File- Monetary Policy Issues-Exchange Rate Intervention – Part D

Reference MG-MAMC/D/0002/001

File begins 04/01/1988

File ends 22/04/1988

Pages 76-95

discount rates at 2½%. In both inflation remains low (though rising slightly) but monetary growth remains a serious concern. In the absence of exchange rate concerns, both would probably like to see higher short-term rates. It seems most probable that an uneasy balance between external and internal factors will continue, with rates at current levels, so long as the US dollar remains vulnerable.

32. Prospects for US bond yields are as always hard to evaluate. US inflation still seems restrained, and with little sign of any wage response to the dollar depreciation, we continue to feel that inflation should be close to 5% in 1988. Against this, current yields of 8¼% at 4 years, and 9% at 10 years, offer a reasonable real return.

33. The US economy remains in serious imbalance, however. The trade deficit seems slow to respond to dollar depreciation and the fiscal deficit does not yet seem to be under credible control. While US demand remains robust the trade deficit will persist.

34. It is possible that the US will be able to continue to avoid recession and to finance continued substantial trade deficits, at the cost of repeated but controllable episodes of dollar weakness. In that sort of world, inflation would probably accelerate slowly in 1989 and beyond, and US bond yields might be expected to drift rather slowly upwards from (perhaps) the middle of this year.

35. Alternatively, US demand may be depressed rather sharply by one of several developments:

- an accelerated slowing in consumption, as consumers stop their accumulation of debt;
- a fresh round of financial turmoil, as markets despair about the trade deficit;
- a more serious attempt to address the US fiscal deficit, through tax increases and spending restraints.

In such circumstances, bond yields might prove rather volatile. We would expect the eventual out-turn to involve a weaker US demand growth, a lower trade deficit, lower inflation and lower yields; but if this came about as a consequence of the effects on confidence of financial turmoil, bond yields might well be sharply higher than now around the time of the crisis.

36. These considerations do not argue strongly for owning a net long position in US fixed income markets at current yields. They do however suggest that a sharp rise in yields should be seen as an opportunity to acquire a long position.

37. The prospects in Germany seem less uncertain. German growth and inflation seem likely to remain restrained, both expected to be rather over 1% in 1988. Against this, yields at about 6½% (at 10 years) look like excellent value. Dutch bonds continue to offer a reasonable extra return (about 1%) at the 4-5 year sector, since the Dutch yield curve is so much flatter than the German.

38. Rather similar considerations apply in France, where the authorities appear determined to resist inflation, now running at only 3.2%. Yields are around 10% at 10 year maturities, which seems reasonable compensation for the risk of depreciation against the DM (or, alternatively, for the rather higher French inflation rate). There are however political risks as regards the size of the likely realignment after the French election this Spring (at least 2%), and the future of fiscal policy.

39. We are investigating the desirability of establishing a portfolio of French government bonds. If the market appears to offer adequate liquidity, we recommend covering part of the proposed DM bloc program by buying French government bonds.

40. It is less easy to be sanguine about Japanese bond yields, given the intrinsic volatility of the bond market and the strains evident in the structure of Japanese equity and land prices. We

consider that present yield levels (about 5% at 10 years) are relatively sustainable; a sharp rise in yields would be a buying opportunity, and bonds should be sold if yields fall below 4½%.

42. We continue to feel that <u>Canadian dollar bonds</u> represent a reasonable investment, in view of their yield advantage over US bonds (currently about 120 basis points at 10 years, and around 200 basis points at 1 year). The Canadian dollar has appreciated against the US dollar, and continues to look a reasonable prospect. Yields are likely to continue to be strongly influenced by developments in the US.

<u>Recommendations</u>

42. Our view of the prospects suggests that something of a deflationary bias may emerge in the world economy. In those circumstances, the EEA should seek to be long fixed income markets overall; it is currently short, by $1.7 bn in 4 year equivalents.

43. While yields remain at current levels, we propose the following:
- a reduction in the short position in US Treasury notes and Federal Agencies by a maximum of $½bn (in 4 year net equivalents),
- the acquisition of Canadian $0.1 bn (in 4 year equivalents) of Canadian Government bonds,
- an increase in the long position in DM bloc securities by up to $¾ bn (in 4 year equivalents).

These acquisitions would be financed by running down the EEA's holdings of bank deposits, thus reducing the exposure to bank risk.

44. The effect would be to produce the following bond market exposures:

	December 1987	($ bn 4 year equivalents) Plan: June 1988
US dollars	-2.5	- 2.0
DM bloc	+0.3	+ 1.0
Yen	+0.5	+ 0.5
Canadian dollars	0	0.1
Total	-1.7	- 0.4

45. The above recommendations are on the basis of our central expectations. Should US yields rise sharply - say to 9½% at 4 years - we propose to purchase extra US Treasury securities for the reasons noted earlier. Conversely if 4 year yields were to decline - to below 7½% - we would propose to sell Treasuries and recreate a significant short position.

I Other Issues

46. Gold Although for the most part the price traded fairly narrowly in the range $450-500, investment interest in gold increased during the period. This interest was reflected in some increased demand for half-sovereigns, sales of which rose to 49,000 (at a premium of 15% over the gold content) despite the launch of the Britannia in October. There were no sales of sovereigns in the period.

47. EEA Issuer Limits. There were two changes to credit limits during the period. In July Moody's downrated Norway from Aaa to Aa1. Although Standard and Poor's maintained its AAA assessment, it was felt that a precautionary adjustment in the EEA's credit limit for bonds issued by this country should be made, and it was reduced from $750 mn to $250 mn. This change did not require any sales of bonds. The limit on holdings of World Bank bonds was fixed at $500 mn last autumn. A year later, following an increase in the overall level of reserves of over 50%, the limit was proving too small even to maintain exposures at neutral (benchmark) levels. The credit limit was reviewed in early October and it was decided that an increase to $750 mn was appropriate.

48. Investments Computer System. A paper describing our plans was sent to HMT in the autumn. Phase 1 - dealing principally with settlements and designed to provide a reliable database of transactions and holdings - was implemented in December, on schedule and within budget. Work on Phase 2 - to provide improved management information - is now under way.

49. German withholding tax is to be imposed in Germany in 1989, probably at a 10% rate (this is effectively a re-introduction: a coupon tax, which was similar but levied at 25%, was removed in October 1984). As a result, Euro DM bonds now yield less than German governments at long maturities (and only marginally more at 4 and 5 year maturities). It is probably not appropriate for the EEA to continue to own Euros in these circumstances, since it will probably be able (as last time) to reclaim tax; if so (and the law has yet to be drafted, far less enacted), we should seek to transfer the Euro-portfolio into rather more liquid governments, at a gain in yield. We need to approach the German authorities for clarification.

50. The EEA currently holds about DM 1.4 bn of Euros (in 4 year equivalents). Many of those were bought at an average spread of about 25-30 bp over German government bonds, in compensation for the loss in liquidity. The tightening of spreads offers the EEA the opportunity to move into Governments without reduction in yields, providing that the EEA's exemption is confirmed. It is probably sensible to start to do this now, ahead of confirmation; but to maintain a reasonable position in Euros against the possibility that Euros trade even further through governments on fears of a future higher rate of withholding tax, or on unforeseen difficulties in reclaiming tax.

51. It is worth noting that current circumstances offer the EEA a considerable profit - of DM 15-20 mn - on the past decision to hold Euros rather than just German government bonds (as most other central banks do).

Bank of England
15 January 1988

TABLE A

EEA ASSETS AS AT 31 DECEMBER 1987

TYPE		HOLDINGS US$ MNS.		TOTAL RESERVES		
US$:	CURRENT ACCOUNTS	927.8		2.09		
	TREASURY BILLS	4231.2		9.55		
	SHORT TERM PAPER	3922.8		8.85		
	EURO DEPOSITS (MARKET)	4450.0		10.04		
	EURO DEPOSITS (BIS)	* 3825.0		8.63		*3385 HELD O/A EMCF
	US TREASURY NOTES	2245.4		5.07		
	FEDERAL AGENCIES	1072.0		2.42		
	FRN'S	840.9		1.90		
	EUROBONDS	1063.8		2.40		
	CENTRAL BANK BONDS	36.4		0.08		
			22615.3		51	
CAN$:	CURRENT ACCOUNTS	131.3		0.30		
	TREASURY BILLS	12.9		0.03		
	GOVERNMENT BONDS	495.0		1.12		
	EUROBONDS	28.9		0.07		
			668.1		2	
DM:	CURRENT ACCOUNTS	30.5		0.07		
	TREASURY BILLS	63.7		0.14		
	EURO DEPOSITS (MARKET)	1920.1		4.33		
	EURO DEPOSITS (BIS)	1658.1		3.74		
	GOVERNMENT BONDS	2208.9		4.98		
	SCHULDSCHEIN	208.1		0.47		
	EUROBONDS	833.5		1.88		
			6922.9		16	
ECU	CURRENT ACCOUNTS	21.9		0.05		
	EURO DEPOSITS (MARKET)	204.6		0.46		
	EUROBONDS	53.9		0.12		
			280.4		1	
YEN:	CURRENT ACCOUNTS	25.9		0.06		
	EURO DEPOSITS (BIS)	39.2		0.09		
	EURO DEPOSITS (MARKET)	825.0				
	GOVERNMENT BONDS	451.9		1.02		
	EUROBONDS	422.5		0.95		
	TREASURY BILLS	0.3			0	
	FRN'S	4.9				
			1769.7		4	
DFLS:	CURRENT ACCOUNTS	1.9		0.00		
	EURO DEPOSITS (BIS)	12.0		0.03		
	GOVERNMENT BONDS	453.1		1.02		
	EUROBONDS	28.8		0.06		
			495.8		1	
SWFC:	CURRENT ACCOUNTS	3.9		0.01		
	EURO DEPOSITS (BIS)	55.0		0.12		
	EUROBONDS	29.8		0.07		
	CENTRAL BANK BONDS	12.9		0.03		
			101.6		0	
FF:	CURRENT ACCOUNTS	2.3				
	EURO DEPOSITS (MARKET)	745.9				
			748.2		2	
WORKING BALANCES			5.6		0	
CURRENCY TOTAL			33,607.6	72.3		

CONTINUED

GOLD ‡		7,240.1	16	‡ 1448 HELD O/A EMCF
SDR RESERVE TRANCHE	1,579.2			
BALANCE	1,228.6			
		2,807.8	6	
VALUATION DIFFERENCE O/A EMCF)		670.7	2	
		---------	-------	
GRAND TOTAL		44,326.2	100	
		=========	=======	

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PUBLIC SECTOR BONDS HELD OUTSIDE THE RESERVES - 41.6

FORWARDS BY CURRENCY	$ MNS	FORWARDS BY MATURITY	$ MNS
US$	4012 #		
CAN$	-1		
DM	2163	UP TO 1 MONTH [JANUARY 1987]‡	1093
YEN	133	UP TO 2 MONTHS [FEBRUARY 1987]	523
SDR	193	UP TO 3 MONTHS [MARCH 1988]	822
ECU	0	OVER 3 MONTHS	3416
~ OTHERS	25		
VALUATION OF EMCF	-671		
	---------		---------
	5854		5854
	=========		=========

‡ INCLUDES EMCF SWAP VALUATION DIFFERENCE OF -671
# EXCLUDES T/N'S AND FTD'S OF US$ 3385 PLEDGED TO BIS
~ EXCLUDES EMCF SWAP ECU'S

GOLD AND FOREIGN EXCHANGE OFFICE
14-Jan-88

		HOLDINGS US$ MNS.		TOTAL RESERVES		
US$:	CURRENT ACCOUNTS	1264.8		3.68		
	TREASURY BILLS	2844.2		8.28		
	SHORT TERM PAPER	2617.0		7.62		
	EURO DEPOSITS (MARKET)	4025.0		11.71		
	EURO DEPOSITS (BIS)	* 3525.0		10.26		*2225 HELD O/A EMCF
	US TREASURY NOTES	1309.0		3.81		
	FEDERAL AGENCIES	1016.2		2.96		
	FRN'S	862.7		2.51		
	EUROBONDS	796.7		2.32		
	CENTRAL BANK BONDS	36.4		0.11		
		---------	18297.0		53	
CAN$:	CURRENT ACCOUNTS	15.3		0.04		
	TREASURY BILLS	1.4		0.00		
	GOVERNMENT BONDS	277.9		0.81		
	EUROBONDS	9.1		0.03		
		---------	303.7		1	
DM:	CURRENT ACCOUNTS	52.3		0.15		
	TREASURY BILLS	25.1		0.07		
	EURO DEPOSITS (MARKET)	461.5		1.34		
	EURO DEPOSITS (BIS)	600.7		1.75		
	GOVERNMENT BONDS	1230.4		3.58		
	SCHULDSCHEIN	260.9		0.76		
	EUROBONDS	844.1		2.46		
		---------	3475.0		10	
ECU	CURRENT ACCOUNTS	8.1		0.02		
	EURO DEPOSITS (MARKET)	10.1		0.03		
	EUROBONDS	51.8		0.15		
		---------	70.0			
YEN:	CURRENT ACCOUNTS	37.8		0.11		
	EURO DEPOSITS (BIS)	39.2		0.11		
	GOVERNMENT BONDS	290.1		0.84		
	EUROBONDS	487.8		1.42		
		---------	854.9		2	
DFLS:	CURRENT ACCOUNTS	0.7		0.00		
	EURO DEPOSITS (BIS)	21.7		0.06		
	GOVERNMENT BONDS	178.2		0.52		
	EUROBONDS	28.5		0.08		
		---------	229.1		1	
SWFC:	CURRENT ACCOUNTS	6.1		0.02		
	EURO DEPOSITS (BIS)	55.0		0.16		
	EUROBONDS	51.1		0.15		
	CENTRAL BANK BONDS	12.9		0.04		
		---------	125.1		0	
WORKING BALANCES			8.0		0	

CURRENCY TOTAL			23,362.8	68.0		

	GOLD	*	7,240.2		21	* 1448 HELD O/A EMCF
	SDR RESERVE TRANCHE	1,796.1				
	BALANCE	1,479.7				
			3,275.8		10	
	VALUATION DIFFERENCE O/A EMCF		485.0		1	
			---------		-------	
GRAND TOTAL			34,363.8		100	
			=========		=======	

PUBLIC SECTOR BONDS HELD OUTSIDE THE RESERVES ...

F WARDS BY CURRENCY	$ MNS	FORWARDS BY MATURITY	$ MNS
US$	3021 #		
CAN$	31		
DFLS	44		
DM	960	UP TO 1 MONTH [JULY 1987] *	179
YEN	140	UP TO 2 MONTHS [AUGUST 1987]	473
SDR	187	UP TO 3 MONTHS [SEPTEMBER 1987]	571
		OVER 3 MONTHS	2674
OTHERS	-1 ^		
VALUATION OF EMCF	-485		
	3897		3897

* INCLUDES EMCF SWAP VALUATION DIFFERENCE OF -485

EXCLUDES T/N'S AND FTD'S OF US$ 2225 PLEDGED TO BIS

^ EXCLUDES EMCF SWAP ECU'S

GOLD AND FOREIGN EXCHANGE OFFICE

02-Jul-87

TABLE C

NON-DOLLAR CURRENCY ASSETS AND LIABILITIES AS AT 31.12.87

MNS

Year	DM bloc (a)		Yen		CAN$	
	A (b)	L	A	L	A	L
1988	13,292	378	173,508	4,916	218	29
1989	575	340	23,322	4,850	102	30
1990	673	523	8,722	4,212	205	30
1991	752	417	20,489	4,085	107	31
1992	722	1312	19,473	4,102	83	32
1993	851	465	10,147	4,062	28	32
1994	948	321	12,517	7,461	118	33
1995	895	306	7,208	2,344	19	33
1996	640	286	12,705	1,368	10	34
1997	471	276	4842	1,202	6	35
1998	35	202		278	7	36
1999		185		77		36
2000 onwards		389		102		211 (d)
TOTAL	19,854	5400	292,933	39,059	903	602
$equiv. (c)	12,409	3375	2,343	312	694	463
(Assets/ settled book cost at parity)	10,737		1,903		667	

(a) Includes DM, SWFcs, BFcs, Aus Sch, FFcs, and ECU, calculated at end December exchange rates.

(b) Assets calculated at market value.

(c) End-December exchange rates.

(d) Including deferrals of long-term debt.

TABLE D

US DOLLAR ASSETS AND LIABILITIES

as at 31.12.87

$ mns

YEAR	LIABILITIES (a)		ASSETS (b)					
	Fixed rate	Floating rate	LIQUID ASSETS	DEPOSITS & FORWARDS	TN & FA's	FRN's	EUROBONDS & CB BONDS	TOTAL ASSETS
1988	442	717	9,168	12,287	635	293	240	21,69[illegible]
1989	323	144			1,456	-	203	1,65[illegible]
1990	404	265			643	-	136	77[illegible]
1991	355	158			392	62	94	54[illegible]
1992	305	2,700			142	14	113	26[illegible]
1993	312	200			57	53	79	18[illegible]
1994	261	584			5	82	50	13[illegible]
1995	225	526			2		60	6[illegible]
1996	201	4,844			7	276	52	33[illegible]
1997	199	637			5		21	2[illegible]
1998	193	-				59		5[illegible]
1999	205	-						
2000 onwards	892(c)	-						
TOTAL (Assets/	4,317	10,775	9,168	12,287	3,344	839	1,048	26,68[illegible]
settled book cost)			9,082	12,287	3,174	841	1,100	26,44[illegible]

a) nominal

b) market value

c) including deferrals of long-term debt.

[illegible].O.B. 31.12.87

$mns Nominal

COUNTRY/INSTITUTION RISK

	Bonds	Short-term Paper & FRNS	Total
Australia	82	212	294
Austria	142	433	575
Belgium	48	443	491
Canada	104	15	119
Denmark	82	148	230
Finland	23	194	217
France	302	1565	1867
Germany	-	-	-
Italy	113	426	539
Japan	45	-	45
Malaysia	15	-	15
New Zealand	41	74	115
Netherlands	-	-	-
Norway	83	41	124
Spain	50	337	387
Sweden	193	627	820
US	7	-	7
ECSC	63	-	63
EEC	127	-	127
EIB	249	174	423
Eurofima	55	-	55
Euratom	8	-	8
Council of Europe	74	-	74
Asian Dev Bank	75	-	75
Nordic Inv. Bank	40	-	40
IADB	115	-	115
IBRD	481	-	481
IBRD CB	48	-	48
ADB CB	2	-	2
IADB CB	3	-	3
TOTAL	2670	4689	7359

Notes:

(1) Table excludes government bonds issued in that government's domestic currency.

(2) Non-dollar bonds are converted to US dollars at current parities as defined in Table 2 of the main paper.

US DOLLAR EXCHANGE RATES

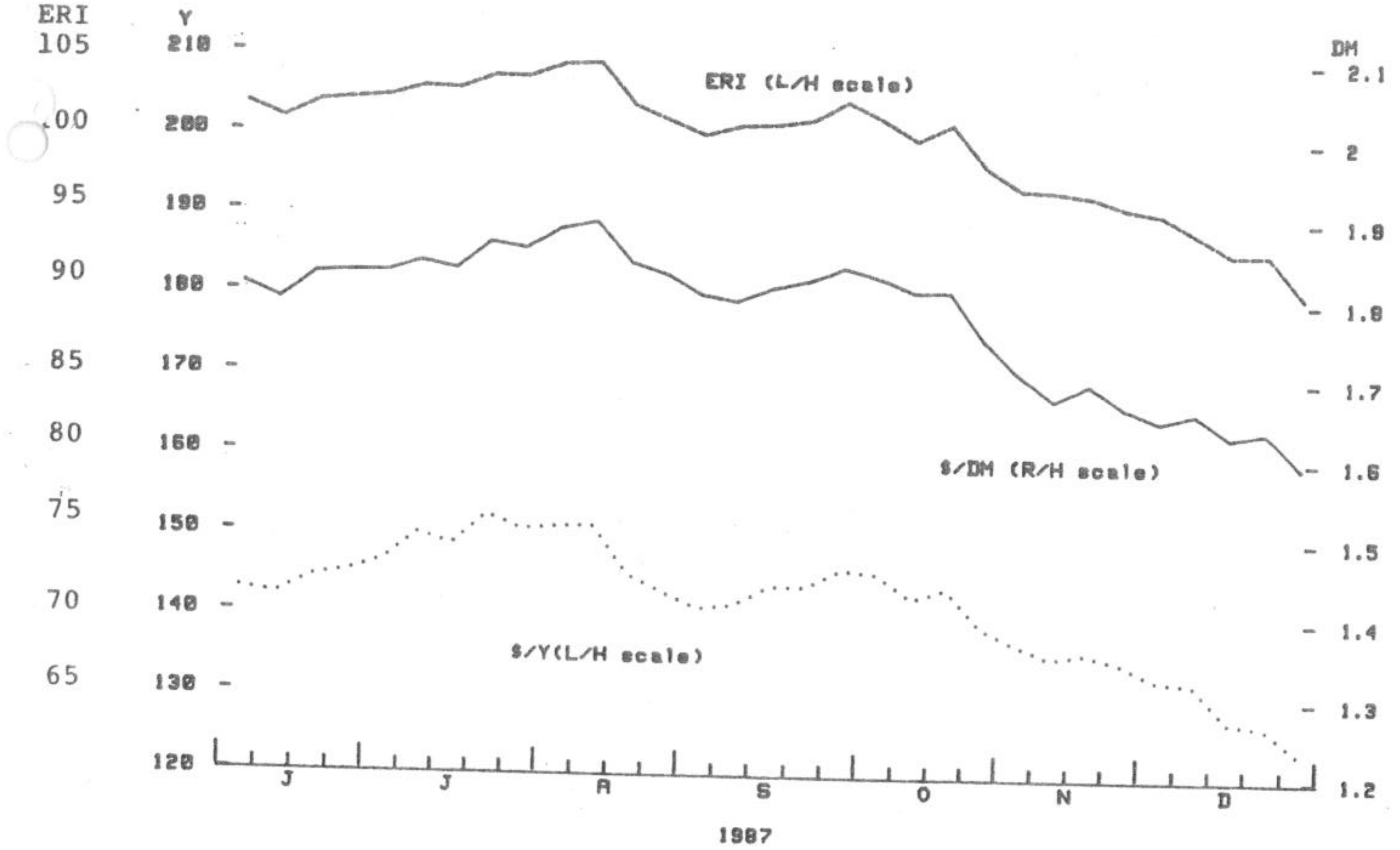


CHART 2

STERLING EXCHANGE RATES

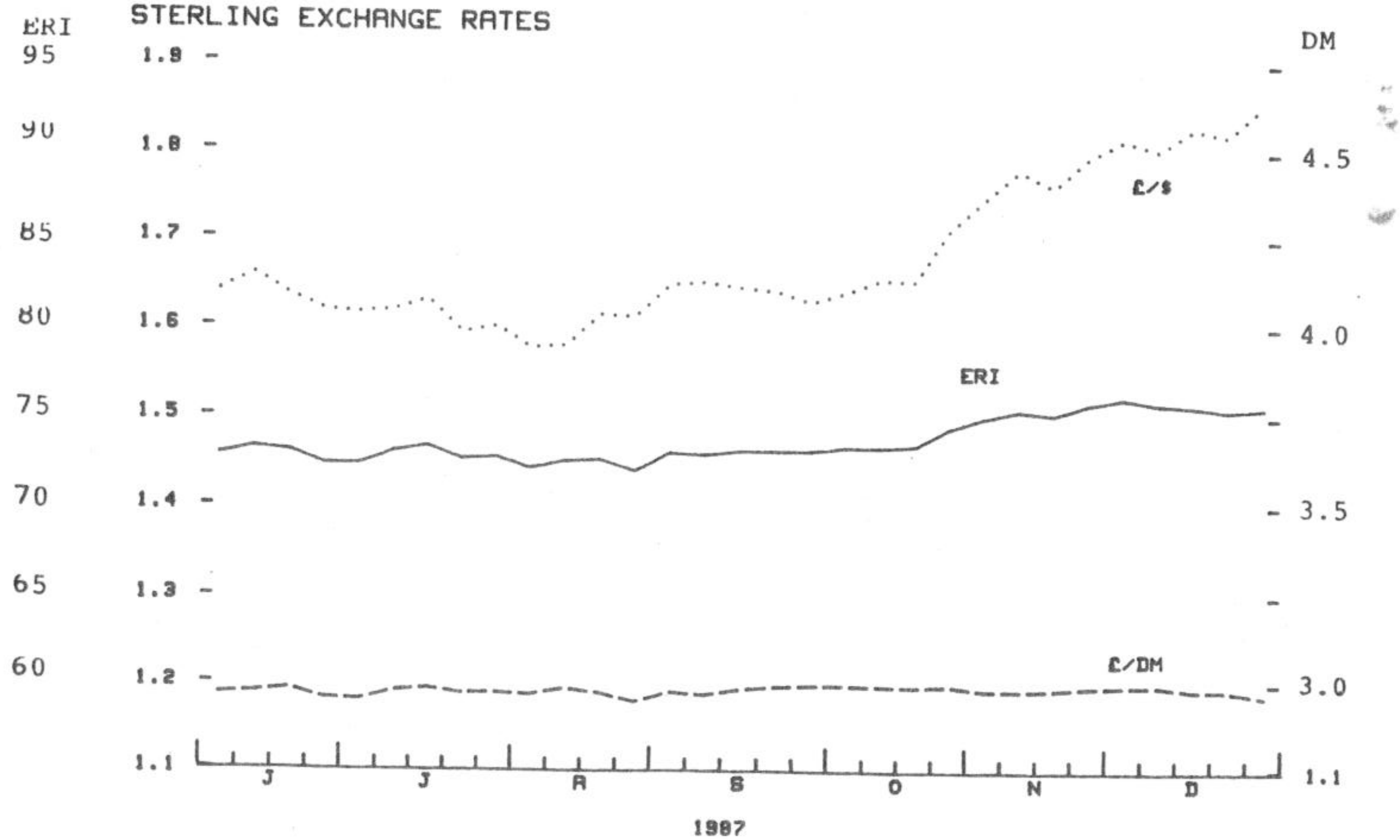


Chart 3

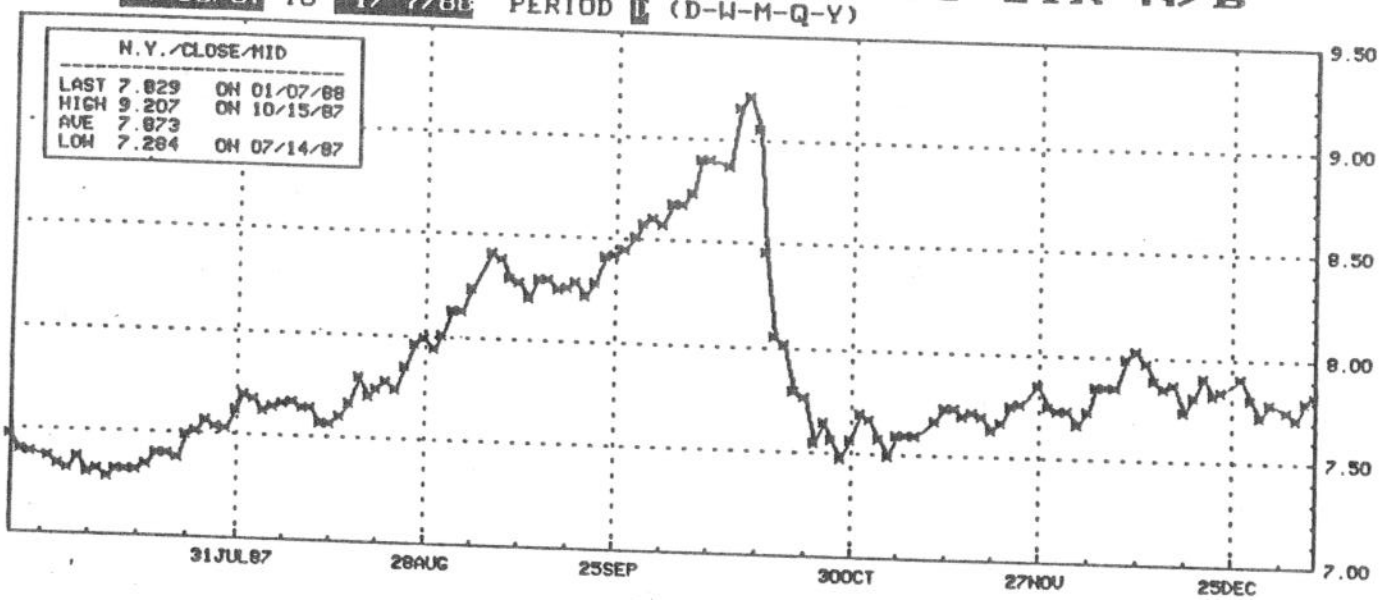
2 Year US Government Yields

GT2 Govt GY

Printer not ready. Govt GY

YIELD CHART for GENERIC 2YR N/B

RANGE 6/30/87 TO 1/ 7/88 PERIOD D (D-W-M-Q-Y)



THE BLOOMBERG

Chart 4

10 Year German Goverment Yields

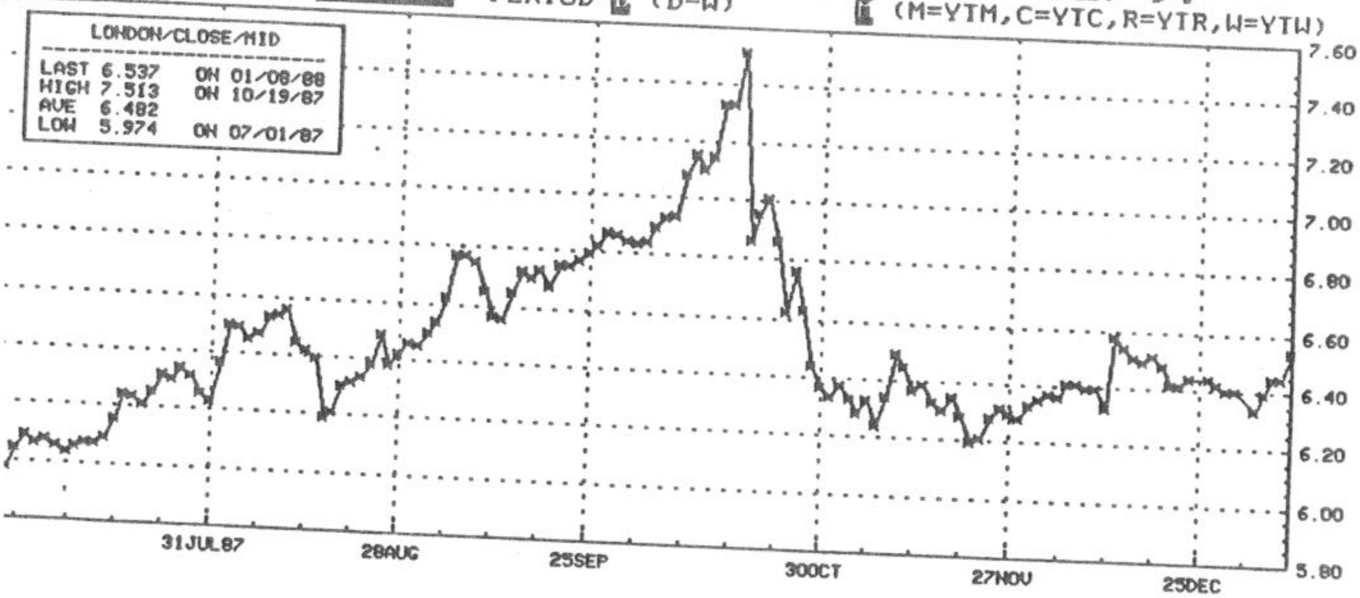
10 Govt GY

Printer not ready.

Corp GY

YIELD CHART for DBR 6 03/20/97

RANGE 6/30/87 TO 1/ 8/88 PERIOD D (D-W) Y (M=YTM,C=YTC,R=YTR,W=YTW)



THE BLOOMBERG

Chart 5

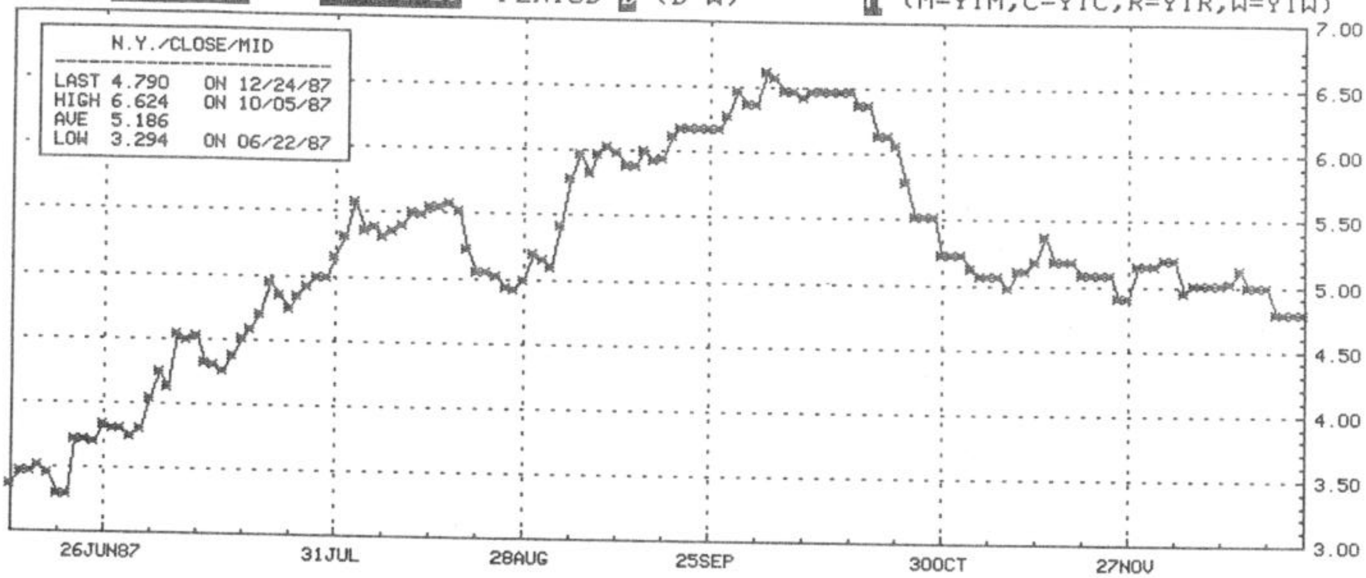
10 year Japanese Government Yields

11

Corp GY

YIELD CHART for JPN 5.1 07/22/96 NO 89

RANGE 6/12/87 TO 12/24/87 PERIOD D (D-W) M (M=YTM,C=YTC,R=YTR,W=YTW)



THE BLOOMBERG

92

MAMC: B3

D2

H M Treasury

Parliament Street London SW1P 3AG

Switchboard 01-270 3000

Direct Dialling 01-270 4369

28 January, 1988

Sir Geoffrey Littler KCB
Second Permanent Secretary

E.A.J. George, Esq.,
Executive Director,
Bank of England,
Threadneedle Street,
LONDON, EC2R 8AH.

Dear Eddie,

INVESTMENT OF THE RESERVES

We discussed your six-monthly review paper of 15 January at my meeting on 20 January, and I am writing to confirm the decisions we took. A more detailed note of the meeting will be circulated later.

2. We agreed that it was sensible to plan on the basis that the dollar was likely to fall further, with movements probably more sudden and sharp than the smooth progression projected in the forecasts. I agreed with your suggestion that the yen may well rise less than the DM. In the light of this we agreed your proposal that, at current exchange rates or if the dollar were to strengthen, and depending on market conditions, we should switch dollars first into yen and then a further amount into DM, up to a total of between $1½ billion and $2 billion. As you say in paragraph 20 of your paper, the scope for achieving this is likely to be circumscribed by political considerations, and we must take advantage of whatever opportunities arise to move in the desired direction.

3. We also agreed that if and when the dollar fell below DM 1.55 and ¥ 120 you should begin to lengthen the dollar position, and be prepared to switch progressively larger amounts at rates below those levels within a ceiling of $1 billion.

4. We agreed that you should acquire a French franc bond portfolio as proposed in paragraph 39; and, as circumstances allowed, acquire further écu deposits.

5. We also agreed to do what we can to reduce further the exposure to bank risk, although the position has already improved somewhat since the end of 1987. It would help in this respect if we were to decide to call the $2½ billion FRN this October, and thereby reduce our gross dollar holdings. You explained that at present this looked like the right decision to make on cost grounds. Although a final decision need not be made until the summer, we agreed it would be sensible to consult the Chancellor in the late spring, at the same

SECRET

i e as taking his mind again on the proposal for a sovereign note programme.

6. You explained that the yield gap between US Treasuries and bank deposits was greatest at short maturities, so that to the extent you switch out of dollar bank deposits it might be sensible to buy longer maturity Treasury bills. That apart, we agreed that at current yields you should seek to reduce the EEA's overall short position in fixed interest markets, principally by lengthening the long position in DM markets, as envisaged in paragraph 43 of your paper. If yields rise sharply we should be prepared to increase interest rate exposure further, and if they fall sharply we should reduce interest rate exposure, as proposed in paragraph 45.

7. I said I hoped to let the Chancellor have a note shortly about our gold holdings, on the basis of the draft that was prepared some months ago, once this has been updated.

8. We discussed how best, and when, to approach the Germans about whether or not they envisaged their new withholding tax would apply to sovereign holders. We agreed that as a first step we would ask the Bonn Embassy to let us have details of what the current proposals are. We have done this, taking advantage of a visit to London by Adrian Thorpe from the Embassy. If necessary, I will have a word later on with Tietmeyer, if that seems appropriate.

9. Finally, we touched on two other points not covered by your paper:-

(i) we agreed that we need to develop better measures of profitability and changes in value of the reserves, in sterling terms. You said it would take some time to incorporate anything sophisticated into the EEA computer system. We agreed to see what could be done in advance of that. Messrs. Foot and Page are to give urgent thought to this, and will discuss with us what would be sensible and feasible;

(ii) as I told you, we have had an informal approach from the NAO about the way the EEA accounts are certified at present. We discussed various possible changes in the arrangements, agreeing that it was in any case too late for any changes to be made to apply to the 1987-88 accounts. We are due to have a further word about this next week, after which we in the Treasury will explore further with the NAO precisely what they are looking for.

And thank you again for an excellent paper

Yours,

Geoffrey

GEOFFREY LITTLER

FROM: H C GOODMAN

DATE: 29 January 1988

MR BATT
MR COURTNEY
MR PAGE - B/E
MR LINDLEY - B/E
MR SMEETON - B/E

cc: Sir Geoffrey Littler
Mr Peretz
Mr Grice
Mr Ilett
Miss O'Mara
Mr Carr
Mr Nelson

THE EXCHANGE EQUALISATION ACCOUNT's HOLDINGS OF GOLD

We have an outstanding remit to write to the Chancellor about the EEA's holdings of gold. Sir Geoffrey Littler decided at a meeting concerning the Investment of the Reserves last week that he would like to do this within the next few weeks. He would like to put up the paper prepared by Messrs Courtney and Ilett 18 months ago under a covering note himself.

However it will be necessary to update the original paper and I would be very grateful for your help in this. I attach a copy of the paper, for those who need it. I would be grateful for contributions as follows:-

Paragraphs 1, 2	- Mr Page.
Paragraphs 3, 7, 8, 10 and 12	- Mr Courtney
Paragraph 20	- Mr Lindley
Paragraph 21	- Mr Batt - to cover Baker, commodities index etc.
Paragraph 23	- Mr Page/Mr Smeeton
Paragraph 24	- Mr Page
Table 1	- Mr Smeeton
Table 2	- Mr Smeeton
Table 3	- Mr Page
Table 4	- Mr Page/Mr Courtney.

If you are not happy with the way I have allocated this please let me know as quickly as possible. I will be grateful to receive contributions by close on 18 February.

The arguments in the paper are little changed. It was concluded then that, if anything, our gold holding should be reduced. In the event, the subsequent rise in our foreign currency reserves has produced this result in proportionate terms. The decision of the World Bank not to sale its gold holdings at this stage means moreover, that there are no other foreseeable market complications. So, I do not anticipate that the paper will need any significant re-drafting.

HC Goodman

H C GOODMAN