FOREIGN EXCHANGE

Dollar's stability is deceptive

"It makes no sense whatsoever," remarked several West German and New York foreign exchange traders on the puzzling stability of the U.S. dollar at roughly 1.86 deutschemarks for the week of February 19-23. Events much less disheartening than any one of the week's news developments — seizure of the U.S. Embassy in Iran, the murder of the U.S. envoy to Afghanistan, a 7 percent plus rise in the price of oil — have laid the dollar low periodically for over two years.

The simple explanation is that the gnomes of London, who, as we reported last issue, have been systematically selling the dollar, opted during the week of February 19 to calm the markets for the short term. Their objective was political. First, the British desire to give critical support to Federal Reserve Chairman G. W. Miller's insistence that his 19th century-style high-interest rate program can stabilize the dollar. (see "Credit Markets")

Second, the British government's strategy to disband the new Franco-German European Monetary System, which formerly centered on destabilizing the dollar to prevent its linkage to the EMS, is now more broadly "geopolitical." Britain reserves the right, as Bank of England Governor Sir George Boulton told the Institute of Bankers Jan. 17, to stop the EMS by such Iranian-modeled turmoil in Europe's trading partners that France and the Federal Republic are themselves weakened.

In Sir George's words:

"The Moslem world is rapidly moving into a condition of religious civil war, and no matter who controls the Gulf, the supply of oil, not only from Iran, will probably shrink. In these circumstances, business over most of Africa and the Middle Eastern countries will suffer and consequential defaults and bankruptcies will multiply. Western Europe will be affected by the rising price of oil exacerbated by shor-

GOLD

A pause in the gold rush

With the Chinese-Vietnamese war placing the world on the brink of World War III, one would expect the price of gold bullion to go through the roof. Instead, the price has oscillated in the $240 to $250 an ounce range during the last week and has failed to retain the $254 record peak reached on Feb. 8. Why?

First, and most important, a political decision was made in London and New York during the last couple of weeks to permit a temporary stabilization of the U.S. dollar on world currency markets (see Foreign Exchange). The dollar's relative strength is based on the rigged oil price rise and supply shortages to which the economies of Western Europe and Japan are much more vulnerable than that of the U.S.

Second, London sources report that the Soviet Union, the world's second largest gold producer, sold small amounts of gold on the Swiss market in the last few days. This was reportedly the first time that the Soviets have sold any gold since October 1978. The USSR is known to be an extraordinarily adept trader and generally manages its gold sales so as not to lower the market price. However, the occurrence of new Soviet sales just before the U.S. Treasury auction (scheduled originally for Feb. 20 but postponed due to weather) has caused traders to be somewhat cautious. The Treasury is auctioning 1.5 million ounces each month as part of the Nov. 1 dollar-support package compared to only 300,000 ounces earlier in 1978.

Third, other precious and industrial metals have advanced sharply, diverting investor attention from gold (see Commodities). February-delivery silver, for example, rose over 35 cents to a record high of $7.9870 on the Chicago Board of Trade on Feb. 21. At the beginning of February, silver was trading for less than $7.00.

—*Alice Shepard*