ago, a relatively small kick would have been sufficient to set the last week's events into motion. Blumenthal and the British gave it a great deal more than that.

Swiss Shift

On the other side, Swiss National Bank President Fritz Leutwiler called reporters in Thursday and accused the U.S. Administration of intentionally trying to depress the dollar's rate, calling on them to support their currency instead. This marks a 180 degree shift in line for the Swiss central banker, who warned last month that the Swiss would not act to bail out the U.S. fund. Leutwiler's unusually strong statement probably had some calming effect on the foreign exchange markets Friday, when some traders wondered that the dollar had not been hit even harder than it was in continental markets. There have been unconfirmed reports from very good Western European banking sources that the European central banks, and the Fed, acted jointly to intervene to support the dollar and also to persuade commercial banks to stop speculating against it. There are also strong predictions from very good banking sources both in New York and Europe that the Europeans will impose exchange controls shortly to stem the inflow of dollars into their credit systems. If there were indeed such mitigating actions, beyond the expected level of central bank reaction, their significance will be relatively minor in the overall scope of events.

A senior official at Bank of America commented, "The only people who benefit from this are the British." Sterling's strength this week despite the sharp rise in dollar interest rates indicates that a new ball game is underway for the sterling-dollar relationship. "There's been no direct reaction on the London market to the rise in dollar interest rates," said Peter Buer at Arnhold S. Bleichroeder and Company in New York. "There is no longer a direct relationship between sterling and dollar interest rates. The hot money that has flown into sterling will remain there, and keep rates at 5 to 5.5 percent," Buer added, even though dollar rates have risen higher. "A rise in dollar rates will have a positive not negative effect on sterling."

The explanation for this unnatural situation is that since the rise in dollar rates is a side effect of foreign exchange speculation against the dollar, funds will hedge against the dollar by moving into sterling.

On top of the short-term developments, the dollar is weakening on fundamentals. Comparing Jan.-Aug. 1976 with Jan.-Aug. 1977, the U.S. balance of trade surplus on manufactures collapsed from $9.5 billion to $3.3 billion.

British 'Boom' May Be Bust

The expected increase in the money supply and the continued inflow of short-term funds into the city of London has stirred fears even within that complacent community that the "British boom" is far from stable. As the Oct. 11 Financial Times *noted, the gilt (government paper) market weakened in the beginning part of this week "following cautionary weekend press comment that the upsurge may be nearing its end and pointing to the problems facing the authorities in the wake of the recent heavy demand for sterling." Below are extracts from the London news alluded to by the* Times.

Daily Telegraph, Oct. 8—In the "City Comment" column entitled "Gilt market starts to look dangerous,"the *Telegraph* points to the danger of massive foreign intervention in the gilt market during recent international euphoria over the pound. "These overseas buyers have suddenly become convinced that the pound is a hard currency, and that it must appreciate as North Sea oil swings our balance of payments into massive surplus...The danger is that this foreign interest is fickle. Foreign investors on the whole do not know much about the London fixed interest market. Their buying is indiscriminate. They have been caught up in a swing in international fashion which for the time being favours Britain. All of which the more experienced
worrying. When newcomers take over a market, they normally drive prices to absurdly high levels. Then prices crack and fall very sharply. The fear is that we could soon see something of this sort happen in the gilt-edged market. . ."

Sunday Times, Oct. 9 — *Sunday Times* Business-news editor Kenneth Fleet writes in his weekly column that now is the "Time to Start Selling Gilts," suggesting that the foreign investors in London may soon start to leave the market. Of discussion of Chancellor of the Exchequer Denis Healey's speech at the recently concluded Labour Party conference, Fleet comments, "I would have felt distinctly uneasy that the vivid manifestations of socialist success are a boom on the Stock Exchange and a huge inflow of hot money from overseas. I would not have been reassured but the Chancellor's boast, made surely in cheek, that record reserves meant 'we can thumb our noses at the financial speculators.' The gnomes have made sterling suddenly a strong currency and stimulated gains in the gilt-edged market of perhaps £10 billion in a year. If for any reason, they make for the exits, I suspect Denis's thumb will be in his mouth rather than up his nose..." Calling the possibility of hot money outflows the "two billion pound question," Fleet argues that Wall Street may well be on its way to recovery, raising problems for the London markets. While no immediate drop in the gilt market is expected, he concludes that "I would not rule out further gains, though on a much more modest scale than in the past two months. But I would let others enjoy the final assault on the summit and the view from the peak. In three months, those looking back on the profits they took in October will be congratulating themselves on their perceptiveness."

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