and the highs (on or about August 23) recorded for most currencies. Most EMS currencies (and the Austrian schilling) posted only slightly reduced trading ranges compared with July when these currencies eased persistently throughout the month. The trading range for the Canadian dollar against the U.S. dollar was unchanged and continued to be the narrowest among the major currencies. The range widened considerably for other major currencies, especially for the pound sterling. The average absolute daily percentage change in the quotations (MAC in Table 2) were markedly higher for most currencies. For the EMS currencies (and the Austrian schilling) this MAC measure increased sharply from about one third of a percentage point to about 0.55 percentage point while it increased less uniformly for for most other major currencies except the Canadian dollar.

Table 2. Intra-Month Variations of Exchange Rates of Major Currencies 1/

	August 2/		High-low spread in percent 3/		MAC 4/	
	High	Low	July	Aug.	July	Aug.
Belgium	52.735	54.665	4.1	3.7	0.33	0.56
Denmark	9.4845	9.8375	4.1	3.7	0.32	0.59
France	7.9190	8.2245	4.3	3.9	0.35	0.56
Germany	2.6280	2.7343	4.2	4.0	0.33	0.57
Ireland	1.2000	1.1554	3.8	3.9	0.35	0.58
Italy	1568.5	1618.5	4.0	3.2	0.32	0.53
Netherlands	2.9395	3.05625	4.0	4.0	0.33	0.57
Austria	18.4775	19.210	4.1	4.0	0.47	0.57
Canada	0.81344	0.80818	0.7	0.7	0.09	0.08
Japan	242.85	246.975	1.1	1.7	0.27	0.32
Norway	7.3790	7.5700	1.4	2.6	0.18	0.43
Sweden	7.7750	7.9615	1.6	2.4	0.18	0.41
Switzerland	2.13725	2.19475	1.8	2.7	0.35	0.46
United Kingdom	1.5311	1.4797	1.7	3.5	0.25	0.48

1/ Exchange rates against the U.S. dollar in the New York market.
2/ Domestic currency units per U.S. dollar except for the pound sterling, the Irish pound and the Canadian dollar, which are in U.S. dollars per domestic currency unit.
3/ Intra-month variation in percent.
4/ Monthly average of absolute daily changes in spot exchange rates in percentage terms.

Changes in gross foreign exchange reserves in August reflected mainly central bank intervention activities to moderate the rise of the U.S. dollar and international borrowings. Germany's reserve loss in the month was $1.5 billion while Japan's loss exceeded $500 million. France recorded a reserve gain in July and August of about $3 billion mainly because of receipt of the proceeds of the recent European Community ECU 4 billion borrowing. Switzerland's reserve gain was partly due to intervention activities. Ireland gained a small amount of reserves as its intervention was directed at supporting the Belgian franc in the EMS parity grid. Other EMS participants and Austria, whose currency has traded in alignment with EMS currencies in recent months, lost reserves.

Table 3. Foreign Exchange Reserves in August 1983 1/

(In millions of U.S. dollars)

	Reserve level	Change in August	Change over 12 months
Belgium	4,205	-237	+1,233
Denmark	2,833	-31	+1,106
France	18,864	+405	+6,898
Germany	36,714	-1,500	+620
Ireland	2,240	+74	-130
Italy	18,107	-472	+3,335
Netherlands	8,722	-222	+1,745
Austria	4,096	-186	-330
Canada	3,241	+60	+583
Japan	20,238	-510	-330
Norway	5,228	+170	-939
Sweden	2,836	-357	+10
Switzerland	12,532	+708	+525
United Kingdom	8,868	-147	-2,036
United States	6,657	-614	-2,393

1/ Includes ECU holdings but excludes gold, SDRs and reserve position in the Fund. Foreign exchange reserves are gross and include balances drawn on short-term swap agreements and the proceeds from other official borrowings.

I. Developments in the Spot Exchange Markets

The U.S. dollar continued to firm against other leading currencies in August but with considerable intra-month variability. The dollar firmed by 1.65 percent in effective (MERM) terms and by 1.21 percent against the SDR. From July 29 to August 5 the Federal Reserve bought $182.6 million in Deutsche mark and $71.5 million in Japanese yen to maintain orderly market conditions. Interest rate relativities played the most important role in the exchange market activity in August; in the United States rates remained high with the economic recovery continuing but with some signs of a slowing pace. The index of leading economic indicators rose 0.3 percent in July following an upward-revised increase of 1.9 percent in June. The civilian unemployment rate was unchanged in August at 9.5 percent. The index of industrial production, seasonally adjusted, rose 0.9 percent in August, the smallest rise in seven months, and was up 8.7 percent year-on-year. The growth of real GNP in the second quarter was revised upwards from 8.7 percent to a seasonally adjusted annual rate of 9.7 percent while the increase in the GNP price deflator was revised downwards to an annual rate of 3.3 percent from 4.5 percent. The budget deficit continued to widen; in July it was $21.4 billion compared with $19.8 billion a year earlier. The trade deficit also widened in July to $6.36 billion from $4.96 billion in June. Among more favorable developments, the producer price index in August rose a seasonally adjusted 0.4 percent and was up only 1.4 percent year-on-year.

The Deutsche mark continued at the bottom of the EMS parity grid in early August but following the coordinated central bank intervention its position in the narrow band improved and the Belgian franc took its place at the bottom of the grid. Bundesbank intervention in the first half of the month (mostly sales of U.S. dollars for Deutsche mark) was over $1 billion. The Deutsche mark eased the least among the EMS currencies against the U.S. dollar over the month as a whole (1.80 percent), and in effective (MERM) terms it firmed by 0.20 percent. The Finance Minister announced his intention to limit growth in nominal government spending to 1.8 percent next year, significantly lower than the projected real economic growth rate of 2.5 percent; in addition, net borrowing would be limited to DM 37 billion compared with about DM 40 billion expected this year. Real GNP in the second quarter rose a seasonally adjusted 1.5 percent following a 1 percent rise in the first quarter. The unemployment rate in August was unchanged from 8.9 percent in July. The index of industrial production in July declined 1.0 percent (from an upward-revised level in June) but was up 4.9 percent year-on-year. The current account in July swung into a deficit of DM 3.1 billion from a downward revised surplus of DM 403 million in June; the deficit in July 1982 was DM 1.9 billion. The wholesale price index in August increased by 0.8 percent but was up only 0.2 percent year-on-year while the producer price index rose 0.6 percent for a 1.3 percent year-on-year increase.

The French franc replaced the Irish pound as the strongest currency in the narrow band of the parity grid toward the end of August. The franc eased 1.90 percent against the U.S. dollar and 0.73 percent in effective (MERM) terms over the month. Real GNP in the second quarter rose only 0.2 percent after being unchanged in the first quarter, reflecting in part the austerity measures imposed to support the EMS currency realignment in March. The unemployment rate in August declined to 8.7 percent from 8.9 percent in July. The trade deficit, seasonally adjusted, narrowed sharply in August to F 400 million from F 3.0 billion in July; this was the slimmest deficit in more than 18 months. The wholesale price index was unchanged in July but was up 9 percent year-on-year.

The Belgian franc replaced the Deutsche mark as the weakest currency in the EMS during August because of internal political uncertainties and the prospect that the budget deficit will reach BF 500 billion (equivalent to 11.5 percent of GNP) next year. The Belgian franc eased by 2.39 percent against the U.S. dollar and 1.01 percent in effective (MERM) terms. During the middle part of the month, the National Bank of Belgium and the Central Bank of Ireland sold relatively small amounts of Irish pounds to support the Belgian franc. Pressure on the Belgian franc was not severe as the discount of the financial franc from the commercial franc widened somewhat but remained less than 1.0 percent. Industrial production in May fell 1.5 percent and was down 6.6 percent year-on-year. The unemployment rate at the end of August declined to 10.3 percent from 10.4 percent in mid-August to return to the same level as at end-July. The wholesale price index in July rose 0.3 percent and was up 3.0 percent year-on-year.

The Netherlands guilder eased 2.00 percent against the U.S. dollar and by 0.68 percent in effective (MERM) terms. Industrial production fell 14.4 percent in July because of seasonal factors but was up 1.1 percent from a year earlier. The number of persons unemployed, seasonally adjusted, rose 1.8 percent in August and the unemployment rate was 17.3 percent in July. The trade surplus narrowed to f. 400 million in July from f. 500 million in June, contrasted with a deficit of f. 500 million in July 1982. The producer price index for consumer and investment goods rose 0.3 percent in June and was up only 0.9 percent year-on-year.

The Danish krone eased by 2.03 percent against the U.S. dollar and by 0.88 percent in effective (MERM) terms. The 1984 budget envisages a reduced deficit of DKr 59 billion (equivalent to 10.9 percent of GNP) compared with an expected 1983 deficit of DKr 63 billion (equivalent to 12.4 percent of GNP). The unemployment rate, seasonally adjusted, declined to 10.6 percent in July from 10.7 percent in June. The trade deficit in July narrowed to DKr 290 million from DKr 1.0 billion in July 1982. The wholesale price index rose 1.0 percent in July and was up 4.5 percent year-on-year.

The Irish pound was the strongest currency in the narrow band of the EMS until it was replaced by the French franc late in the month. As noted earlier, in the middle part of the month the National Bank of Belgium and the Central Bank of Ireland undertook small sales of Irish pounds to support the Belgian franc. Over the month as a whole against the U.S. dollar, the Irish pound eased the most among the currencies in the EMS narrow band (2.40 percent) and it eased by 1.17 percent in effective (MERM) terms. The trade surplus in July, seasonally adjusted, widened to the equivalent of $34.8 million from the equivalent of $10 million in June, compared with a deficit in July 1982 equivalent to $72 million. The number of persons unemployed in August, seasonally adjusted, rose 0.6 percent and the unemployment rate was unofficially estimated at nearly 15 percent. The consumer price index rose 2.8 percent in the three months to August and was up 10 percent year-on-year.

The Italian lira continued to be the strongest currency in the EMS. Against the U.S. dollar, however, the lira eased the most among the EMS currencies (2.79 percent) and its margin over the weakest currency in the system slipped from 5.80 percent to 5.21 percent in terms of central rates expressed in ECU. In effective (MERM) terms the lira eased 1.44 percent. The unemployment rate in April rose to a record high of nearly 10 percent. Real GDP in the second quarter fell 1.7 percent and was down 3.6 percent year-on-year. The trade deficit in July narrowed to Lit 69 billion from Lit 426 billion in June and Lit 728 billion in July 1982. The wholesale price index rose 0.7 percent in July and was up 9.4 percent year-on-year.

For the first time since March this year, the pound sterling's value against the U.S. dollar moved generally parallel to those of other major currencies; the pound eased by 1.72 percent against the dollar and 0.20 percent in effective (MERM) terms. The pound weakened considerably on announcement that the current account, seasonally adjusted, swung into a deficit of £100 million in July from a surplus in June of £412 million. Later, however, the current account surplus for 1982 was revised upwards from £4 billion to £5.4 billion mostly because of increased estimates of foreign investment income, suggesting that the monthly estimates for 1983 have also been too low. Industrial production in July rose 2.1 percent and was up 2.5 percent year-on-year. The unemployment rate in August, seasonally adjusted, declined to 12.3 percent from 12.4 percent in July. The producer price index for manufactured products rose 0.2 percent in August for a 5.4 percent year-on-year rise.

The Swiss franc eased 2.40 percent against the U.S. dollar and 1.40 percent in effective (MERM) terms. Intervention by the Swiss National Bank (mostly sales of Swiss francs and U.S. dollars for Deutsche mark) early in the month was reported by the Bank to have amounted to several hundred million Swiss francs. The unemployment rate in August was unchanged at 0.8 percent. The trade deficit widened in August to Sw F 1.075 billion from Sw F 418.6 million in July and Sw F 780.6 million in August 1982. Wholesale prices rose 0.5 percent in August and were up only 0.8 percent year-on-year.

The Japanese yen eased 1.91 percent against the U.S. dollar and 1.03 percent in effective (MERM) terms. Real GNP in the second quarter rose 0.9 per cent following a rise of 0.2 percent in the first quarter. The unemployment rate in July declined to 2.5 percent from 2.6 percent in June. The current account surplus, seasonally adjusted, widened to $2.12 billion in July from $1.40 billion in June while in August the trade surplus widened to a seasonally adjusted $2.37 billion from $2.30 billion in July. The wholesale price index declined 0.2 percent in August and was down 2.9 percent from August 1982.

The Canadian dollar was essentially unchanged against the U.S. dollar in August but firmed by 0.76 percent in effective (MERM) terms reflecting favorable economic developments. Real GNP in the second quarter grew at an annual seasonally adjusted rate of 7.2 percent, led mainly by exports. The GNP deflator in the same quarter rose at an annual rate of 2.8 percent, an unchanged growth rate from the first quarter. The current account surplus in the second quarter, seasonally adjusted, widened to Can$1.1 billion from Can$253 million in the first quarter. The trade surplus in July, however, narrowed to a seasonally adjusted Can$1.40 billion from Can$1.53 billion in June. The unemployment rate declined in August to 11.8 percent from 12.0 percent in July. Industrial selling prices rose 0.4 percent in July for a 3.6 percent year-on-year rise.

The Austrian schilling eased by 2.13 percent against the U.S. dollar and 0.80 percent in effective (MERM) terms. The Norwegian krone eased by 1.47 percent against the U.S. dollar and 0.28 percent in effective (MERM) terms. The Swedish krona eased 2.17 percent against the U.S. dollar and 1.12 percent in effective (MERM) terms.

II. Monetary Developments, Forward Exchange Quotations and Covered Interest Differentials

Monetary and credit conditions in most major industrial countries in August were little changed from July although some pressures on the credit markets were evident in some countries. Short-term interest rates firmed moderately in France, Germany, Japan, the Netherlands, and the United States, while they eased in Switzerland and the United Kingdom.

In the United States, short-term interest rates continued to firm until the middle of August, attributed to the steady growth of the M1 measure of money supply and the consequent expectation of a credit-tightening by the Federal Reserve. On August 8, major banks raised their prime lending rates to 11 percent from 10.5 percent, the first such increase since February this year. The spread between the prime rate and the CD rate had narrowed sharply from 2.16 percent at the end of April to 0.50 percent on August 8. However, later in the month, the M1 measure of money supply recorded consecutive declines and with signs that the pace of economic recovery would not be as rapid as in the second quarter, interest rates tended to move lower. Over the month as a whole, the three-month bond equivalent yield on Treasury bills firmed from 9.59 percent at the end of July to 9.64 percent at the end of August. The 90-day CD rate firmed by 0.19 percentage point to 9.76 percent. Federal fund rates averaged at 9.44 percent in the last week of August, compared with 9.47 percent in the last week of July. As for money supply, M1 averaged $516.6 billion in August, up from $515.5 billion in July, and for the latest 13 weeks it rose at an annual rate of 10.9 percent from the preceding 13 weeks. M2 rose to $2.1362 trillion in August from $2.1254 trillion in July and M3 rose to $2.528 trillion from $2.510 trillion; the growth rates in all three categories fell within the target range of the Federal Reserve.

Among the countries in the European Monetary System, short-term interest rates in Germany continued to firm, attributed mainly to the rapid growth of the money supply and the influence of high U.S. interest rates. Germany's interest rates firmed until mid-August and eased later, broadly in line with the movement of the U.S. interest rates. The Bundesbank remained opposed to raising its lending rates so as not to dampen the sluggish economic recovery. The broadly defined money supply, M3, rose by DM 7.5 billion or 6.8 percent in July, compared with an increase of DM 15.5 billion or 9.2 percent in June. M2 increased by 2.9 percent in July (5.5 percent in June) and M1 increased by 10.6 percent (16.1 percent in June). In France, the Ministry of Economy, Finance and Budget announced reduction in the interest rate on savings deposits from 8.5 percent to 7.5 percent and that on five-year Treasury bills cut by one percentage point to 13 percent, effective August 1. However, the three-month interbank rate firmed by 0.26 percentage point during August to 12.55 percent. The National Bank of Belgium cut the interest rate on one- and two-month Treasury certificates by 0.25 percentage point to 8.75 percent and 9 percent, respectively; the interest rate on three-month certificates remained unchanged at 9.25 percent.

In the United Kingdom, sterling M3 rose by 0.2 percent in the banking month ended August 17, compared with rises of 0.8 percent in July and 1.7 percent in June. M1 rose by 0.9 percent in August after falling by 0.4 percent in July and Public Sector Liquidity 2 rose by 0.8 percent following a rise of 0.7 percent in July. Over the six months since mid-February 1983, sterling M3 grew at an annual rate of 12.4 percent, M1 at 14.3 percent, and PSL2 at 15.0 percent, compared with the target for each of the three categories of 7-11 percent annual increase during the 14 months from mid-February 1983 to mid-April 1984.

Table 4. Inflation Rates and Short-Term Interest Rates

	Month 2/	Inflation Rates 1/ (year-on-year percent changes) Wholesale price index		Consumer price index 3/		Short-term interest rates 4/ (end-of-month) July	Aug.
Austria	June/July	-1.5	(-3.0)	2.8	(2.5)	3.75	3.75
Belgium	July/Aug.	3.0	(3.1)	7.9	(7.5)	9.00	9.25
Canada	July			5.5	(5.6)	9.20	9.54
Denmark	July	4.5	(4.5)	6.2	(7.1)	7.50	7.50
France	July	9.0	(9.9)	9.4	(8.8)	12.29	12.55
Germany	Aug.	0.2	(-2.0)	3.0	(2.5)	5.68	5.88
Italy	July/Aug.	9.4	(10.3)	13.7	(15.4)	17.75	17.75
Japan	Aug./July	-2.9	(-2.4)	2.2	(2.0)	6.76	6.83
Netherlands	June/Aug.	0.9	(1.3)	2.6	(2.4)	5.54	6.31
Norway	Aug./July	5.7	(5.9)	7.9	(8.8)	8.00	8.00
Sweden	July	11.8	(11.7)	9.1	(8.8)	8.50	8.50
Switzerland	July/Aug.	0.1	(0.3)	1.7	(2.2)	4.88	4.50
United Kingdom	Aug.	5.4	(5.5)	4.6	(4.2)	9.72	9.53
United States	Aug./July	1.4	(1.4)	2.4	(2.6)	9.59	9.64

1/ Rates appearing in parentheses are those for the preceding month.

2/ In case of double entry (month/month), the first entry applies to the wholesale price index and the second entry applies to the consumer price index.

3/ Retail price index for France and the United Kingdom, and cost of living index for Germany and the Netherlands.

4/ Three-month rates are: Market yields on Treasury bills for the United States and the United Kingdom; Treasury bill rate for Canada; inter-bank rates for Germany, France, Italy, and the Netherlands; three-month euro-franc rate for Switzerland; discount rate on two-month private bills for Japan; central bank discount rates for Austria, Belgium, Denmark, Norway and Sweden.

In Japan, although short-term interest rates were little changed, real interest rates continued to firm. The Bank of Japan, however, left its discount rate unchanged because of concerns about the value of the yen on foreign exchange markets. Japan's broadly defined money supply, M2 and CDs, grew an average 7.1 percent in July from a year earlier, compared with 7.7 percent growth in June. M1 increased an average of 3.1 percent in July, down from 3.8 percent in June. M3 and CDs at the end of July was 9.2 percent above its level a year earlier, compared with 8.7 percent at the end of June.

In the euro-currency markets, the three-month euro-dollar interest rate firmed by 0.06 percentage point to 10.31 percent at the end of August. The uncovered interest differentials favoring euro-dollar investment narrowed for Germany, Japan, and the Netherlands but widened for the United Kingdom. Those favoring domestic investment widened for France but narrowed for Italy.

In the forward exchange market, the premia against the U.S. dollar widened for the pound sterling but narrowed for the Deutsche mark, the Japanese yen and the Netherlands guilder while the discount against the U.S. dollar widened for the French franc and the Italian lira. Consequently, the covered interest differentials favoring domestic investment narrowed for Germany, Italy, and Japan and remained unchanged for the Netherlands. Those favoring euro-dollar investment widened sharply for France and slightly for the United Kingdom.

Table 5. Covered Interest Differentials for Three-Month Investments (End-month)

	Uncovered interest differentials 1/ (1)		Forward exchange quotations 2/ (2)		Covered interest differentials 1/ (3) = (1)-(2)	
	July	Aug.	July	Aug.	July	Aug.
France	-2.04	-2.24	-3.62	-4.54	+1.58	+2.30
Germany	+4.57	+4.43	+5.42	+4.82	-0.85	-0.39
Italy	-7.50	-7.44	-5.96	-7.05	-1.54	-0.39
Japan	+3.49	+3.48	+3.76	+3.61	-0.27	-0.13
Netherlands	+4.71	+4.00	+4.84	+4.13	-0.13	-0.13
United Kingdom	+0.54	+0.78	+0.42	+0.59	+0.12	+0.19

1/ Positive sign indicates differential in favor of euro-dollar investment relative to domestic investment, while negative sign indicates the reverse. Domestic interest rates for France, Germany, Italy and the Netherlands are interbank rates. For Japan discount rate for two-month private bills is used and for the United Kingdom the Treasury bill rate is used.

2/ Positive sign indicates three-month forward premium of domestic currency against the U.S. dollar, while negative sign indicates forward discount.

III. Yields on the SDR and Other SDR-Denominated Assets

Beginning August 1, 1983, the SDR interest rate is being fixed weekly at the level of the combined domestic interest rate as of Friday of the preceding week in accordance with the revised Rule T-1. For the week beginning August 1, it was 8.81 percent, compared with 8.65 percent that was set for the calendar quarter beginning July 1 under the previous rules. The SDR interest rate in the second and the third week of August firmed to 8.96 percent and 9.03 percent, respectively, and then eased to 8.89 percent and 8.84 percent in the fourth and the fifth week, respectively. The rate of remuneration paid on creditor positions in the Fund (85 percent of the SDR interest rate) firmed to 7.51 percent in the last week of August from 7.35 percent in July.

Table 6. The SDR Interest Rate and the Rate of Remuneration 1/

	July	August				
		1	8	15	22	29
SDR interest rate	8.65	8.81	8.96	9.03	8.89	8.84
Rate of remuneration	7.35	7.49	7.62	7.68	7.56	7.51

1/ For July, the rates pertain to the month. From August 1, the rates pertain to the week beginning on the dates indicated above.

As shown in Appendix B, the average domestic interest rates on the instruments for the currencies included in the SDR basket firmed by 0.06-0.28 percentage point during August, except in the United Kingdom where they eased by 0.13 percentage point. As a result, the average combined market interest rates continued its firming trend since April, this year, and was 8.93 percent in August, 0.19 percentage point higher than in July.

The combined domestic interest rates for maturities ranging from three months to five years firmed by 0.17-0.32 percentage point from the end of July to the end of August, reflecting higher interest rates on the relevant instruments in the United States and in Germany which firmed by 0.20-0.47 percentage point and 0.25-0.38 percentage point, respectively, while they were mixed in the United Kingdom, France and Japan. The combined domestic rates display a rising yield curve which moves up from 8.90 percent on the three-month maturity through 9.26 percent and 9.71 percent on the six-and twelve-month maturities, respectively, to 10.93 percent on the five-year maturity.

The combined euro-currency interest rates for three, six, and twelve months continued to firm by 0.34, 0.25, and 0.24 percentage points, respectively, to 9.44 percent, 9.87 percent, and 10.18 percent at the end of August. This reflected higher euro-currency interest rates for most of the relevant currencies which firmed by 0.06-1.63 percentage point during August, partly offset by a slight decline in euro-sterling deposit rates which were 0.06-0.13 percentage point lower at the end of August than at the end of July.

Average interest rates on SDR-denominated deposits of selected commercial banks firmed by 0.21-0.30 percentage point at the end of August. The deposit rates displayed a rising yield curve moving up from 8.83 percent on one-month deposits through 9.26 percent and 9.65 percent on three- and six-month deposits, respectively, to 9.96 percent on twelve-month deposits. The yields on SDR-denominated bonds quoted on the Luxembourg Stock Exchange eased at the end of August. The current yield ranged from 8.88 percent to 11.47 percent, with the average current yield easing by 0.02 percentage point to 9.86 percent while the yield to maturity ranged from 10.52 percent to 11.77 percent with the average yield to maturity easing by 0.26 percentage point to 11.11 percent between the end of July and the end of August.

Table 7. Yields on Alternative SDR-Denominated Assets 1/

	July	August
Combined market interest rates 2/		
Based on domestic rates		
3-month maturity (Rule T-1)	8.73	8.90
6-month maturity	9.02	9.26
12-month maturity	9.39	9.71
5-year maturity	10.65	10.93
Based on euro-currency rates		
3-month maturity	9.10	9.44
6-month maturity	9.62	9.87
12 month maturity	9.94	10.18
Average commercial bank deposit rates 3/		
1-month deposits	8.56	8.83
3-month deposits	8.96	9.26
6-month deposits	9.44	9.65
12-month deposits	9.71	9.96
Bonds quoted on the Luxembourg Stock Exchange 4/		
Average current yield	9.88	9.86
Average yield to maturity	11.37	11.11

1/ Rates pertain to last Wednesday of the month.

2/ As of January 1, 1981, combined market rates (according to the Rule T-1) are calculated by multiplying the yields or rates of each of the respective instrument by the number of units of the corresponding currency listed in Rule O-1 and the value in terms of the SDR of a unit of that currency as determined by the Fund under Rule O-2(a) and (b). Domestic rates are those used to determine interest rates on the SDR or on borrowings by the Fund. Euro-currency rates are midpoint midmorning rates in London, and for sterling, in Paris.

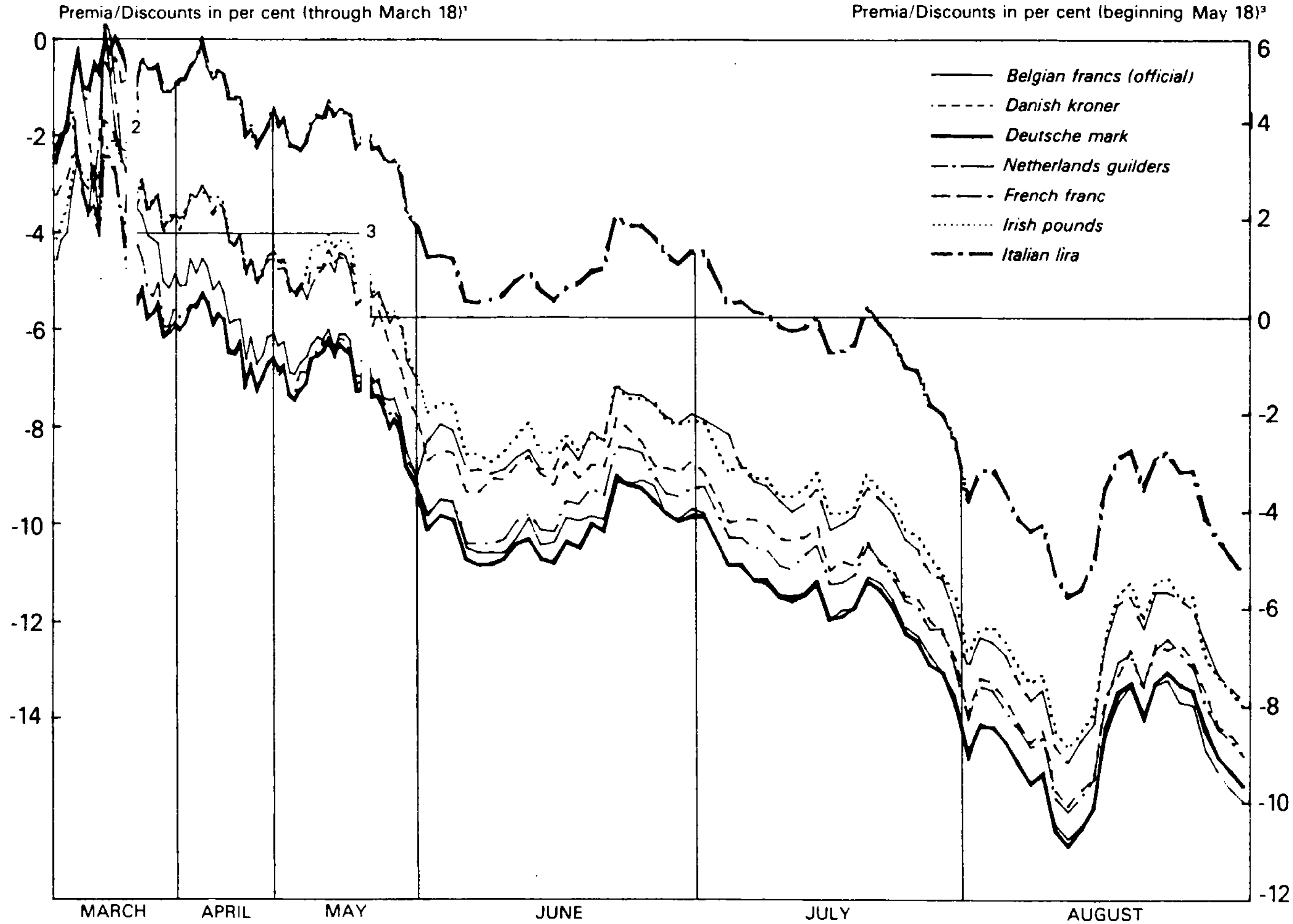
3/ Average of rates quoted by selected commercial banks.

4/ Maturity dates for these issues range from 1984 to 1989.

CHART 1

SPOT EXCHANGE RATES: EUROPEAN MONETARY SYSTEM

(Based on noon quotations in New York)



[1] Premia/discounts over declared ECU central rates converted to U.S. dollar terms on the basis of 1 ECU = $0.98 through March 18, 1983.

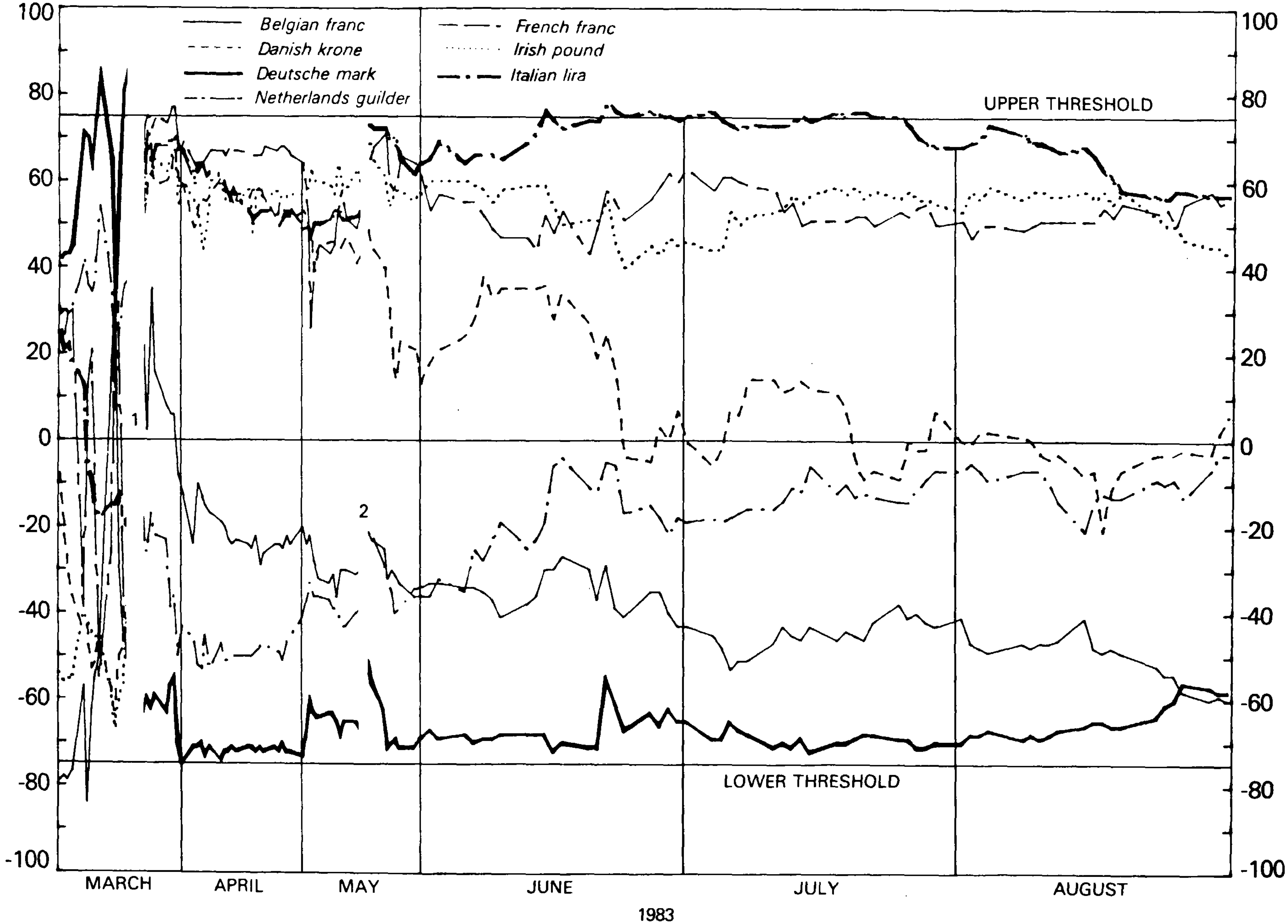
[2] Effective March 21, the Deutsche mark, the Netherlands guilder, the Danish krone, and the Belgian franc were revalued by 5.5, 3.5, 2.5, and 1.5 per cent, respectively, and the French franc, the Italian lira, and the Irish pound were devalued by 2.5, 2.5, and 3.5 per cent respectively. Consequently, the premia/discounts over declared ECU central rates are calculated on the basis of the rate as of March 22 of 1 ECU = $0.930217.

[3] Effective May 18 the central ECU rate of the pound sterling was appreciated and those of the other participants depreciated in connection with the Common Agricultural Policy. Premia/discounts over declared ECU central rates have been converted into U.S. dollar terms at the rate of 1 ECU = .920041.

CHART 2

EUROPEAN MONETARY SYSTEM: DIVERGENCE INDICATORS

(Based on noon quotations in London)



[1] Effective March 22, the Deutsche mark, the Netherland guilder, the Danish krone, and the Belgian franc were revalued by 5.5, 3.5, 2.5, and 1.5 per cent respectively, while the French franc, the Italian lira and the Irish pound were devalued by 2.5 per cent, 2.5 per cent, and 3.5 per cent respectively.

[2] Effective May 18 ECU central rate for the pound sterling was revalued by 7.3 per cent and those for the other participating currencies devalued a uniform 1.2 per cent in connection with the Common Agricultural Policy.

CHART 3

SPOT EXCHANGE RATES

(Noon quotations in New York)

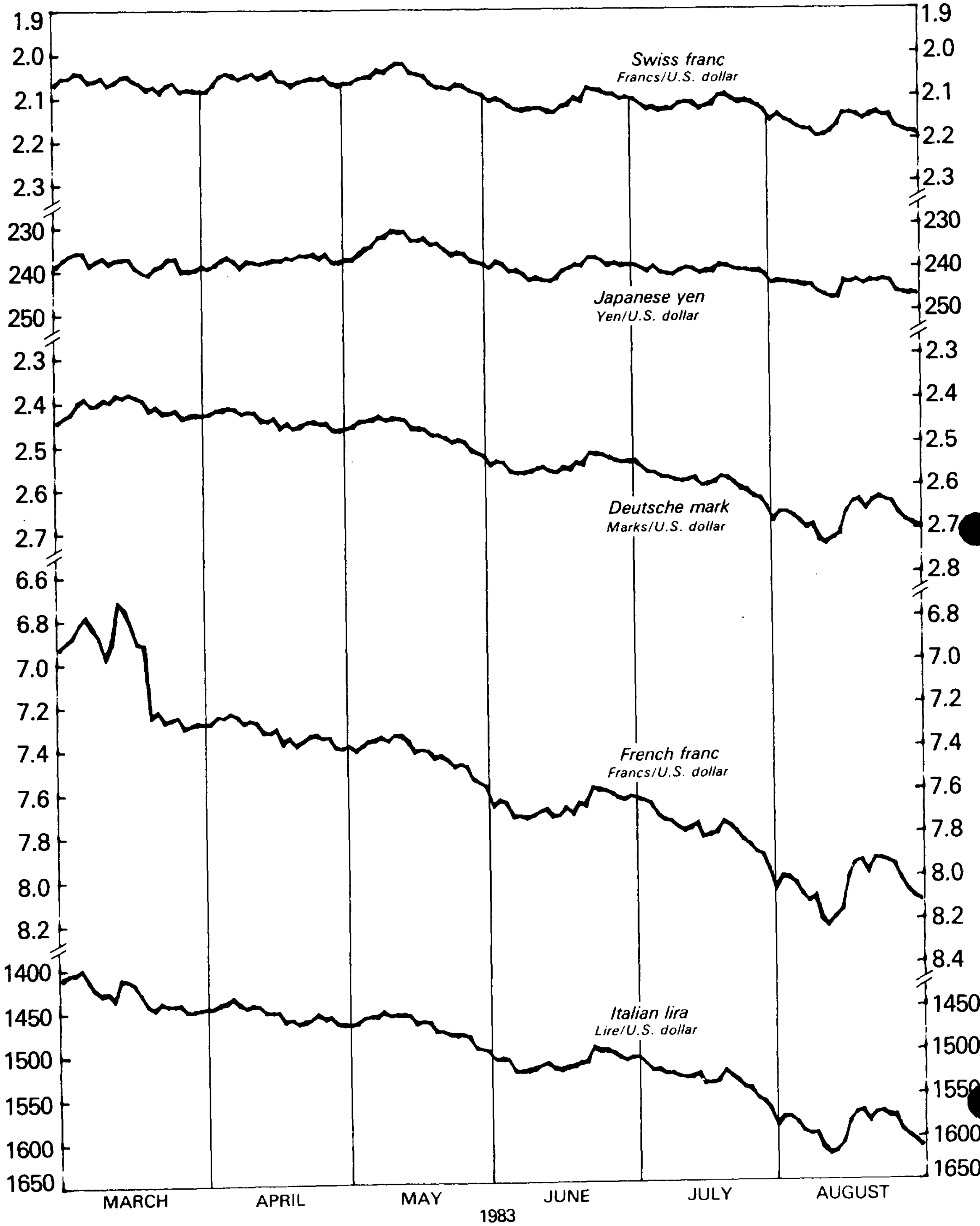


CHART 4

SPOT EXCHANGE RATES

(Noon quotations in New York)

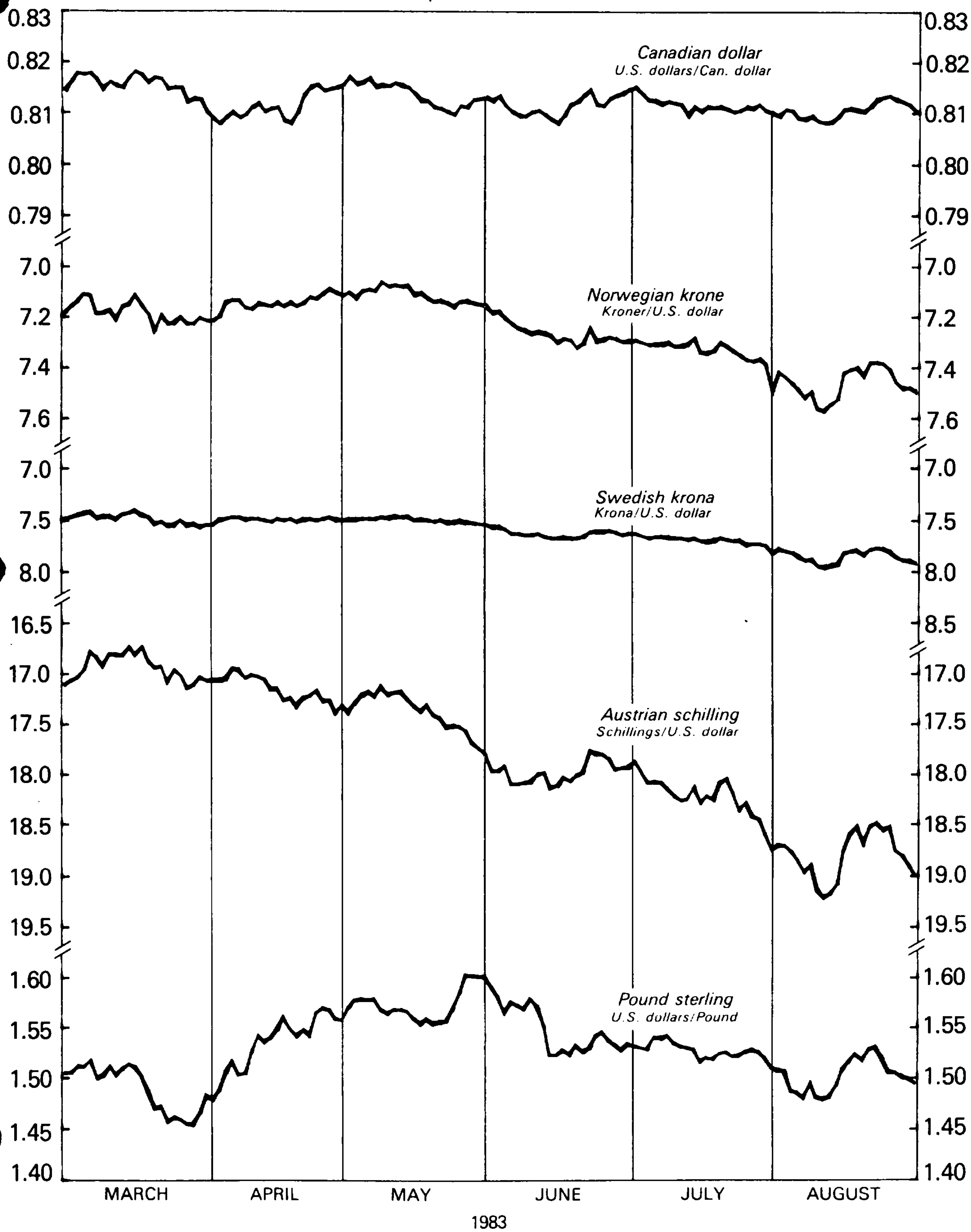
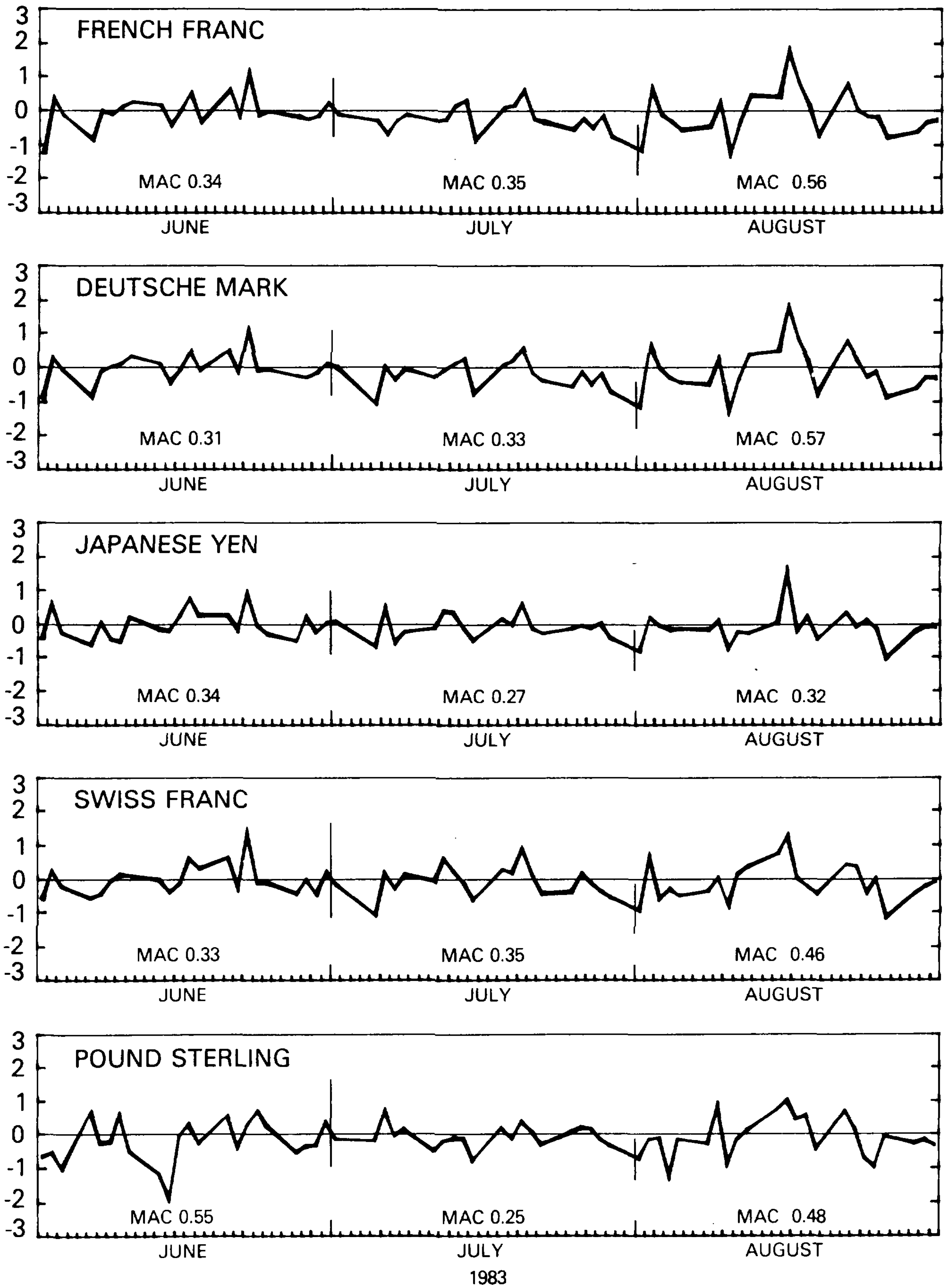


CHART 5

DAILY CHANGES IN SPOT EXCHANGE RATES

(In per cent against the U.S. dollar, based on noon quotations in New York)[1]



[1]Monthly averages of absolute changes (MAC) are also indicated.

CHART 6

INDEXES OF EXCHANGE RATES OF FIVE MAJOR CURRENCIES AGAINST THE SDR

JUN. 1974 - AUG. 1983

(June 28, 1974=100)

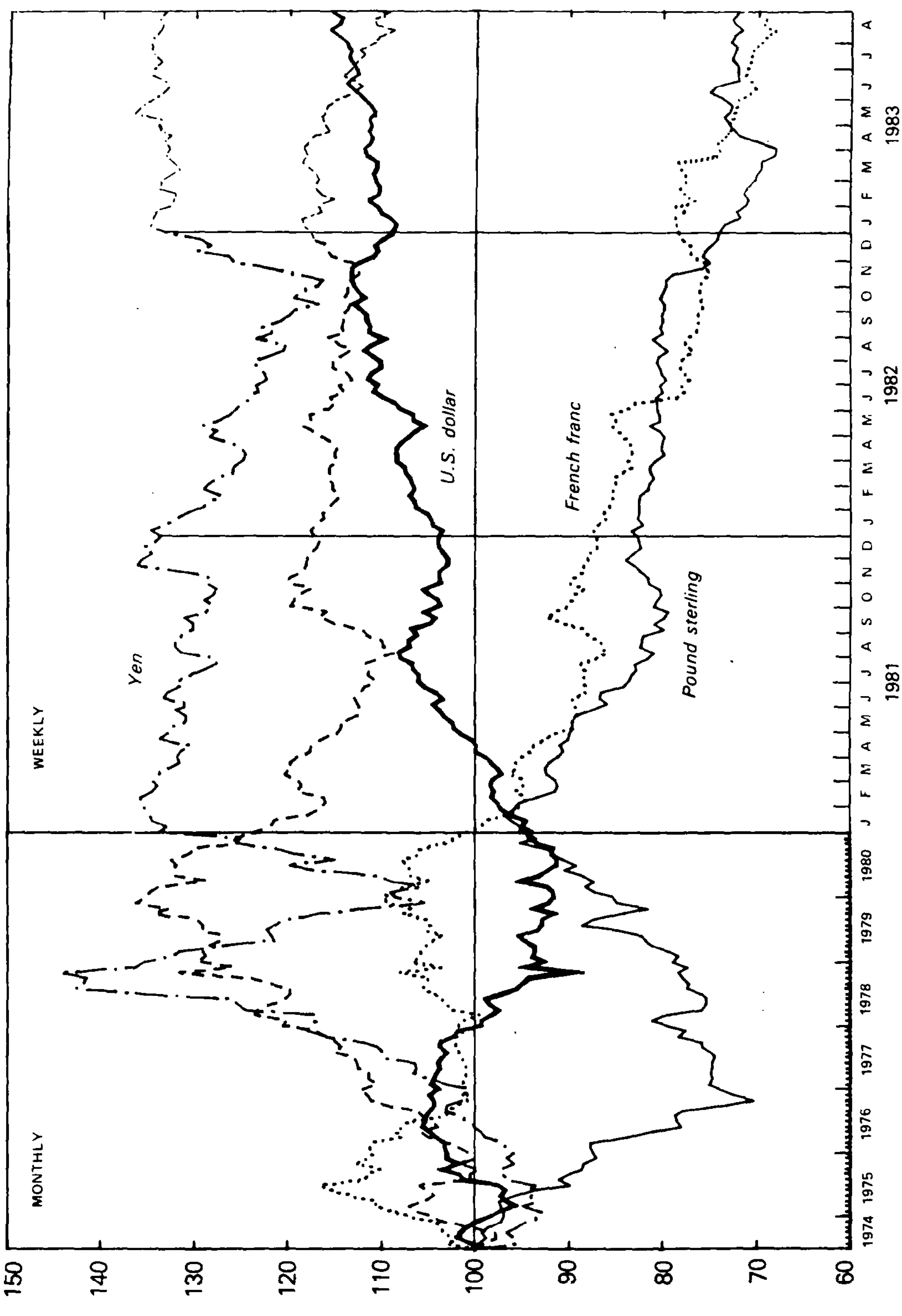
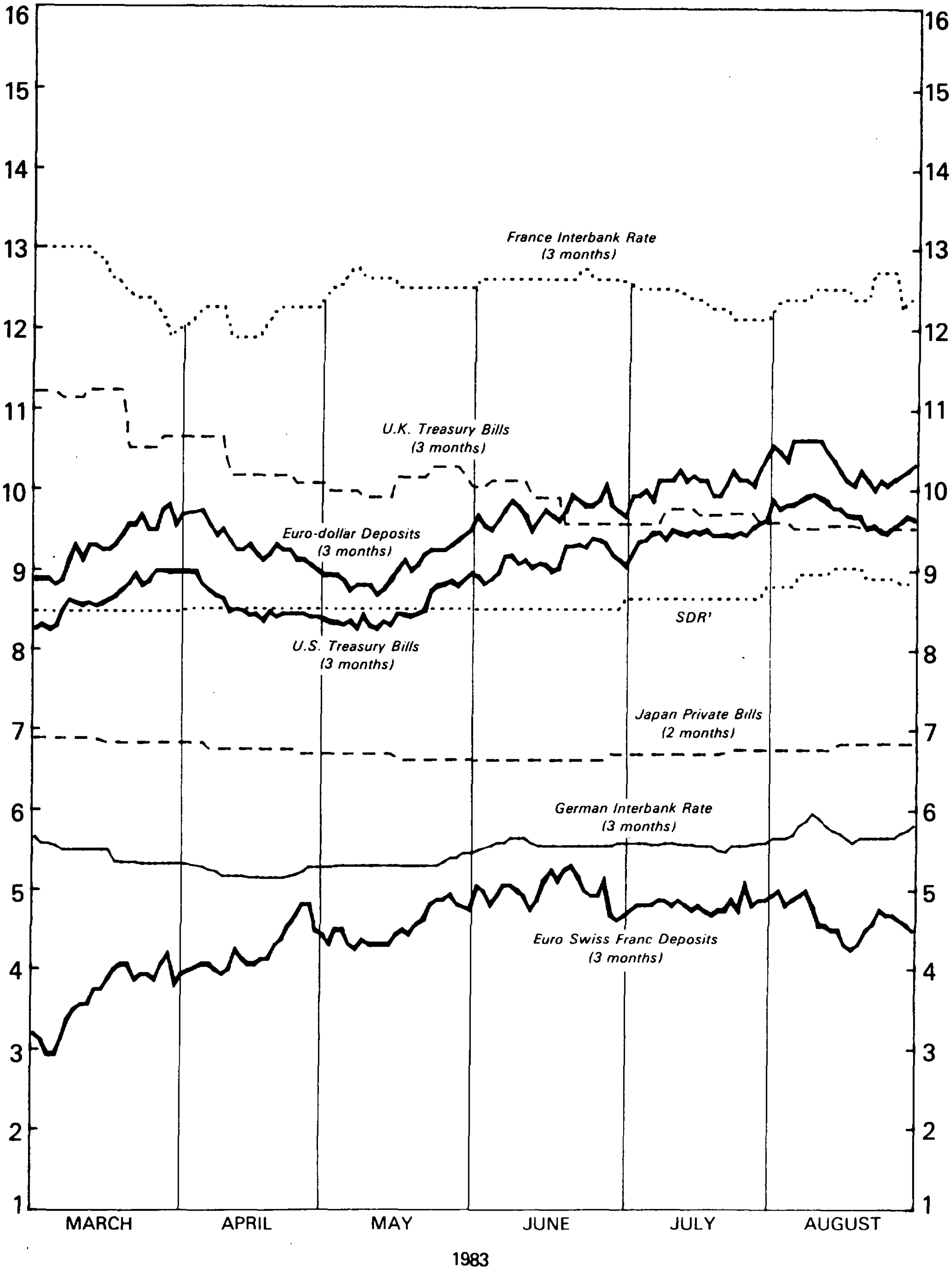


CHART 7

SHORT-TERM MONEY MARKET RATES

(Per cent per annum)



[1]The rate of interest on SDR holdings for each quarter, under Rule T-1(b), is based on a combined market rate of interest.

CHART 8

THREE-MONTH FORWARD RATES

Margins from Spot Rates based on noon quotations in New York
(Per cent per annum)

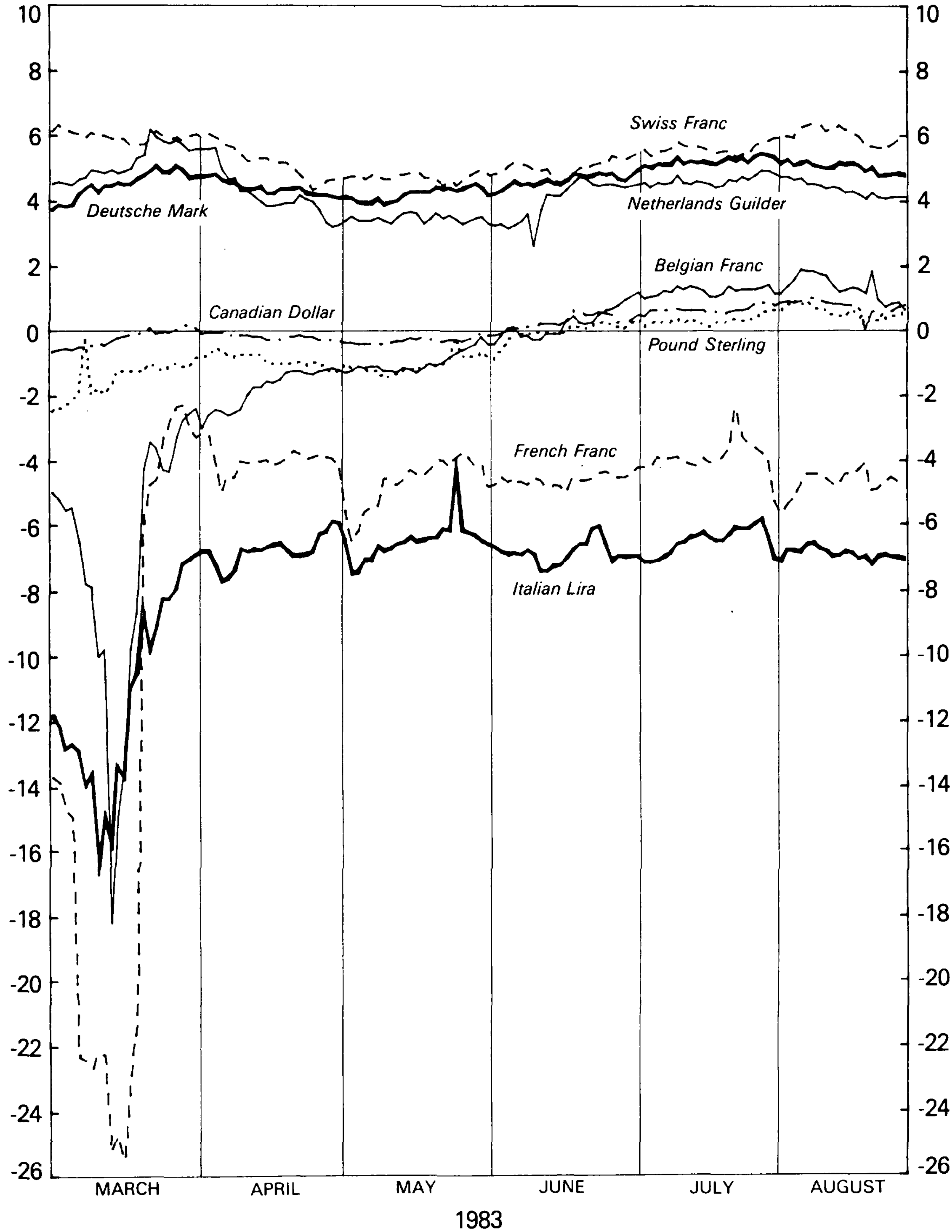
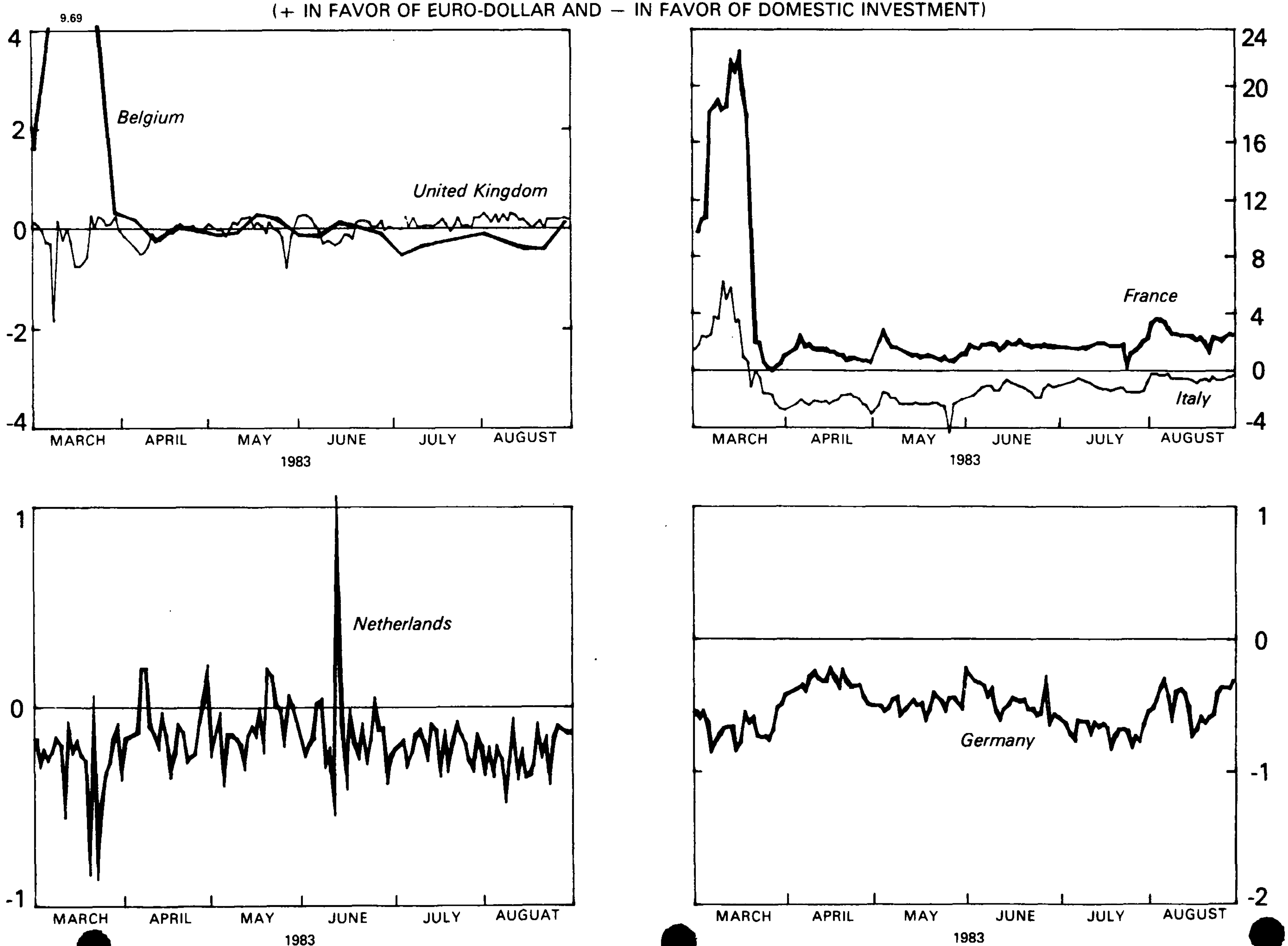


CHART 9

COVERED INTEREST DIFFERENTIALS BETWEEN THREE-MONTH EURO-DOLLAR DEPOSITS AND LOCAL SHORT-TERM INVESTMENTS

(+ IN FAVOR OF EURO-DOLLAR AND — IN FAVOR OF DOMESTIC INVESTMENT)



Foreign Exchange Rates, July-August 1983 1/

	July				August				
	6	13	20	27	3	10	17	24	31
Austrian schilling	18.0700	18.2335	18.0785	18.4175	18.7025	19.1425	18.5875	18.5525	18.9950
Belgian franc									
Official	51.440	51.735	51.560	52.455	53.295	54.510	53.005	52.990	54.210
Financial	51.835	52.035	51.815	52.665	53.485	54.475	53.290	53.425	54.655
Canadian dollars	0.81251	0.80972	0.81133	0.81096	0.81087	0.80857	0.81103	0.81314	0.81044
Danish kroner	9.2325	9.2675	9.2738	9.4365	9.5675	9.8025	9.5500	9.4850	9.7095
Deutsche mark	2.56725	2.58450	2.57665	2.6240	2.66105	2.72430	2.64000	2.63550	2.69650
French francs	7.7095	7.7715	7.7450	7.8865	8.0050	8.1965	7.9413	7.9325	8.1125
Irish pounds	1.2298	1.2227	1.2270	1.2057	1.1871	1.1600	1.1955	1.1945	1.1663
Italian lire	1520.500	1529.000	1522.375	1553.500	1574.625	1610.500	1571.000	1575.500	1610.500
Japanese yen	239.450	239.750	239.275	240.845	243.200	245.750	243.550	242.850	246.400
Netherlands guilder	2.8760	2.8868	2.8808	2.9343	2.9736	3.0465	2.9550	2.9493	3.0183
Norwegian kroner	7.3060	7.3050	7.3013	7.3730	7.4365	7.5575	7.4075	7.3840	7.4925
Pounds sterling	1.5400	1.5301	1.5243	1.5280	1.5062	1.4815	1.5150	1.5203	1.4944
Swedish kroner	7.6625	7.6885	7.6713	7.7380	7.8035	7.9525	7.8100	7.7825	7.9225
Swiss francs	2.12475	2.11175	2.09875	2.11450	2.15325	2.19475	2.14000	2.14575	2.18625

1/ Wednesday noon spot quotations in New York, expressed in terms of currency units per U.S. dollar, except for the Canadian dollar, the Irish pound, and the pound sterling which are expressed in U.S. dollars per currency unit.

Short- and Medium-Term Interest Rates

APPENDIX B

(Monthly and weekly averages)

		National Money Markets 1/						Euro-currency Markets 2/						Lending Rate		U.S.
		United States (1)	Germany (2)	United Kingdom (3)	France (4)	Japan (5)	Weighted average (6)	U.S. dollar (7)	Deutsche mark (8)	Pound sterling (9)	French franc (10)	Japanese yen (11)	Swiss franc (12)	LIBOR 3/ (13)	U.S. prime 4/ (14)	Treasury 5/ Securities (15)
1982																
Sept.		8.21	8.29	10.36	14.24	7.31	8.94	11.85	7.83	10.93	19.43	7.38	4.08	12.75	13.50	12.25
Oct.		7.97	7.68	9.59	13.65	7.19	8.56	10.51	7.19	9.82	19.01	7.03	3.75	10.82	12.52	10.80
Nov.		8.34	7.41	9.08	13.16	7.23	8.59	9.82	7.07	9.35	18.77	7.12	3.83	10.06	11.85	10.38
Dec.		8.20	6.71	10.30	12.90	7.19	8.49	9.57	6.38	10.55	22.46	7.05	3.73	9.84	11.50	10.22
1983																
Jan.		8.15	5.90	10.72	12.76	7.00	8.32	9.01	5.53	11.17	21.16	6.52	2.80	9.25	11.16	10.03
Feb.		8.40	5.92	11.14	13.07	6.92	8.51	9.22	5.66	11.33	22.11	6.71	2.98	9.53	10.98	10.26
Mar.		8.67	5.52	10.95	12.77	6.85	8.50	9.32	5.06	10.98	26.92	6.71	3.67	9.53	10.50	10.08
Apr.		8.52	5.27	10.30	12.31	6.76	8.26	9.26	5.02	10.25	13.37	6.29	4.28	9.44	10.50	10.02
May		8.50	5.39	10.08	12.73	6.66	8.27	9.03	5.04	10.25	13.90	6.29	4.53	9.18	10.50	10.03
June		9.14	5.65	9.85	12.81	6.64	8.62	9.75	5.33	10.00	14.45	6.55	5.00	10.05	10.50	10.63
July		9.44	5.65	9.69	12.45	6.72	8.74	10.07	5.18	9.89	14.15	6.58	4.81	10.51	10.50	11.21
Aug.		9.72	5.79	9.56	12.62	6.80	8.93	10.35	5.47	9.86	15.22	6.67	4.66	10.82	10.89	11.63
1982 Weekly																
Sept.	3	8.65	8.47	10.39	14.09	7.40	9.20	11.71	8.19	10.93	21.22	7.38	4.06	12.72	13.50	12.54
	10	8.63	8.35	10.25	14.26	7.34	9.16	11.61	7.86	10.91	20.19	7.39	3.81	12.66	13.50	12.43
	17	8.31	8.28	10.29	14.42	7.32	9.00	12.20	7.79	10.95	18.65	7.42	4.10	13.16	13.50	12.47
	24	7.78	8.22	10.52	14.32	7.27	8.74	11.88	7.69	11.00	19.31	7.41	4.10	12.73	13.50	12.11
Oct.	1	7.77	8.22	10.32	14.04	7.25	8.68	11.65	7.82	10.73	18.28	7.29	4.34	12.29	13.50	11.74
	8	[illegible]	8.00	10.12	13.98	7.21	8.82	11.56	7.59	10.50	17.54	7.30	4.25	12.00	13.50	11.29
	15	7.72	7.65	9.82	13.66	7.21	8.46	10.24	7.05	9.70	17.88	6.88	3.55	10.45	12.86	10.46
	22	7.78	7.50	9.35	13.59	7.15	8.40	9.94	6.95	9.43	20.45	6.90	3.49	10.23	12.00	10.50
	29	8.19	7.44	8.96	13.24	7.17	8.52	10.07	7.04	9.50	20.35	6.95	3.61	10.35	12.00	10.73
Nov.	5	8.04	7.42	9.28	13.10	7.19	8.46	9.74	6.99	9.29	19.00	7.01	3.49	9.93	12.00	10.34
	12	8.35	7.35	8.78	13.12	7.25	8.55	9.82	7.07	9.16	n.a	7.09	3.69	9.98	12.00	10.44
	19	8.60	7.43	8.78	13.22	7.25	8.70	10.03	7.12	9.20	18.13	7.16	4.07	10.28	12.00	10.51
	26	8.21	7.41	8.98	13.18	7.21	8.51	9.69	7.08	9.27	18.46	7.15	4.06	10.01	11.50	10.21
Dec.	3	8.42	7.23	10.32	13.03	7.21	8.17	9.80	6.88	10.23	19.35	7.31	3.89	10.14	11.50	10.31
	10	8.23	6.57	9.98	12.80	7.21	8.44	9.50	6.34	10.11	19.83	6.96	3.47	9.78	11.50	10.26
	17	8.07	6.67	10.52	12.90	7.21	8.45	9.63	6.44	10.66	22.85	7.05	4.07	9.93	11.50	10.23
	24	8.17	6.76	10.42	12.96	7.15	8.50	9.61	6.44	11.06	26.50	7.08	3.97	9.86	11.50	10.22
	31	8.28	6.62	10.25	12.93	7.15	8.51	9.41	5.98	10.72	24.21	6.88	3.36	9.61	11.50	10.15
1983 Weekly																
Jan.	7	8.32	6.05	10.05	12.83	7.08	8.38	9.03	5.74	10.52	23.78	6.57	3.11	9.23	11.50	10.04
	14	7.92	5.74	10.25	12.67	7.02	8.12	8.80	5.38	11.33	21.43	6.44	2.69	9.00	11.26	9.88
	21	8.01	5.73	11.13	12.72	n.a.	n.a.	8.88	5.40	11.14	20.28	6.40	2.55	9.10	11.00	9.92
	28	8.33	6.05	11.20	12.80	6.95	8.48	9.27	5.57	11.60	19.35	6.65	2.83	9.58	11.00	10.22
Feb.	4	8.45	6.03	11.34	12.95	6.95	8.56	9.45	5.75	11.57	20.30	6.69	2.95	9.80	11.00	10.38
	11	8.51	6.00	11.30	13.05	6.95	8.59	9.29	5.80	11.24	21.00	6.73	2.99	9.66	11.00	10.45
	18	8.44	5.90	10.98	13.16	6.91	8.51	9.18	5.68	11.13	23.63	6.68	2.89	9.46	11.00	10.28
	25	8.22	5.78	11.00	13.05	6.89	8.37	9.08	5.49	11.40	22.85	6.74	3.03	9.31	11.00	9.95
Mar.	4	8.26	5.68	11.16	13.15	6.89	8.40	8.85	5.26	11.34	24.85	6.74	3.06	9.06	10.50	9.76
	11	8.56	5.58	11.13	13.18	6.89	8.52	9.15	5.10	11.16	36.70	6.74	3.43	9.32	10.50	10.03
	18	8.63	5.55	11.23	12.88	6.83	8.52	9.31	5.08	10.78	41.70	6.74	3.89	9.54	10.50	10.08
	25	8.88	5.41	10.52	12.52	6.83	8.49	9.56	4.93	8.63	15.53	6.74	3.94	9.75	10.50	10.26
Apr.	1	8.97	5.40	10.66	12.17	6.83	8.53	9.70	4.95	10.86	12.22	n.a.	4.00	9.94	10.50	10.28
	8	8.77	5.30	10.66	12.42	6.79	8.43	9.56	5.02	10.28	14.11	6.39	4.02	9.74	10.50	10.13
	15	8.47	5.24	10.19	12.04	6.76	8.18	9.28	5.00	10.15	13.38	6.24	4.10	9.46	10.50	9.98
	22	8.43	5.23	10.19	12.34	6.76	8.19	9.23	5.05	10.26	13.38	6.28	4.30	9.39	10.50	10.02
	29	8.42	5.33	10.08	12.47	6.70	8.20	9.05	5.02	10.25	12.98	6.25	4.65	9.24	10.50	9.95
May	6	8.32	5.37	9.98	12.80	6.70	8.18	8.84	5.00	10.15	14.70	6.24	4.37	8.96	10.50	9.77
	13	8.33	5.37	9.92	12.80	6.70	8.18	8.79	4.99	10.19	13.98	6.20	4.32	8.91	10.50	9.84
	20	8.45	5.37	10.15	12.67	6.63	8.24	9.07	5.02	10.35	13.70	6.30	4.51	9.21	10.50	10.10
	27	8.80	5.44	10.29	12.67	6.63	8.45	9.29	5.10	10.32	13.38	6.37	4.86	9.48	10.50	10.32
June	3	8.90	5.58	10.07	12.77	6.63	8.51	9.56	5.39	10.34	13.97	6.55	4.91	9.83	10.50	10.51
	10	9.10	5.71	10.12	12.80	6.63	8.64	9.75	5.46	10.25	14.44	6.54	5.00	10.05	10.50	10.61
	17	9.04	5.64	9.92	12.80	6.63	8.57	9.64	5.27	9.88	14.40	6.49	5.03	9.99	10.50	10.49
	24	9.33	5.63	9.58	12.85	6.63	8.69	9.84	5.27	9.84	14.73	6.59	5.14	10.14	10.50	10.71
July	1	9.22	5.65	9.58	12.80	6.67	8.64	9.84	5.25	9.73	14.43	6.55	4.82	10.14	10.50	10.80
	8	9.42	5.67	9.58	12.67	6.70	8.74	9.98	5.23	9.86	14.34	6.56	4.81	10.31	10.50	11.07
	15	9.46	5.67	9.78	12.61	6.70	8.77	10.17	5.21	9.92	14.19	6.58	4.83	10.64	10.50	11.22
	22	9.46	5.60	9.70	12.45	6.70	8.74	10.04	5.10	9.92	14.30	6.60	4.75	10.53	10.50	11.22
	29	9.50	5.64	9.72	12.29	6.76	8.76	10.16	5.14	9.92	13.73	6.59	4.88	10.68	10.50	11.39
Aug.	5	9.79	5.72	9.61	12.47	6.76	8.94	10.50	5.39	9.96	15.31	6.68	4.90	10.99	10.50	11.74
	12	9.91	5.94	9.54	12.62	6.76	9.05	10.60	5.75	9.92	15.58	6.69	4.77	11.13	10.71	11.89
	19	9.73	5.75	9.56	12.61	6.82	8.92	10.21	5.38	9.81	15.10	6.65	4.37	10.68	11.00	11.49
	26	9.52	5.73	9.53	12.85	6.83	8.83	10.09	5.33	9.77	14.93	6.65	4.64	10.51	11.00	11.34

1/ As of January 1, 1981, the combined market interest rate under the amended Rule T-1 is calculated by multiplying the yield or rate on each of the respective instruments listed below by the number of units of the corresponding currency listed in Rule O-1 and the value in terms of the SDR of a unit of that currency as determined by the Fund under Rule O-2(a) and (b). The interest rates and the respective currency units (shown in parentheses) are as follows: market yield for three-month U.S. Treasury bills (0.54), three-month interbank deposit rate in Germany (0.46), three-month interbank money rate against private paper in France (0.74), discount rate on two-month (private) bills in Japan (34), and market yield for three-month U.K. Treasury bills (0.071).

2/ Euro-currency interest rates are those on three-month deposits for the U.S. dollar, the Deutsche mark, the Swiss franc, and the French franc (in London), and for the pound sterling (in Paris).

3/ LIBOR is six-month euro-dollar offered rate in London.

4/ Prime lending rate of major New York banks.

5/ Yield is adjusted to constant five-year maturity by the U.S. Treasury and is based on only recently issued, actively traded securities. The interest rate paid to lenders and charges on drawings under the Supplementary Financing Facility are based on this rate.