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Treasurer's Department

Foreign Exchange and Financial Markets in May 1984

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The strong firming trend of the U.S. dollar continued on the major exchange markets in the earlier part of May but the dollar tended to weaken thereafter as a result of some easing of U.S. interest rates and the expectation that the Federal Reserve would not tighten its monetary stance in the face of liquidity problems faced by some U.S. banks. Relatively heavy intervention in the second week of the month by the Bundesbank coupled with its continued intervention later but at a smaller scale, and occasional presence of other central banks in the market might have also affected the dollar on the exchanges. Over the month as a whole, the U.S. dollar firmed by 0.55 percent against the SDR and 1.66 percent in effective (MERM) terms. The Japanese yen was the weakest among the major currencies, easing by nearly 2.0 percent against the U.S. dollar as well as in effective (MERM) terms, reflecting principally market reactions to the possibility that Japan's oil imports might be reduced as the Iran-Iraq war escalated. The Bank of Japan reportedly intervened to support the currency on May 18 when the Persian Gulf war escalated markedly. Announcement of further measures toward the internationalization of the yen near the end of the month, however, provided some support to the currency. The Canadian dollar continued to be weak against the U.S. dollar on the market perception that the Bank of Canada would not be able to keep Canadian interest rates in line with those in the United States in the face of rising unemployment (see Table 1).



Table I. Changes in Exchange Rates in May 1984 1/

(In percent)

	<u>Monthly exchange rate changes</u>			Changes in effective exchange rate since May 1983 <u>3/</u>
	Against U.S. dollar <u>2/</u>	Against SDR <u>3/</u>	Effective exchange rate <u>3/4/</u>	
Belgium	-0.56	-0.04	-0.01	-3.21
Denmark	-0.78	-0.23	-0.37	-4.78
France	-0.48	-0.79	-0.54	-4.82
Germany	-0.38	-0.05	-0.11	-1.92
Ireland	-0.38	-0.16	-0.09	-4.68
Italy	-0.56	+0.03	+0.27	-6.03
Netherlands	-0.45	-0.79	-0.60	-1.74
Austria	-0.47	+0.02	-0.51	-2.62
Canada	-0.78	-0.24	-0.40	-2.88
Japan	-1.97	-1.56	-1.86	+7.67
Norway	-0.76	-0.20	+0.22	-3.24
Sweden	-1.23	-0.38	-0.05	-1.37
Switzerland	-0.60	-0.15	-0.10	-2.73
United Kingdom	-0.88	-0.26	-0.21	-9.33
United States	--	+0.55	+1.66	+5.86

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). Effective rates and rates against the SDR are based on representative exchange rates officially advised to the Fund.

4/ Since several countries did not advise representative exchange rates for the last day of April and the last day of May, the monthly changes have been based on second-to-last days.

The firming trend of the U.S. dollar evident in April continued into early May under the influence of rising U.S. interest rates and industrial unrest in Germany and the United Kingdom. Following the increase in the prime lending rate from 12.0 percent to 12.5 percent by major U.S. banks, the Bundesbank increased the scale of its intervention to support the Deutsche mark against the U.S. dollar. On May 8-10, the Bundesbank reportedly sold nearly \$600 million, and intervention by the Bank of Japan and the Bank of England was also suspected by many market participants. The U.S. dollar tended to weaken since then, amid some fluctuations, on easier interest rates and on the expectation as indicated earlier, that the U.S. Federal Reserve might

not tighten monetary policy in the light of potential liquidity problems of major U.S. banks with large foreign loan exposures. In addition, the Bundesbank continued to sell generally small amounts of U.S. dollars, totaling about \$250 million in the last three weeks of the month. On May 24 rumors that a major New York bank was in a liquidity crisis similar to that faced by a large Illinois bank (which had been rescued from liquidity difficulties by Federal agencies earlier in the month) caused the U.S. dollar to ease sharply; the Federal Reserve Bank of New York reportedly intervened to settle the market by selling Deutsche mark equivalent to about \$140 million. On balance, the U.S. dollar closed the month moderately firmer, as compared with the closing quotations of April.

Within the European Monetary System, the spread in the narrow band remained well below the permitted 2.25 percent margin, with the Belgian franc at the bottom and the Netherlands guilder at the top for most of the month; the Deutsche mark replaced the Netherlands guilder at the top on a few occasions late in May (see Chart 1). The divergence indicator for the Belgian franc was below its lower threshold most of the first half of the month but then moved above it (see Chart 2). The Italian lira continued to be the strongest currency in the EMS with a spread in the range of 2.81-3.45 percent from the Belgian franc. Against the U.S. dollar, the EMS currencies eased by 0.38-0.78 percent over May.

The range within which major currencies were traded in May narrowed considerably as the dollar's rapid appreciation was halted in midmonth and reversed toward late May. The range of fluctuations recorded by the EMS currencies was 2.3-2.8 percent compared with 4.0-4.8 percent in April. Other currencies moved within similar trading ranges except the Canadian dollar, which continued to fluctuate the least against the U.S. dollar (see Table 2). The average absolute daily percentage changes against the U.S. dollar (MAC in Table 2 and Chart 5) widened somewhat for all the major currencies, reflecting occasional erratic trading since midmonth as contradictory influences affected market participants' views about the international financial environment.

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

	May <u>2/</u>		High-low spread in percent <u>3/</u>		MAC <u>4/</u>	
	High	Low	Apr.	May	Apr.	May
Belgium	55.210	56.525	4.3	2.4	0.36	0.38
Denmark	9.9160	10.1675	4.3	2.5	0.35	0.47
France	8.3020	8.8350	4.2	2.8	0.38	0.48
Germany	2.7040	2.7810	4.8	2.8	0.36	0.49
Ireland	1.1340	1.1055	4.6	2.6	0.38	0.43
Italy	1678.5	1717.0	4.0	2.3	0.36	0.37
Netherlands	3.04575	3.12475	4.5	2.6	0.34	0.44
Austria	19.010	19.5415	4.5	2.8	0.35	0.48
Canada	0.77601	0.77080	0.8	0.7	0.09	0.14
Japan	226.35	233.315	1.9	3.1	0.23	0.24
Norway	7.7175	7.8795	2.9	2.1	0.25	0.36
Sweden	7.9880	8.1450	3.3	2.0	0.22	0.33
Switzerland	2.24125	2.28920	4.3	2.1	0.32	0.35
United Kingdom	1.4135	1.3770	2.8	2.7	0.28	0.35

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.

Among the countries recording changes in foreign exchange reserves in May (see Table 3), the most notable was the decline of \$1,475 million recorded by Germany, resulting mainly from the Bundesbank's intervention during the month. Sweden, on the other hand, posted a sizable reserve increase in May. Other countries recorded small to moderate changes in reserves in May. Over the latest twelve-month period, sizable reserve increases were recorded by France, Italy, Sweden, and to a lesser extent, by Japan, while significant declines in reserves recorded by the United States, the United Kingdom, Belgium, and Canada.



Table 3. Foreign Exchange Reserves in May 1984 ^{1/}

(In millions of U.S. dollars)

	End-month reserve level	Change in May	Change over 12 months
Belgium	3,174	-271	-869
Denmark	3,195	+86	+149
France (April)	18,935	+404	+1,713
Germany	39,460	-1,475	+783
Ireland	2,480	+51	+776
Italy	17,522	+225	+2,392
Netherlands	8,580	-125	-481
Austria	3,951	-81	-366
Canada	2,094	+356	-929
Japan	21,150	-29	+871
Norway	6,981	-300	+428
Sweden	4,015	-679	+911
Switzerland	12,252	-79	+238
United Kingdom	7,656	-121	-1,530
United States	6,430	-164	-1,420

^{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 proceeds from other official borrowings.

I. Developments in Major Factors Affecting the Exchange Market

The U.S. dollar firmed 1.66 percent in effective (MERM) terms and 0.55 percent against the SDR as interest rates continued to rise under the influence of the strong economic recovery and unsettling events affecting some of the other major currencies. The U.S. index of leading economic indicators rose 0.5 percent in April and the March figure was revised to show a decline of 0.1 percent compared with 1.1 percent estimated earlier. Industrial output rose 1.4 percent in April, the 17th consecutive monthly rise, following a rise of 0.5 percent in March; the increase over the last 12 months was 14.4 percent. The first quarter real GNP growth was revised further to an annual rate of 8.8 percent (from 8.3 percent) and the rise in the GNP price deflator was revised downward to an annual rate of 3.7 percent from 4.1 percent. The unemployment rate declined to 7.5 percent in May from 7.8 percent



in April. The budgetary position, a factor influencing U.S. interest rates, swung into a surplus of \$11.5 billion in April from deficits of \$28.6 billion in March and \$3.3 billion in April 1983; for the first seven months of the fiscal year, the deficit narrowed to \$106.3 billion from \$132.5 billion in the same period of the previous fiscal year. The trade deficit, however, continued to widen; the deficit was \$12.19 billion in April compared with \$10.26 billion in March. The inflation rate remained low despite the vigor of the economy; the producer price index was unchanged in April and was up only 2.9 percent year-on-year.

The Deutsche mark eased 0.38 percent against the U.S. dollar and 0.11 percent in effective (MERM) terms. The Deutsche mark was adversely affected by uncertainties associated with the metal workers' strike and the Bundesbank, as noted earlier, intervened to support the currency on the exchange market. Among the major economic factors, the index of industrial production, seasonally adjusted, was little changed in April but rose 3.2 percent year-on-year. The unemployment rate declined in May, largely on seasonal factors, to 8.6 percent from 9.1 percent in April and 8.8 percent in May 1983. The current account balance swung into a deficit of DM 400 million in April from surpluses of DM 1.85 billion in March and DM 2 million in April 1983. The wholesale price index rose 0.4 percent in April for a 4.9 percent year-on-year rise; the producer price index also rose 0.4 percent for a 3.1 percent year-on-year rise.

The French franc eased 0.48 percent against the U.S. dollar and 0.54 percent in effective (MERM) terms. The index of industrial production in France, seasonally adjusted, rose 1.5 percent in March after falling 0.8 percent in February and was up 4.7 percent year-on-year. The number of persons unemployed rose a seasonally adjusted 2.3 percent in April and was up 17.8 percent year-on-year; the unemployment rate was about 9.8 percent. The trade deficit widened in April to a seasonally adjusted F 4.4 billion from F 2.8 billion in March. Industrial wholesale prices rose 0.8 percent in April and 14.2 percent year-on-year.

The Belgian franc eased 0.56 percent against the U.S. dollar and was essentially unchanged in effective (MERM) terms. The franc remained the weakest currency in the EMS during May but no intervention by the National Bank of Belgium was required to maintain the currency within the agreed margin. The discount of the financial franc from the commercial franc remained in the range of 1.5-2.0 percent. Industrial production in Belgium rose 5.8 percent in March, largely because of seasonal factors, and was up only 5.3 percent year-on-year. Real GDP rose 0.4 percent in the first quarter of 1984, following a rise of 0.6 percent in the fourth quarter of 1983. The unemployment rate declined at the end of May to 12 percent from 12.2 percent at the end of April. The current account deficit of the Belgo-Luxembourg Economic Union (BLEU) narrowed to BF 11.3 billion in the January-February period from

BF 30.2 billion a year earlier. The wholesale price index rose 0.5 percent in April and was up 11.0 percent year-on-year.

The Netherlands guilder eased 0.45 percent against the U.S. dollar and 0.60 percent in effective (MERM) terms. Industrial production, seasonally adjusted, in the Netherlands rose 1.0 percent in March, and was up 6.3 percent year-on-year. The number of persons unemployed, seasonally adjusted, rose 0.7 percent in May; the unemployment rate in April was 18 percent. The trade deficit widened in March to f. 2.1 billion from f. 818 million in February but was unchanged from March 1983. The producer price index for consumer and investment goods rose 0.1 percent in March and was up 4.9 percent year-on-year.

The Danish krone eased 0.78 percent against the U.S. dollar and 0.37 percent in effective (MERM) terms. The unemployment rate in Denmark, seasonally adjusted, declined to 10.6 percent in April from 10.8 percent in March. The trade deficit in April, seasonally adjusted, widened to DKr 890 million from DKr 506 million in March. The wholesale price index rose 0.9 percent in April for a 9.8 percent year-on-year rise. The Irish pound eased 0.38 percent against the U.S. dollar and 0.09 percent in effective (MERM) terms.

The Italian lira eased 0.56 percent against the U.S. dollar but firmed 0.27 percent in effective (MERM) terms; it remained the strongest currency in the EMS, being traded at a premium over the weakest currency moderately above the narrow band of the parity grid. The Bank of Italy reduced its official interest rates early in the month and commercial banks followed suit by reducing their prime lending rate. Industrial production in Italy rose 2.6 percent in the first quarter of 1984 compared with the same period in 1983 while the trade deficit widened slightly to Lit 4,184 billion from Lit 4,106 billion in the first quarter of 1983. The budget deficit in the first quarter widened to Lit 17,170 billion from Lit 13,450 billion a year earlier. The wholesale price index rose 0.8 percent in April and was up 11.4 percent year-on-year.

The pound sterling eased 0.88 percent against the U.S. dollar and 0.21 percent in effective (MERM) terms. The pound was adversely affected, especially early in May, by the coal miners' strike but it received some support later in the month as concerns about the supply of oil from the Persian Gulf region increased. Over the past 12 months, the pound has been the weakest of the major currencies in effective (MERM) terms, depreciating by over 9 percent. Industrial output, seasonally adjusted, declined 1.4 percent in March, due mainly to the coal miners' strike, and the current account swung into a seasonally adjusted deficit of £588 million in April from a surplus of £23 million in March. The estimate of the current account surplus for 1983 was, however, revised sharply upwards from £2.0 billion to £2.9 billion reflecting mainly revised estimates of invisible transactions. For the first quarter of 1984, the surplus was revised upwards to £838

million from £691 million. Real GDP in the first quarter rose 0.2 percent and was up 2.9 percent year-on-year. The index of leading indicators for activity one year ahead was unchanged in April after rising in earlier months of 1984. The unemployment rate, seasonally adjusted, increased to 12.7 percent in May from 12.6 percent in April. The producer price index for manufactured goods rose 0.4 percent in May and was up 6.4 percent year-on-year.

The Swiss franc eased 0.60 percent against the U.S. dollar and 0.10 percent in effective (MERM) terms. The unemployment rate was unchanged in April at 1.2 percent. The trade deficit narrowed in April to Sw F 664 million from Sw F 969 million in March. The wholesale price index rose 0.2 percent in May for a 3.7 percent year-on-year rise.

The Japanese yen was the weakest of the major currencies in May; it eased 1.97 percent against the U.S. dollar and 1.86 percent in effective (MERM) terms, principally because of concerns about the supply of oil from the Persian Gulf area. The yen's twelve-month effective (MERM) appreciation declined from 10 percent to 7.7 percent. A package of measures aimed at further internationalization of the yen helped lend some support to the currency late in May. The package included the lifting of ceilings on yen swap agreements, a reduction in the minimum allowable size of certificates of deposit that foreign banks can issue in Japan, permission for foreign banks to participate in syndicated euro-yen loans of less than one-year maturity and permission for more governments and corporations to issue euro-yen bonds and Samurai bonds in Japan. Some of these measures would take effect at a later date. Indications were also given that the Japanese authorities might consider elimination of interest rate ceilings and establishment of a yen-denominated bankers' acceptance market. Among other economic developments, industrial production rose 12.1 percent in April over the same month in 1983 while the unemployment rate declined to 2.8 percent from 3.1 percent in March. The current account surplus, seasonally adjusted, widened in April to \$3,562 million from \$2,428 million in March while the trade surplus, seasonally adjusted, narrowed to \$2,226 million in May from \$3,020 million in April. The wholesale price index rose 0.1 percent in May but was down 0.1 percent year-on-year.

The Canadian dollar continued to remain weak against the U.S. dollar; it eased 0.78 percent against the dollar and 0.40 percent in effective (MERM) terms on the expectation that the Bank of Canada would have to ease monetary policy to prevent the unemployment rate from further increases. The unemployment rate rose to 11.7 percent in May from 11.4 percent in April. The index of leading economic indicators rose 1.16 percent in February compared with a rise of 1.20 percent in January. The index of industrial production rose 0.2 percent in March and was up 10.2 percent year-on-year. The trade surplus widened to a seasonally adjusted Can\$1.75 billion in April from Can\$1.41 billion in March. Industrial selling prices rose 0.5 percent in April, the same as in March, and were up 4.4 percent year-on-year.

The Austrian schilling eased 0.47 percent against the U.S. dollar and 0.51 percent in effective (MERM) terms. The Norwegian krone eased 0.76 percent against the U.S. dollar but firmed 0.22 percent in effective (MERM) terms. The Swedish krona eased 1.23 percent against the U.S. dollar but was essentially unchanged in effective (MERM) terms.

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

Monetary and credit conditions appeared to have tightened somewhat in most major industrial countries in May. Short-term interest rates in the United States, the United Kingdom, Germany, Canada, Switzerland, and, to a lesser extent, Japan and the Netherlands tended to firm during the month. Interest rates in France and Italy, however, eased.

In the United States, interest rates firmed sharply during the first half of the month, attributed to market expectations that the Federal Reserve would pursue a restrictive monetary policy because of its concern over a possible re-emergence of inflation in an environment of strong economic performance. A larger than expected \$5.3 billion increase in the seasonally adjusted M1 money supply measure in the week ended May 7 was followed by large increases in interest rates. Major banks raised their prime lending rate by half a percentage point to 12.5 percent on May 8 after the Federal funds rate rose above 11 percent for the first time since the end of 1982. The previous increase in the prime rate was on April 5 when it was raised from 11.5 percent to 12 percent. In the second half of the month, however, interest rates began to ease as market expectations shifted toward an easing of policy in light of liquidity problems faced by a major commercial bank. Daily average borrowing at the discount window hit \$4.6 billion in the week ended May 16, breaking the previous record set in 1974, which lent some support to the view that the Federal Reserve, at least temporarily, would not allow interest rates to rise. The Federal funds rate moved between 10.51 and 10.81 percent in the last week of May compared with 10.48-11.12 percent in the second week and 9.55-10.67 percent in the last week of April. The 90-day CD rate also rose past the 11 percent level in the first half of May, peaking at almost 11.5 percent, while the bond equivalent yield on three-month Treasury bills firmed less sharply than the CD rate, reaching a high of about 10.5 percent around midmonth. The widening interest rate spread between 90-day CDs and three-month Treasury bills was one consequence of rumors, which were later confirmed, about liquidity problems faced by a major U.S. commercial bank. The 90-day CD rate was 11.30 percent or slightly lower in the last week of May, compared with about 11.40 percent around midmonth but sharply higher than 10.50 percent in the last week of April. The bond equivalent yield on three-month Treasury bills was about 10.1 percent in the last week of May, about 0.25 percentage point lower than that in the second week of May but 0.10 percentage point higher than the level in the last week of April. Thus, while



Table 4. Inflation Rates and Short-Term Interest Rates

	Month <u>2/</u>	Inflation rates <u>1/</u> (year-on-year percent changes)		Short-term interest rates <u>4/</u> (end-of-month)	
		Wholesale price index	Consumer price index <u>3/</u>	April	May
Austria	April	-- (--)	5.9 (5.8)	3.75	3.75
Belgium	Apr./May	11.0 (10.9)	7.2 (7.5)	11.90	11.90
Canada	April	4.4 (4.8)	4.9 (4.7)	10.63	11.30
Denmark	April	9.8 (7.8)	6.6 (7.0)	7.00	7.00
France	Apr./May	14.2 (14.8)	7.7 (7.9)	12.55	12.55
Germany	Apr./May	4.9 (5.4)	2.8 (3.0)	5.91	6.34
Italy	Apr./May	11.4 (11.4)	11.2 (11.6)	17.44	16.94
Japan	May/Mar.	-0.1 (-0.8)	2.5 (2.9)	6.19	6.31
Netherlands	Mar./May	4.6 (4.5)	3.7 (3.9)	5.94	6.13
Norway	Feb./Apr.	6.0 (5.6)	6.6 (6.6)	8.00	8.00
Sweden	April	-- (--)	8.9 (9.0)	8.50	8.50
Switzerland	May	3.7 (3.7)	2.9 (3.2)	3.69	4.06
United Kingdom	May/Apr.	6.4 (6.6)	5.2 (5.2)	8.54	9.21
United States	April	2.9 (2.9)	4.5 (4.7)	10.09	10.13

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, the Netherlands, and Switzerland.

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; four-month certificates of the Government Securities Stabilization Fund for Belgium; central bank discount rates for Austria, Denmark, Norway and Sweden.

interest rates in the United States eased during the second half of the month, they still remained above their levels at the end of April.

The M1 measure of the U.S. money supply, seasonally adjusted, was \$541.9 billion in the week ended May 28, compared with \$534.6 billion in the week ended April 30, putting the money supply toward the end of May about \$3.3 billion below the upper limit of the target range. The average for M1, seasonally adjusted, for the 13 weeks ended May 28 stood 7.4 percent above the average for the 13 weeks ended May 30 last year.

Interest rate developments were mixed in the countries participating in the European Monetary System. In Germany, the three-month interbank deposit rate increased steadily from under 6.0 percent in April to over 6.25 percent during the last half of May. Germany's money supply figures, seasonally adjusted, in April showed that M3 growth rose to 6 percent from 2 percent in March, and M2 growth rose to 6.1 percent from 0.5 percent in March. In France, interest rates eased in the month of May. The Bank of France lowered its money market intervention rate from 12 percent, the rate prevailing since November 1983, to 11.75 percent on May 9. The three-month interbank money rate also fell to around 12.3 percent in the last three weeks of May from around 12.6 percent in the same period in April. The reduction in France's intervention rate was reportedly facilitated by the French franc's ability to maintain its relative strength in the European Monetary System. The Italian Treasury, on May 4, reduced the country's official discount rate and its refinancing rate by half a percentage point to 15.5 percent. The rates were last adjusted on February 15 when they were cut by a full percentage point to 16 percent.

Interest rates in the United Kingdom firmed sharply over the month while those in Japan rose modestly. In the United Kingdom, major banks raised their base lending rates to 9.00-9.25 percent from 8.50-8.75 percent, the first base rate hike since January 1983. After trading within a narrow range around 8.55 percent in April, the rate on three-month U.K. Treasury bills moved to over 9.0 percent at the end of May. The U.K. monetary aggregate M0, the wide monetary base, was estimated by the Bank of England to have risen by about 0.5 percent in the four weeks ended May 18, compared with a fall of 0.1 percent in April. Since February, the beginning of the official target period, M0 has grown at an estimated 4.25 percent pace, near the bottom of its 4-8 percent target. The U.K. broadly defined money supply sterling M3 grew at an estimated annual pace of about 10.5 percent in the same period, thus exceeding the top of its 6-10 percent target range. Sterling M3 rose by 0.9 percent in the four weeks ended May 18 compared with a rise of 0.4 percent in April. In Japan, interest rates tended to rise modestly with three-month domestic rates rising by 0.12 percentage point at the end of May from the end of April.

Japan's broadly defined money supply, M2 plus CDs, grew on average by 7.7 percent in April over April 1983, after a 8.4 percent year-on-year gain in March.

In the eurocurrency market, the three-month eurodollar deposit rate firmed by 0.81 percentage point to 11.81 percent from the end of April to the end of May. The three-month euro-sterling and euro-French franc deposit rates also rose by a similar margin, while deposit rates for the Deutsche mark and the Japanese yen in the eurocurrency market rose by 0.37 and 0.17 percentage points respectively.

As a result of a relatively sharp increase in the eurodollar rate compared with domestic interest rates in the major industrial countries, the uncovered interest differentials favoring eurodollar investment continued to widen for Germany, Japan, the Netherlands, and the United Kingdom and those favoring domestic investment narrowed for Belgium, France, and Italy (see Table 5).

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

	Uncovered interest differentials ^{1/}		Forward exchange quotations ^{2/}		Covered interest differentials ^{1/}	
	(1)		(2)		(3) = (1)-(2)	
	Apr.	May	Apr.	May	Apr.	May
Belgium	-0.90	-0.09	-0.74	-0.22	-0.16	+0.13
France	-1.55	-0.74	-1.57	-1.53	+0.02	+0.79
Germany	+5.09	+5.47	+5.62	+6.13	-0.53	-0.66
Italy	-6.44	-5.13	-4.34	-3.41	-2.10	-1.72
Japan	+4.81	+5.50	+4.94	+5.70	-0.13	-0.20
Netherlands	+5.06	+5.69	+5.25	+5.99	-0.19	-0.30
United Kingdom	+2.46	+2.60	+2.27	+1.94	+0.19	+0.66

^{1/} Positive sign indicates differential in favor of eurodollar 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 the discount rate for two-month private bills is used, for the United Kingdom the three-month Treasury bill rate, and for Belgium the rate on four-month certificates of the Government Securities Stabilization Fund.

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

In the forward exchange markets, the premia against the U.S. dollar widened for the Deutsche mark, the Japanese yen, and the Netherlands guilder, but narrowed for the pound sterling. The discount against the dollar narrowed for the Belgian franc, the French franc, and the Italian lira. As a result of these movements in interest rates and forward exchange quotations, the covered interest differentials favoring eurodollar investment widened for France and the United Kingdom and switched in favor of eurodollar investment for Belgium. The covered interest differentials favoring domestic investment widened modestly for Germany, Japan, and the Netherlands but narrowed significantly for Italy.

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

The SDR interest rate rose to 8.99 percent in the week beginning May 28 from 8.91 percent in the week beginning April 30. Yields on the relevant instruments for the currencies in the SDR basket were mixed; they firmed for Germany, Japan, and the United Kingdom by 0.12-0.67 percentage point but eased for France and the United States by 0.13-0.14 percentage point. The rate of remuneration paid on the creditor positions in the Fund rose accordingly to 7.94 percent from 7.57 percent on April 30. It may be noted that the remuneration coefficient (the relationship of the rate of remuneration to the SDR interest rate) was raised from 85 percent to 88.33 percent in the quarter beginning May 1, 1984.

The combined domestic interest rates rose relatively sharply between the end of April and the end of May for longer than the three-month maturity. Rates for maturities of one-year and longer firmed by 0.87-0.94 percentage point while that for the six-month maturity firmed by 0.75 percentage point. Higher and progressively rising yields on the relevant instruments made the yield curve for the combined market rates steeper: yields on the relevant U.S. instruments at the three-, six-, twelve-, two and a half-, and five-year maturities moved up by 0.14, 1.02, 1.23, 1.31, and 1.39 percentage points between the end of April and the end of May. Yields on the relevant U.K. instruments rose by more than U.S. yields while those for maturities of one year and longer were higher in Japan; German yields rose for all maturities.

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

	Apr. 30	May			
		7	14	21	28
SDR interest rate	8.91	9.03	9.20	9.07	8.99
Rate of remuneration	7.57	7.98	8.13	8.01	7.94

^{1/} The rate pertains to the week beginning on the date indicated above, except for the rate of remuneration for April 30, which was raised to 7.87 percent for the period May 1-6.

The combined eurocurrency interest rates rose sharply by 0.63 percentage point for the three-month maturity and by 1.00 percentage point for the six-month maturity. Eurodollar and euro-sterling interest rates recorded the largest increases, rising by 0.75-1.25 percentage point, while other rates rose by 0.19-0.50 percentage point.

Average interest rates on SDR-denominated deposits of selected commercial banks rose sharply, with the yield curve becoming steeper. The rate on one-month deposits firmed by 0.34 percentage point and that on 12-month deposits rose by 1.10 percentage point.

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

	April	May
Combined market interest rates <u>2/</u>		
Based on domestic rates		
3-month maturity (Rule T-1)	8.87	9.10
6-month maturity	9.19	9.94
12-month maturity	9.56	10.50
2-1/2 year maturity	10.38	11.25
5-year maturity	10.88	11.81
Based on eurocurrency offered rates		
3-month maturity	9.50	10.13
6-month maturity	9.75	10.75
Average commercial bank deposit rates <u>3/</u>		
1-month deposits	8.88	9.22
3-month deposits	9.19	9.83
6-month deposits	9.51	10.44
12-month deposits	9.90	11.00
Bonds quoted on the Luxembourg Stock Exchange <u>4/</u>		
Average current yield	10.14	n.a.
Average yield to maturity	11.16	n.a.

1/ Rates pertain to last Wednesday of the month.

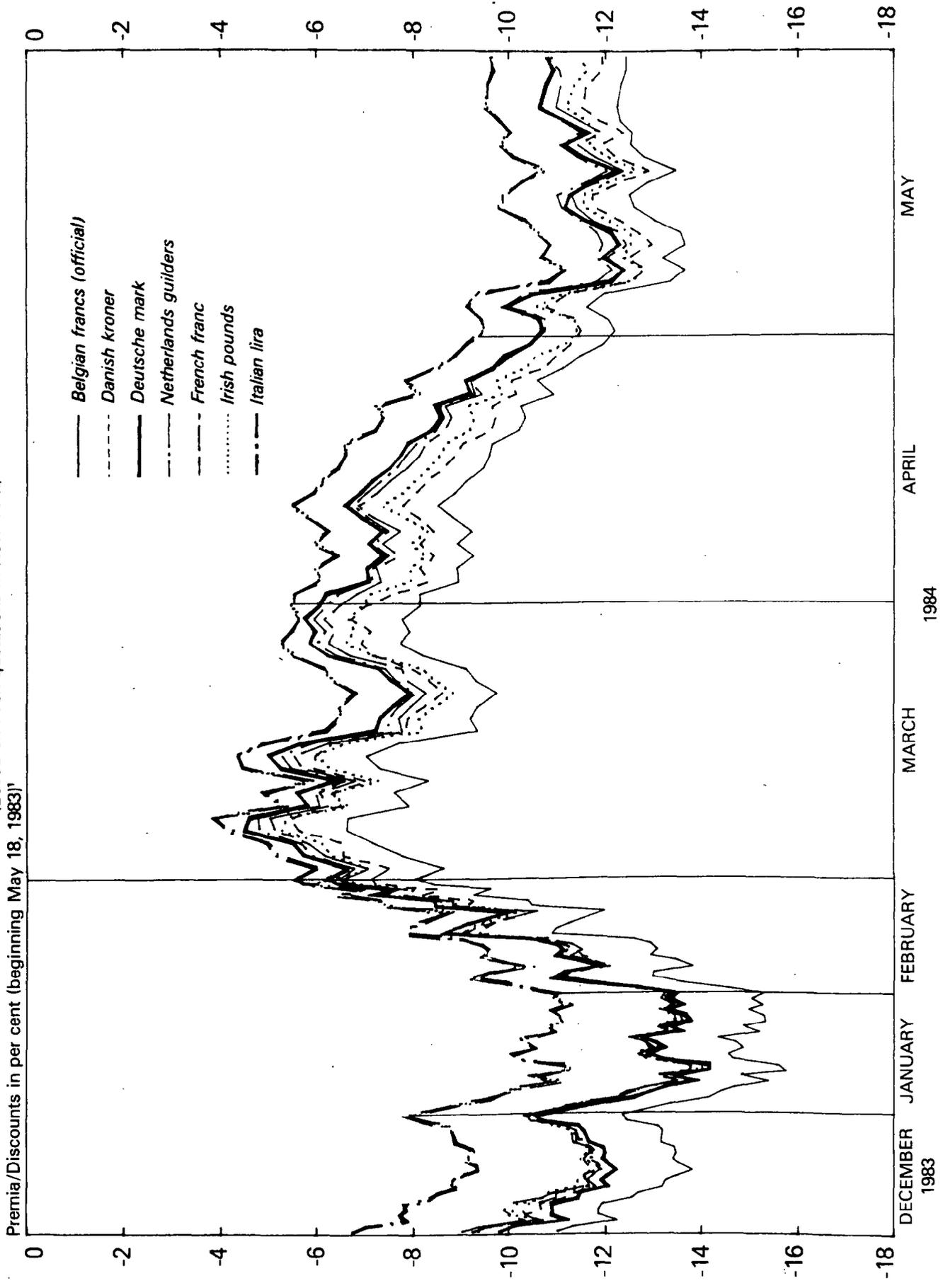
2/ Combined market rates (according to the Rule T-1) are calculated by multiplying the yields or rates of each of the respective instrument by the number of units of the corresponding currency listed in Rule 0-1 and the value in terms of the SDR of a unit of that currency as determined by the Fund under Rule 0-2(a) and (b). Interest rates are those used to determine interest rates on the SDR or on borrowings by the Fund.

3/ Average of rates quoted by selected commercial banks.

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

SPOT EXCHANGE RATES: EUROPEAN MONETARY SYSTEM

(Based on noon quotations in New York)



Effective May 18, 1983 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 US dollar terms at the rate of 1 ECU = .920041.

MONETARY SYSTEM: DIVERGENCE INDICATORS

(Based on noon quotations in London)

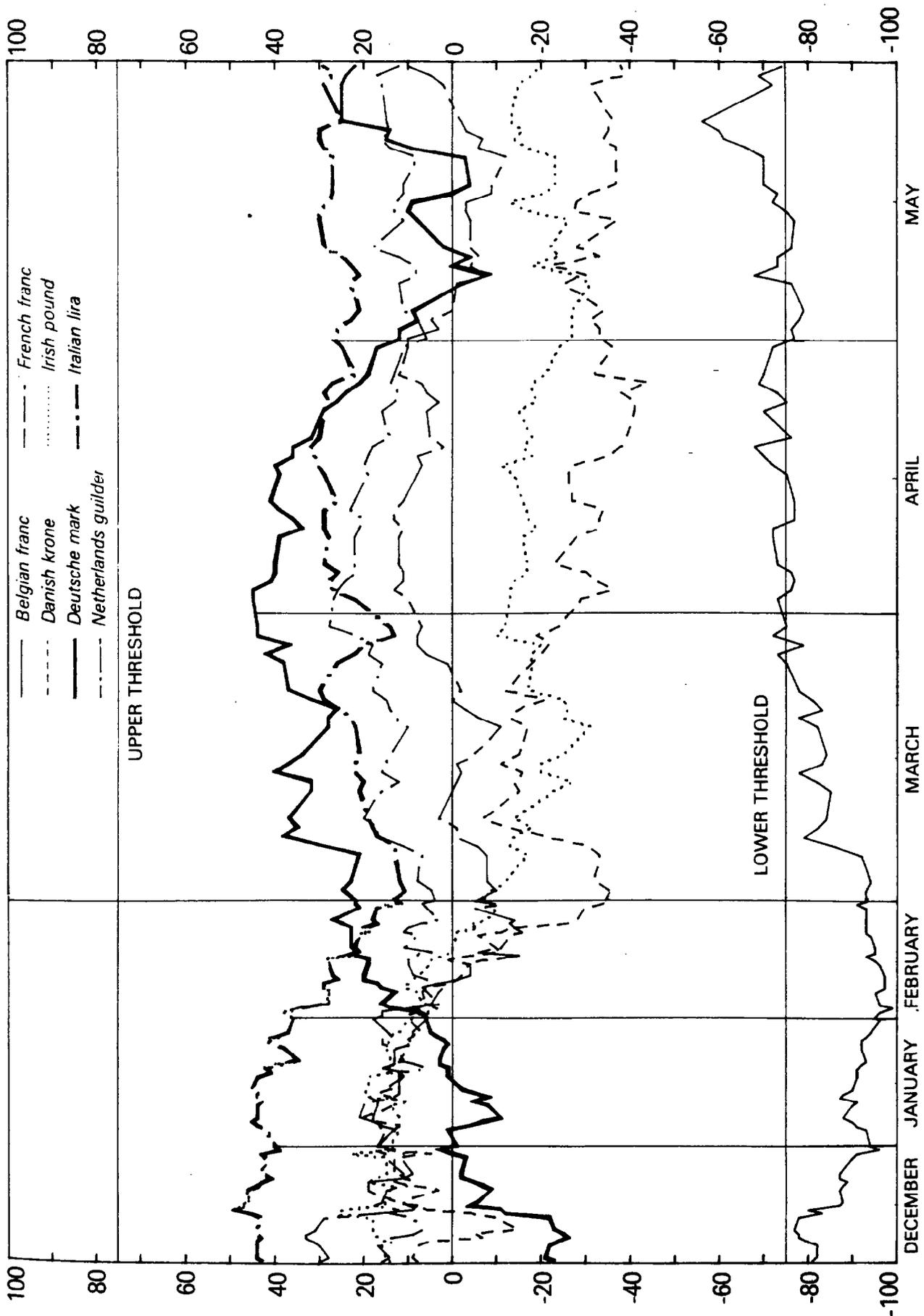


CHART 3 SPOT EXCHANGE RATES

(Noon quotations in New York)

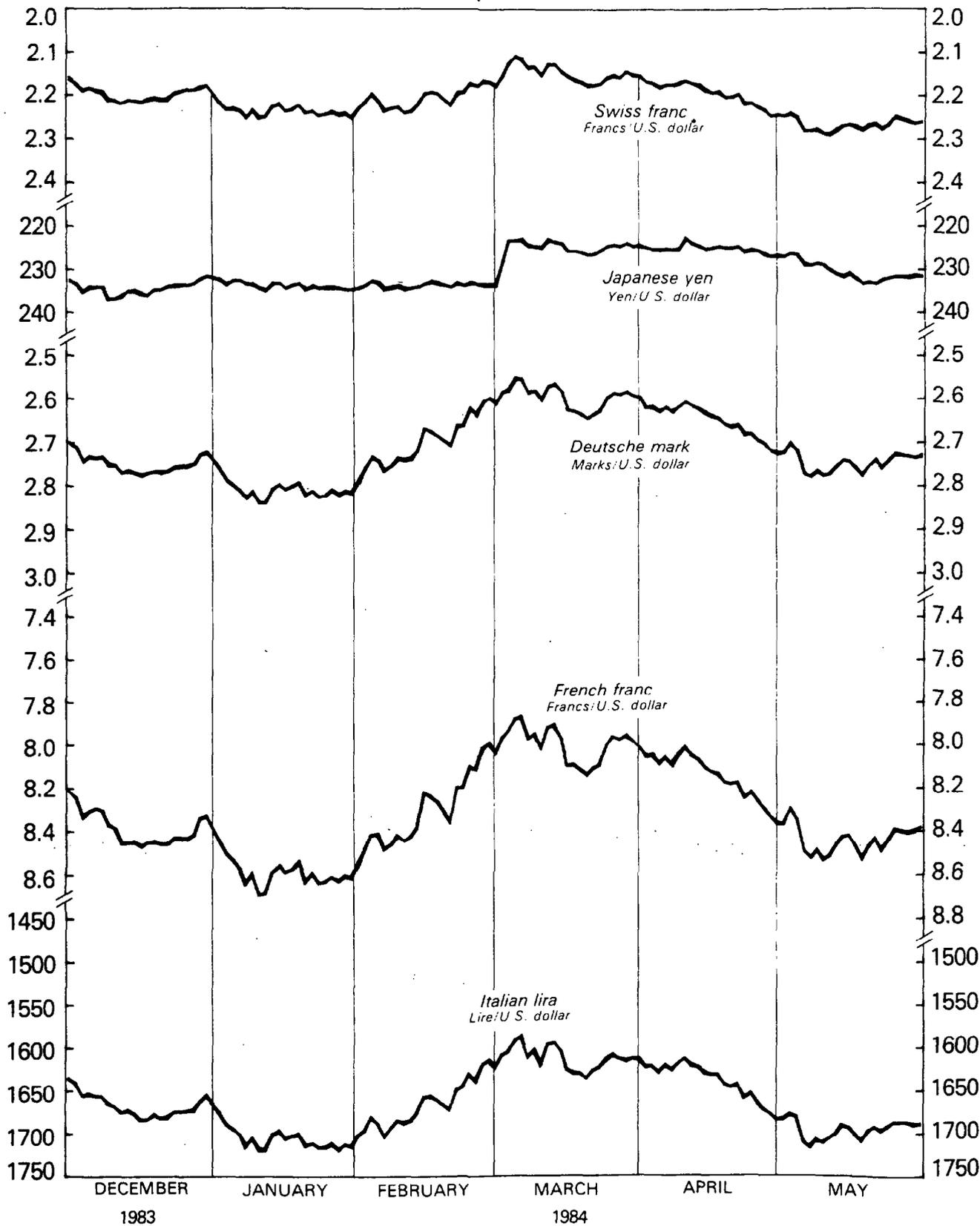


CHART 4 SPOT EXCHANGE RATES

(Noon quotations in New York)

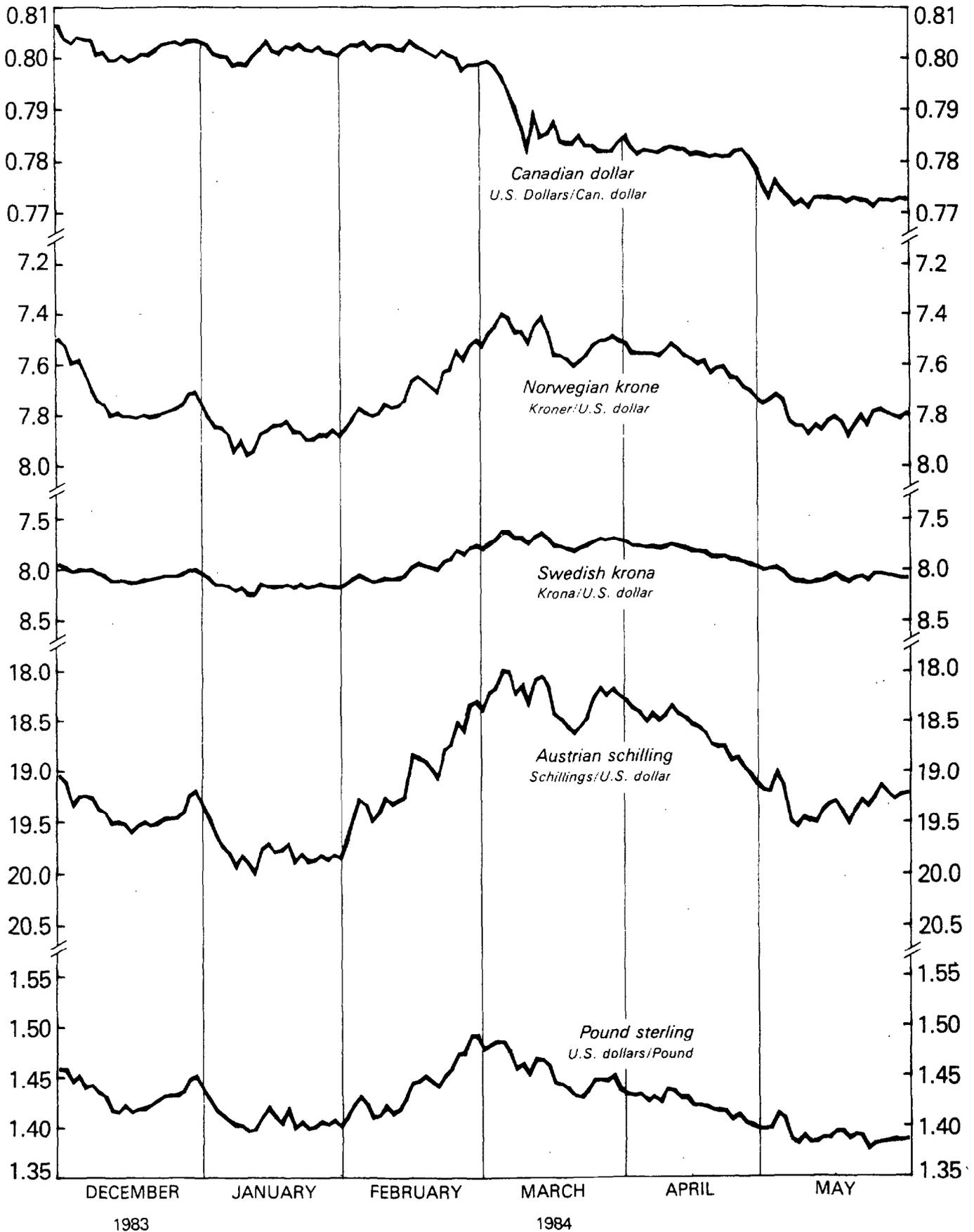
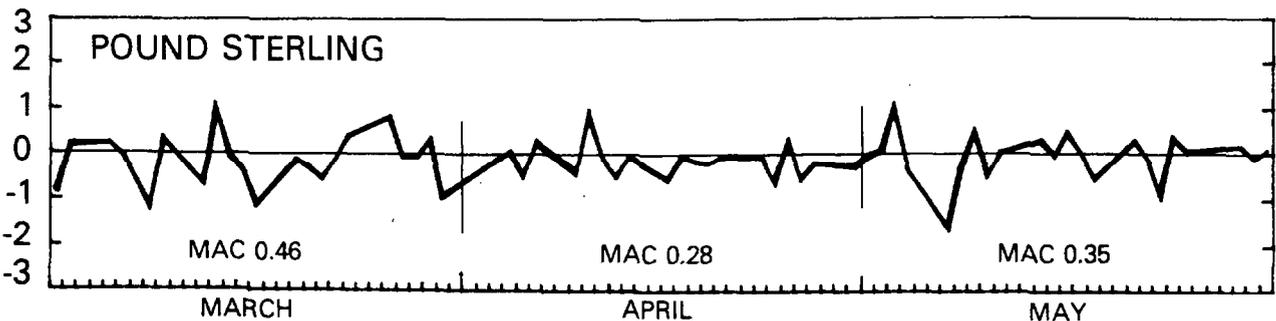
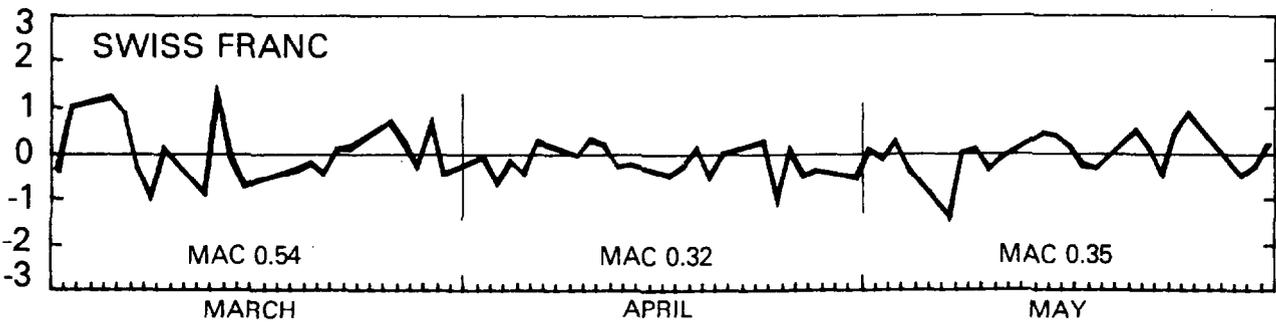
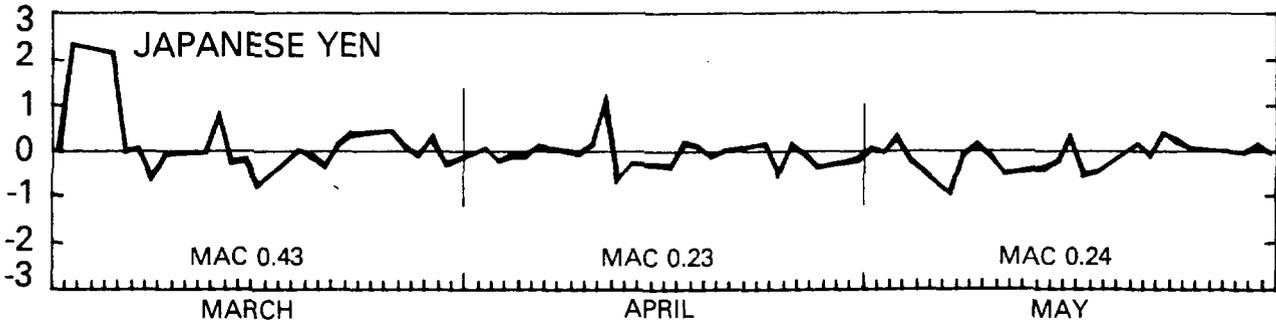
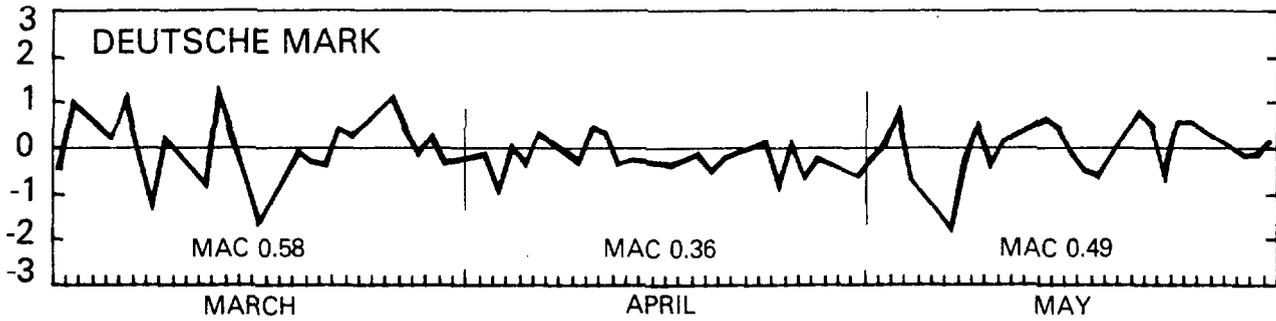
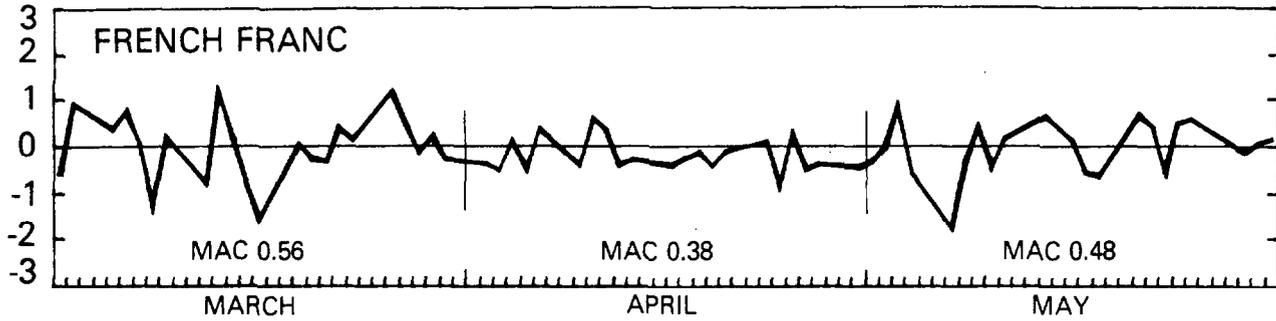


CHART 5 DAILY CHANGES IN SPOT EXCHANGE RATES

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



1984

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

CHART 6
INDEXES OF EXCHANGE RATES OF
FIVE MAJOR CURRENCIES AGAINST THE SDR
JUN. 1974 - MAY 1984
(June 28, 1974=100)

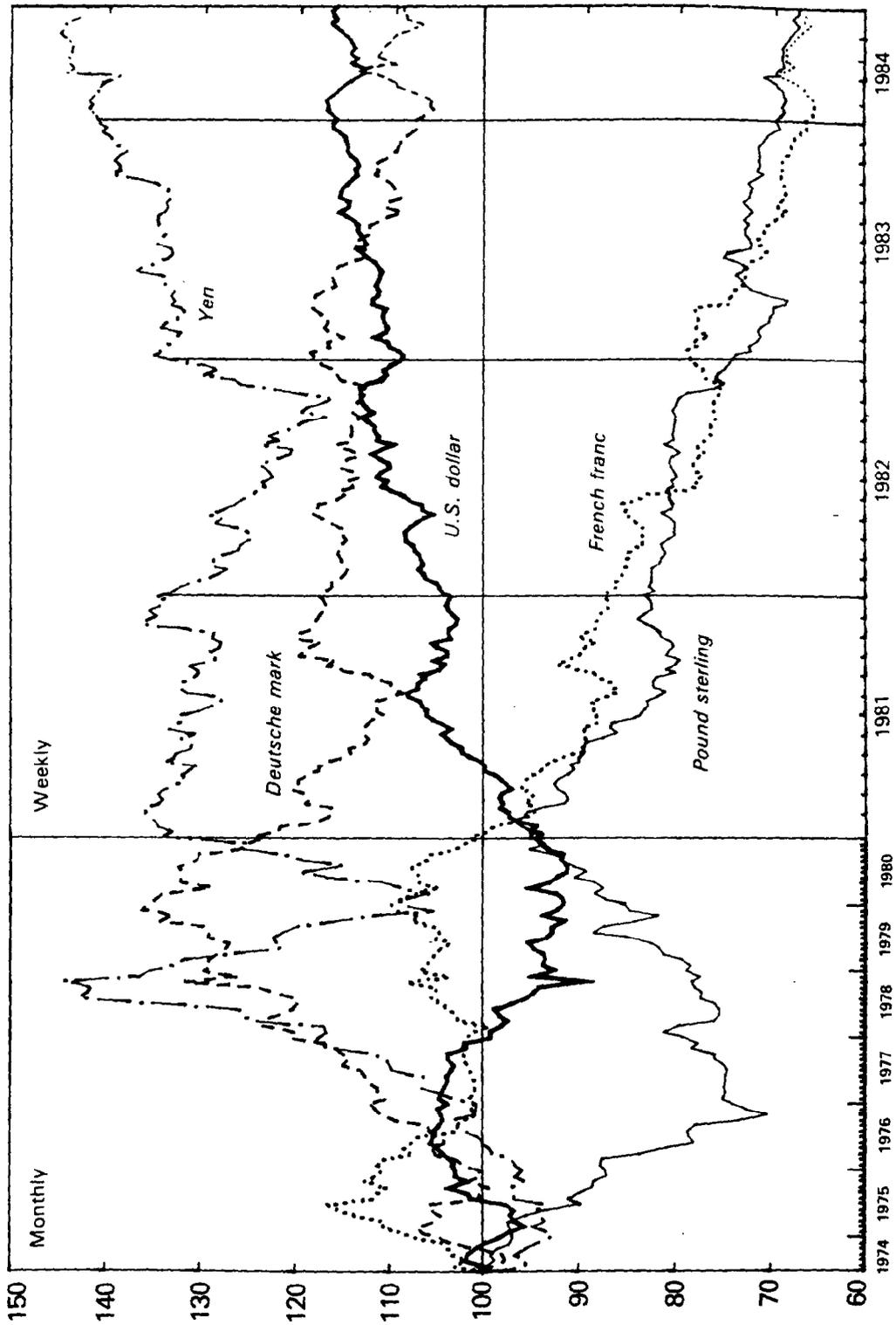


CHART 7 SHORT-TERM MONEY MARKET RATES

(Per cent per annum)

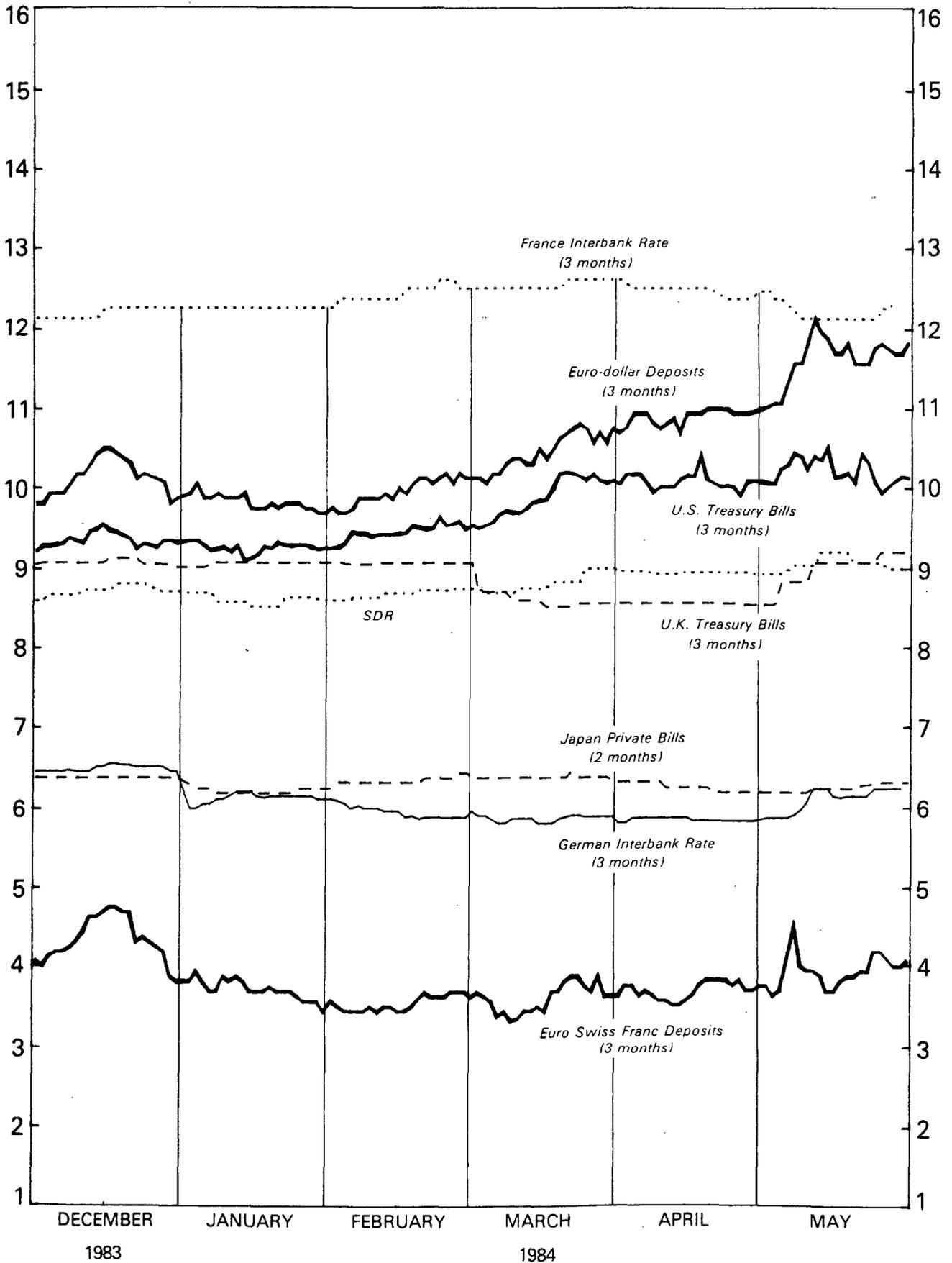




CHART 8
THREE-MONTH FORWARD RATES
Margins from Spot Rates based on noon quotations in New York
(Per cent per annum)

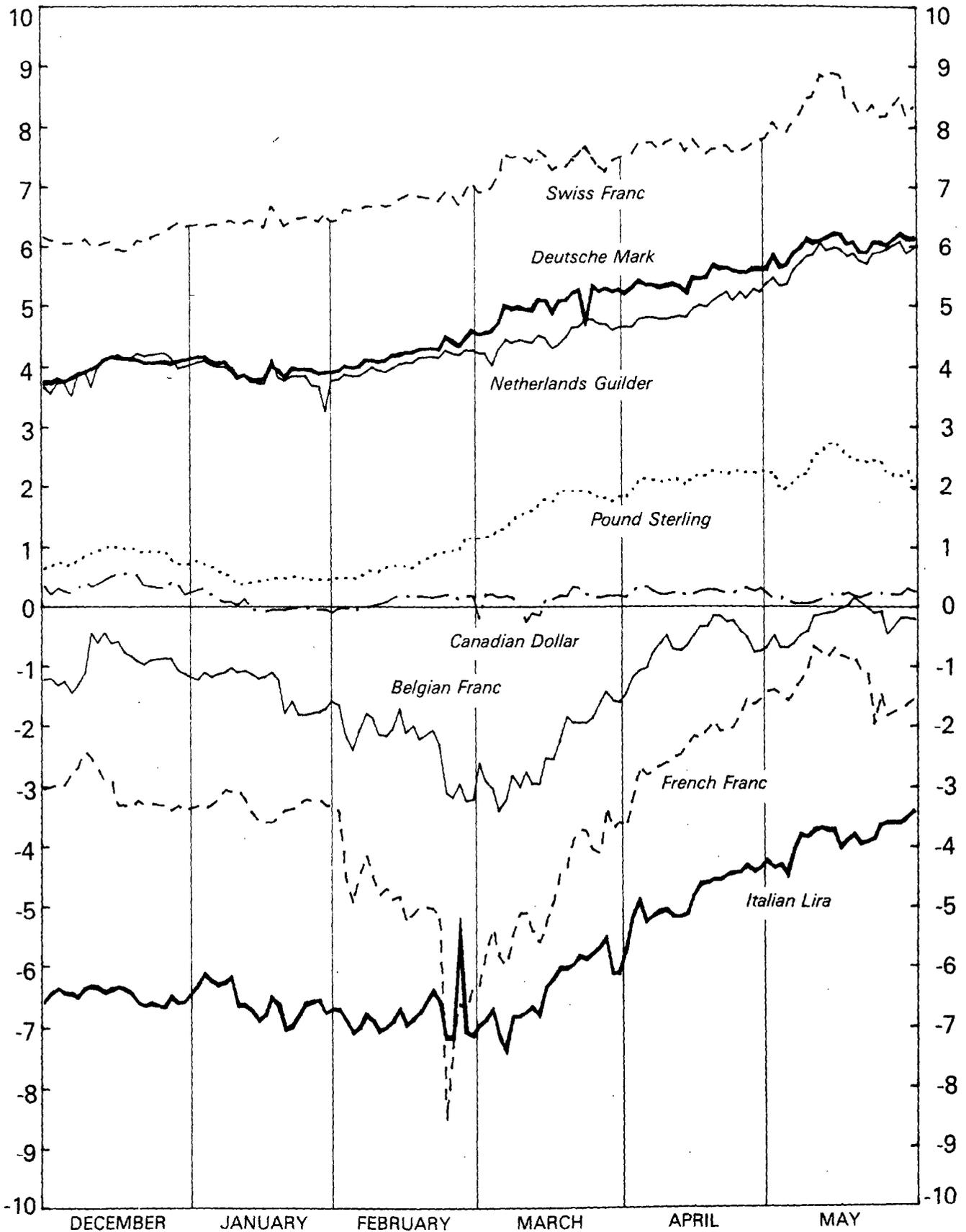
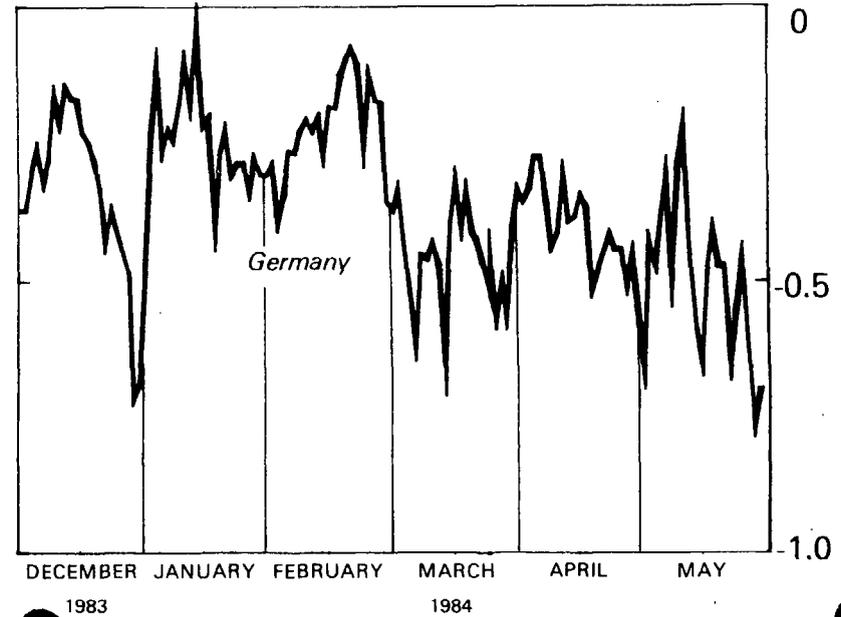
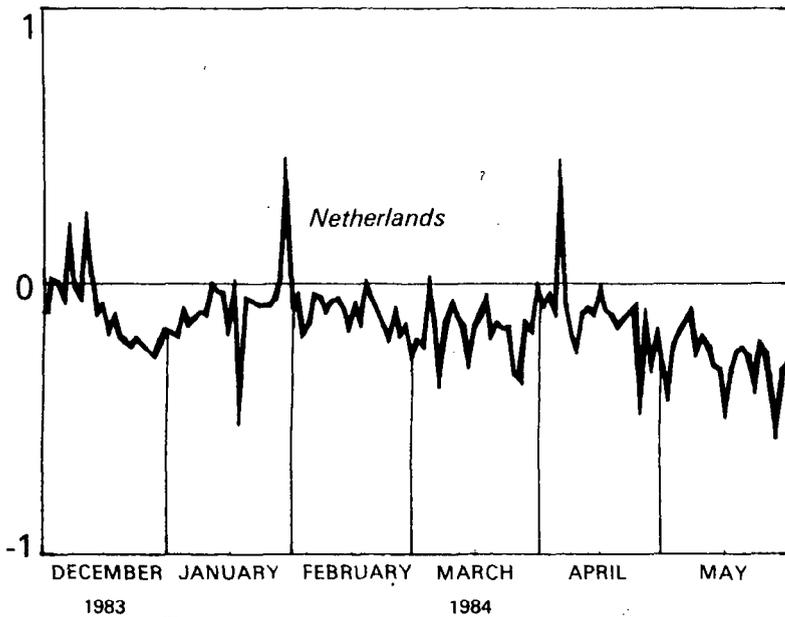
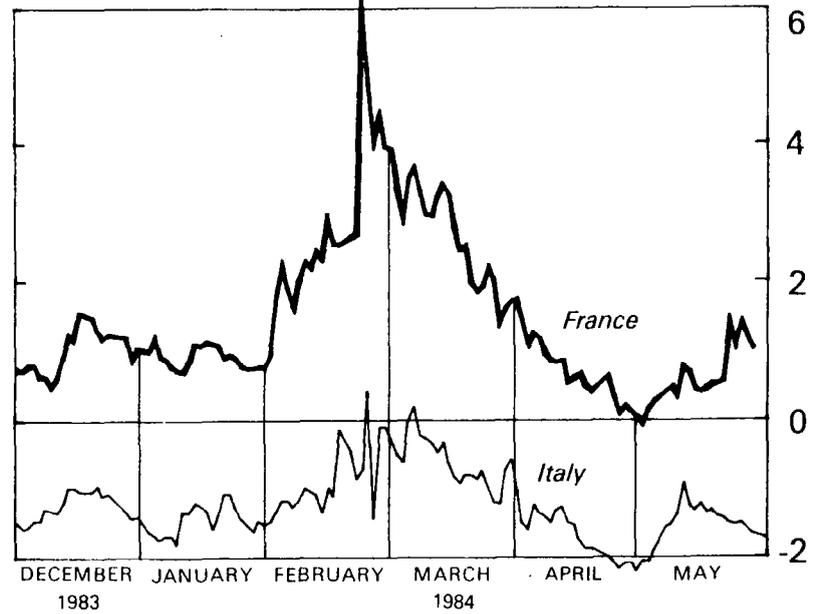
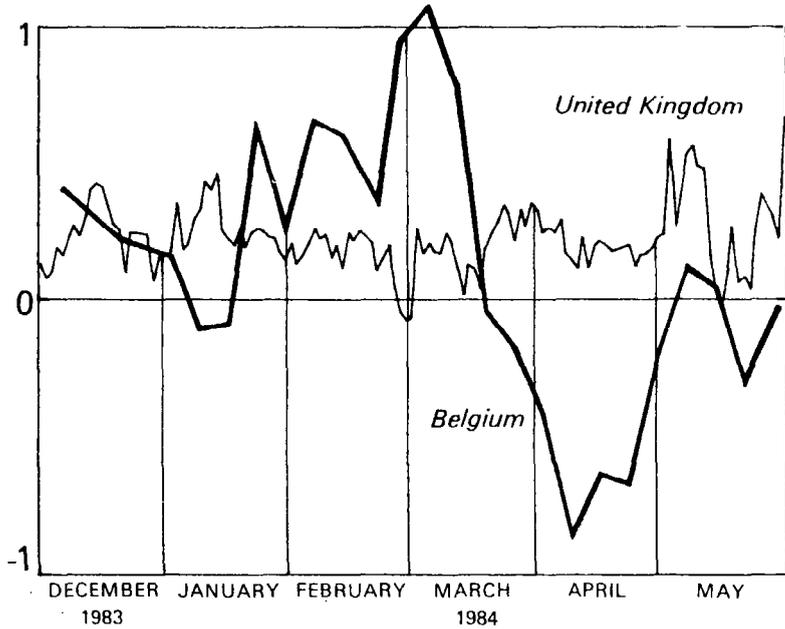




CHART 9

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, April-May 1984

	A p r i l				M a y				
	4	11	18	25	2	9	16	23	30
Austrian schilling	18.4200	18.3500	18.6300	18.8625	19.1950	19.4520	19.2800	19.3325	19.2200
Belgian franc									
Official	53.575	53.335	54.020	54.580	55.480	56.225	55.785	55.820	55.745
Financial	55.455	55.125	55.255	55.615	56.545	57.385	56.585	56.445	56.525
Canadian dollars	0.78140	0.78269	0.78104	0.78177	0.77271	0.77223	0.77271	0.77217	0.77265
Danish kroner	9.6310	9.5950	9.7263	9.8375	9.9810	10.1075	10.0235	10.1000	10.0485
Deutsche mark	2.62100	2.60875	2.64550	2.68000	2.72600	2.76750	2.74550	2.75800	2.73550
French francs	8.0538	8.0225	8.1438	8.2285	8.3725	8.4945	8.4225	8.4845	8.3988
Irish pounds	1.1673	1.1747	1.1577	1.1445	1.1240	1.1110	1.1217	1.1175	1.1205
Italian lire	1622.500	1614.00	1633.500	1655.000	1684.000	1707.500	1693.000	1695.500	1689.000
Japanese yen	225.300	222.650	224.750	225.550	227.000	228.835	231.050	232.320	231.440
Netherlands guilder	2.9565	2.9445	2.9865	3.0230	3.0695	3.1130	3.0845	3.1025	3.0808
Norwegian kroner	7.5545	7.5175	7.5862	7.6550	7.7360	7.8440	7.8025	7.8350	7.8095
Pounds sterling	1.4330	1.4365	1.4197	1.4119	1.3995	1.3894	1.3942	1.3770	1.3845
Swedish kroner	7.7785	7.7650	7.8413	7.9175	8.0000	8.1240	8.0490	8.1100	8.0845
Swiss francs	2.17075	2.16500	2.18980	2.21525	2.24720	2.27925	2.26725	2.27675	2.26425

^{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)

1983	National Money Markets 1/						Eurocurrency Markets 2/	Lending Rate 3/	Treasury Securities 4/							
	United States (1)	Germany (2)	United Kingdom (3)	France (4)	Japan average (5)	Weighted average dollar (6)				U.S. Dollar market (7)	Swiss franc (8)	London sterling (9)	French franc (10)	Japanese yen (11)	Swiss franc (12)	Libor 3 month (13)
June	9.14	5.65	9.85	12.81	6.64	8.62	9.75	5.33	10.00	12.45	6.55	5.00	10.05	10.50	10.00	11.00
July	9.46	5.65	9.69	12.25	6.72	8.76	10.07	5.18	9.99	14.15	6.54	4.81	10.31	10.50	11.00	11.00
Aug.	9.72	5.79	9.56	12.63	6.80	8.93	10.35	5.18	9.86	15.12	6.67	4.80	10.52	10.99	11.00	11.00
Sept.	9.36	5.95	9.41	12.61	6.86	8.72	9.70	5.27	9.66	14.71	6.81	4.81	10.29	11.00	11.00	11.00
Oct.	8.97	6.27	9.06	12.62	6.96	8.56	9.86	5.80	9.37	14.49	6.81	4.81	9.76	11.00	11.00	11.00
Nov.	9.11	6.38	9.03	12.50	6.38	8.57	9.86	6.07	9.32	13.56	6.43	4.15	10.00	11.00	11.00	11.00
Dec.	9.35	6.57	9.09	12.56	6.38	8.71	10.14	6.29	9.42	13.27	6.43	4.15	10.00	11.00	11.00	11.00
1984																
Jan.	9.75	6.71	9.06	12.42	6.12	8.59	9.84	5.98	9.45	13.45	6.55	4.71	10.09	11.00	11.00	11.00
Feb.	9.43	6.04	9.06	12.42	6.12	8.69	9.95	5.88	9.48	13.79	6.56	4.71	10.21	11.00	11.00	11.00
Mar.	9.88	5.96	8.41	12.72	6.38	8.95	9.95	5.66	8.98	13.55	6.38	4.62	10.21	11.00	11.00	11.00
Apr.	10.07	5.92	8.55	12.66	6.38	8.92	10.49	5.79	8.82	13.56	6.43	4.62	10.21	11.00	11.00	11.00
May	10.22	6.18	8.97	12.37	6.38	9.07	11.80	5.93	9.37	12.77	6.37	4.62	10.21	11.00	11.00	11.00
1983 Weekly																
June	9.90	5.54	10.07	12.77	6.81	8.51	10.59	5.79	10.36	13.97	6.75	4.91	10.41	11.00	11.00	11.00
July	9.10	5.71	10.15	12.80	6.81	8.64	9.75	5.49	10.25	14.46	6.56	5.00	10.05	11.00	11.00	11.00
Aug.	9.09	5.66	9.92	12.80	6.81	8.57	9.76	5.27	9.88	14.60	6.59	5.00	9.99	11.00	11.00	11.00
Sept.	9.33	5.63	9.58	12.85	6.81	8.69	9.84	5.27	9.88	14.71	6.59	5.00	10.11	11.00	11.00	11.00
1983 Monthly																
July	1	9.22	5.88	12.80	6.47	8.64	9.84	5.15	9.71	12.63	6.55	4.82	10.14	11.00	11.00	11.00
8	9.42	5.87	9.58	12.67	6.70	8.72	9.95	5.12	9.86	12.73	6.56	4.81	10.14	11.00	11.00	11.00
15	9.46	5.87	9.78	12.67	6.70	8.72	10.17	5.11	9.92	12.70	6.56	4.81	10.04	11.00	11.00	11.00
22	9.46	5.80	9.76	12.66	6.70	8.72	10.06	5.10	9.92	12.70	6.56	4.81	10.06	11.00	11.00	11.00
29	9.50	5.86	9.72	12.59	6.70	8.72	10.16	5.10	9.92	12.71	6.59	4.98	10.09	11.00	11.00	11.00
Aug.	5	9.79	5.72	12.62	6.76	8.94	10.50	5.19	9.97	13.11	6.67	4.82	10.21	11.00	11.00	11.00
12	9.91	5.94	9.56	12.61	6.82	9.05	10.21	5.25	9.82	12.99	6.65	4.82	10.13	11.00	11.00	11.00
19	9.71	5.75	9.56	12.61	6.82	8.92	10.21	5.26	9.81	12.99	6.65	4.82	10.13	11.00	11.00	11.00
26	9.52	5.73	9.55	12.63	6.81	8.93	10.09	5.31	9.77	12.93	6.65	4.82	10.13	11.00	11.00	11.00
Sept.	2	9.63	5.90	12.55	6.84	8.96	10.42	5.63	9.63	13.08	6.72	4.83	10.27	11.00	11.00	11.00
9	9.56	6.02	9.53	12.58	6.89	8.85	10.11	5.68	9.72	12.92	6.75	4.83	10.27	11.00	11.00	11.00
16	9.45	5.94	9.53	12.64	6.86	8.86	9.96	5.70	9.68	13.06	6.76	4.85	10.25	11.00	11.00	11.00
23	9.30	5.92	9.40	12.62	6.83	8.72	9.79	5.71	9.66	13.06	6.76	4.85	10.25	11.00	11.00	11.00
30	9.10	5.92	9.14	12.60	6.83	8.58	9.52	5.71	9.46	12.82	6.75	4.79	9.77	11.00	11.00	11.00
Oct.	7	8.95	6.27	12.74	6.83	8.56	9.3	5.64	9.41	12.68	6.71	4.94	9.69	11.00	11.00	11.00
14	9.16	6.28	6.02	12.76	6.83	8.63	9.12	5.61	9.32	12.89	6.58	4.02	9.85	11.00	11.00	11.00
21	8.96	6.27	6.04	12.57	6.89	8.51	9.56	5.76	9.26	12.43	6.43	4.17	9.75	11.00	11.00	11.00
28	8.99	6.26	6.04	12.54	6.38	8.42	9.05	5.61	9.37	13.16	6.42	4.16	9.84	11.00	11.00	11.00
Nov.	4	8.92	6.28	12.56	6.38	8.49	9.45	5.89	9.11	13.03	6.55	4.13	10.06	11.00	11.00	11.00
11	9.11	6.35	6.02	12.55	6.38	8.50	9.80	5.85	9.14	13.03	6.55	4.13	10.06	11.00	11.00	11.00
18	9.13	6.43	6.06	12.55	6.38	8.60	9.80	5.89	9.11	13.03	6.55	4.13	10.06	11.00	11.00	11.00
Dec.	2	9.43	6.52	12.32	6.38	8.64	9.46	5.71	9.12	13.06	6.68	4.15	10.09	11.00	11.00	11.00
9	9.22	6.55	6.02	12.29	6.38	8.76	10.31	5.86	9.32	12.91	6.61	4.21	10.31	11.00	11.00	11.00
16	9.45	6.58	6.09	12.34	6.38	8.79	10.39	6.43	9.49	13.11	6.61	4.21	10.31	11.00	11.00	11.00
23	9.35	6.61	6.11	12.42	6.38	8.73	10.29	6.33	9.51	13.24	6.67	4.25	10.46	11.00	11.00	11.00
30	9.31	6.56	6.03	12.42	6.38	8.76	9.92	6.43	9.39	13.44	6.61	4.21	10.21	11.00	11.00	11.00
1984 Weekly																
Jan.	6	9.30	6.11	12.42	6.25	8.66	9.84	5.91	9.39	13.46	6.68	4.18	10.24	11.00	11.00	11.00
13	9.21	6.24	6.08	12.42	6.19	8.57	9.80	5.98	9.51	13.11	6.33	3.81	10.14	11.00	11.00	11.00
20	9.23	6.24	6.02	12.42	6.19	8.58	9.76	5.90	9.45	13.01	6.31	3.76	10.02	11.00	11.00	11.00
27	9.28	6.24	6.02	12.42	6.23	8.61	9.79	5.94	9.45	13.18	6.38	3.63	10.02	11.00	11.00	11.00
Feb.	3	9.26	6.17	12.47	6.11	8.60	9.79	5.90	9.44	13.39	6.39	3.50	9.96	11.00	11.00	11.00
10	9.24	6.09	6.05	12.55	6.31	8.68	9.85	5.84	9.39	14.68	6.38	3.45	10.05	11.00	11.00	11.00
17	9.46	6.01	6.06	12.60	6.31	8.69	9.80	5.80	9.42	15.37	6.39	3.48	10.16	11.00	11.00	11.00
24	9.54	5.96	6.06	12.74	6.38	8.74	10.12	5.86	9.38	17.52	6.50	3.64	10.39	11.00	11.00	11.00
Mar.	2	9.53	5.98	12.70	6.40	8.73	10.12	5.81	9.24	17.24	6.59	3.64	10.44	11.00	11.00	11.00
9	9.64	5.92	6.68	12.67	6.30	8.72	10.27	5.82	9.02	16.16	6.59	3.64	10.44	11.00	11.00	11.00
16	9.79	5.91	6.53	12.67	6.36	8.79	10.36	5.76	8.96	15.93	6.44	3.43	10.25	11.00	11.00	11.00
23	10.14	5.95	6.53	12.75	6.40	8.99	10.67	5.73	8.89	15.06	6.37	3.29	11.04	11.00	11.00	11.00
30	10.10	5.96	6.55	12.81	6.37	8.92	10.66	5.63	8.95	14.72	6.29	3.27	11.00	11.00	11.00	11.00
Apr.	6	10.13	5.93	12.71	6.31	8.96	10.45	5.71	8.93	14.63	6.26	3.69	11.17	11.00	11.00	11.00
13	10.02	5.93	6.55	12.66	6.22	8.96	10.79	5.65	8.85	13.45	6.21	3.55	11.12	11.00	11.00	11.00
20	10.14	5.91	6.55	12.67	6.19	8.95	10.90	5.66	8.83	13.42	6.19	3.69	11.28	11.00	11.00	11.00
27	10.02	5.91	6.54	12.55	6.19	8.92	1.96	5.63	8.88	12.77	6.25	3.76	11.28	11.00	11.00	11.00
May	4	10.11	5.92	12.59	6.19	8.94	11.43	5.65	8.93	12.81	6.23	3.72	11.34	11.00	11.00	11.00
11	10.36	6.08	6.66	12.59	6.20	9.11	11.76	5.66	9.15	12.61	6.28	4.09	12.05	11.00	11.00	11.00
18	10.27	6.27	6.08	12.29	6.45	9.11	11.86	5.69	9.24	12.58	6.32	4.09	12.05	11.00	11.00	11.00
25	10.17	6.28	6.10	12.32	6.29	9.06	11.65	5.95	9.41	12.98	6.28	4.09	12.05	11.00	11.00	11.00

1. As of January 1, 1981, the combined market interest rate under the amended Rule F-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 F-1 and the value in terms of the SDR of a unit of that currency as determined by the Fund under Rule 0-22(a) and (b). The interest rates and the average live currency

