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CAPITAL MARKET DEVELOPMENTS ABROAD

I. Germany: Money and Capital Markets During March

After a prolonged period of high liquidity, the money market tightened in late February and early March because of the impending March 10 deadline for major tax payments. Later it eased, partly because of easing actions on March 3 by the German Federal Bank, but even more because of the renewed inflow of funds from abroad after the March 6 revaluation of the deutsche mark. In a renewed effort to discourage such inflows, the Bank reduced reserve requirements again on March 8, and lowered further the rate at which it stands prepared to sell Treasury bills to the market; by March 23 the yield on 90-day Treasury bills was down to 2 5/8 per cent.

Although the foreign exchange markets were calmer in the last half of March than during the hectic week after revaluation, they remained unsettled as large amounts of funds continued to flow into Germany.

On the bond market, the confident tone that had prevailed in January and February continued throughout March. The strengthening of bond prices produced a decline in long-term interest rates during the month. The index of industrial bond yields, which in January dropped below 6 per cent for the first time since late 1959, continued to decline in February and March.

Share prices tended upward in the latter part of March to levels only slightly below those prevailing just before revaluation. Money market ease and rising dividends gave the market a lift. Non-resident funds which after the revaluation had moved into other continental countries whose currencies were rumored for possible revaluation flowed back into German shares before the end of March. These funds may have moved back to Germany in the hope of a possible further upward revaluation of the mark, but by the end of the month were expected to stay in the German shares so long as market opportunities remained attractive.

Money market. Prior to the major tax payment deadline of March 10, the German money market was relatively tight, a change from the comparative ease prevailing during most of February (See Chart 4). After March 10 the market eased somewhat and remained so for the rest of the month. In an anticipatory move to guard against an end-of-month (pre-Easter) rise in circulation and renewed tightness in the market, the Federal Bank on March 8 lowered reserve ratios (retroactive to March 1) for the third time since January 20. The three reductions released an estimated DM 1.2 billion ($300 million) of reserves to the commercial banks. Twice in February and four times in March the Federal Bank also lowered its selling rates on Treasury paper and restored part of previous cuts in the rediscount quotas of the commercial banks. A further reduction in reserve requirements on April 6 was expected to relase an additional DM 400 million to the banks.

Since last November (1960) the German Federal Bank has pursued an active policy of pushing down Treasury bill rates (See Chart 4). At that time, the Bank changed from a restrictive credit policy to one of easing interest rates in order to narrow the international differential that had contributed to the continuing large inflows of funds. Bill rates were lowered by a total of 3/8 per cent in two moves on successive days in early November and by another 1/2 per cent after the November 11 reduction of the discount rate from 5 to 4 per cent. In eight further steps from November 11 to date, bill rates have been reduced by an additional 1-1/2 per cent and the discount rate was further lowered to 3-1/2 per cent on January 20.1/

From		60-90 days Treasury bills	6-month Treasury bonds
1960	Nov. 11	4.00	4.25
	Dec. 20	3.75	4.00
1961	Jan. 20	3.25	3.50
	Feb. 9	3.13	3.38
	Feb. 14	3.00	3.25
	Mar. 3	2.88	3.13
	Mar. 8	2.75	3.00
	Mar. 17	2.63	2.88
	Mar. 23	2.50	2.75

Money market rates in Frankfurt declined throughout the month. In the Frankfurt market day-to-day money declined over the month from 3.88 - 4.25 per cent to 2.50 - 3.00 per cent. Declines over the same period for 30-day money were from 4.00 per cent to 3.38 per cent, and for 90-day money from 4.00 to 3.38 per cent.

Frankfurt Money Market Rates

	Day-to-day money Lowest rate	Day-to-day money Highest rate	one-month loans	Three-month loans
1960				
December (monthly range)	3.50	5.13	5.25 - 5.75	5.00 - 5.13
1961				
January (monthly range)	3.00	4.75	4.13 - 4.50	4.50 - 4.88
February (monthly range)	2.63	4.13	3.75 - 4.13	3.88 - 4.38
March (weekly range) 1-7	3.88	4.25	3.75 - 4.00	3.88 - 4.00
8-15	2.88	3.88	3.50 - 3.75	3.63 - 3.88
16-23	2.63	3.00	3.38 - 3.50	3.50 - 3.63
24-31	2.50	3.00	3.38 - 3.50	3.38 - 3.50

1/ Treasury bill rates are the rates, set by the Federal Bank, at which the Bank stands ready to sell government paper in the open market. Frankfurt money market rates, on the other hand, represent commercial bank lending rates to private individuals or institutions; these rates are not fixed or quoted officially, but are reported by the commercial banks and may be considered to be representative.

As a result of money market tightness in early March, the gap between short-term yields in the United States and Germany widened, as compared to the end of February. The gap then narrowed during most of March rising slightly in the last week of the month. The spread between German 3-month Treasury bills and 90-day U.S. bills has narrowed steadily since the end of last year.

	German 3 mos. lending rate	U.S. bill rate	Spread over U.S.	Forward exchange discount (-), premium (+) as per cent per annum[2]	Net incentive on covered basis
1960					
Dec. 30	4.25	2.20	2.05	-1.58	.47
1961					
Jan. 27	4.13	2.18	1.95	- .98	.97
Feb. 24	3.38	2.52	.86	--	.86
Mar. 3	4.13	2.51	1.62	--	1.62
" 10	3.44	2.42	1.02	--	1.02
" 17	3.00	2.30	.70	--	.70
" 24	3.50	2.32	1.18	--	1.18

	German 3 mos. Treasury bill rate	U.S. bill rate	Spread over U.S.	Forward exchange discount (-), premium (+) as per cent per annum[2]	Net incentive on covered basis
1960					
Dec. 30	3.75	2.20	1.55	-1.58	-.03
1961					
Jan. 27	3.25	2.18	1.07	- .98	.09
Feb. 24	3.00	2.52	.48	--	.48
Mar. 3	2.88	2.51	.37	--	.37
" 10	2.75	2.42	.33	--	.33
" 17	2.63	2.30	.33	--	.33
" 24	2.50	2.32	.18	--	.18

Foreign exchange. The 5 per cent appreciation of the DM on March 6 (followed almost immediately by a similar appreciation of the Dutch builder) upset exchange markets generally during most of March throughout Europe. An outflow of funds from Germany following the appreciation, in anticipation of exchange rate changes elsewhere (Switzerland, Italy, France), were more than offset by a subsequent reflow into Germany speculating that the revaluation might be carried further. The American

2/ Between the end of August 1960 and February 13, 1961, the premium on the forward dollar resulted from the swap arrangement of the Federal Bank under which German commercial banks could sell DM's spot for dollars and repurchase the DM's forward, a premium being given on the dollars sold forward. Established at one per cent per annum, the premium was raised to 1-1/2 per cent in October. Prior to establishment of the premium the Federal Bank granted dollar swaps at par and since February 13 has granted dollar swaps for the exchange cover of short-term capital exports, but only at par.

dollar dropped after holding near par on March 7 and 8, and was quoted throughout most of the rest of the month at the lower intervention point, rising higher only rarely and then only slightly. The dollar remained near or at the lower intervention point during the first week of April.

DM-Dollar middle rate		par (DM 4.20 = $1 to 3-5-61) (DM 4.00 = $1 from 3-6-61)
Feb. 1	4.1743	
" 28	4.1700	
Mar. 3	4.1705	
" 6	3.9900	
" 7	3.9830	
" 8	3.9700	
" 15	3.9700	
" 23	3.9700	
" 30	3.9700	
Apr. 5	3.9701	

On February 13, the Federal Bank abolished the dollar swap premium which it had established late last August, as an incentive for commercial banks to lend dollars abroad or to lend at slightly lower rates to German importers of dollar goods, thereby discouraging importers from borrowing abroad. Under the arrangement, German commercial banks could buy dollars spot (sell DM's) and sell dollars forward (buy DM's) at a premium of one per cent per annum for the dollar. The premium was raised to 1-1/2 per cent in October. It has been reported that, to promote capital outflow, the Federal Bank now prefers to make German long-term rates attractive to foreign borrowers rather than to promote short-term capital exports by the commercial banks, through the swap premium, since such outflows could be repatriated by the banks at times which the Federal Bank found inconvenient. Moreover, the Federal Bank felt that by leading to the movement of funds out of the domestic market the swap premium at times had resulted in an artificially high German money market rate. In addition, the monetary authorities expect the revaluation of the DM to reduce the inflow of funds and thus to dampen the rise in liquidity.

The Federal Bank still grants dollar swaps for the exchange cover of short-term capital exports, but only at par, i.e. without giving a premium, but also without charging a fee.

Bond market. The bond market strengthened during March as the Federal Bank intensified its efforts to lower German interest rates. The March activity continued the modest rally in the bond market which began with the inception of the Bank's lower interest rate policy last November. In the preceding ten months the market had been stagnant, no major issues, either public or private, having been placed.

The January 20 reduction in the discount rate, accompanied by a lowering of reserve requirements, had done little more than help to maintain the modest improvement evident in the last weeks of 1960. The January actions stimulated the bond market ot only a slight extent as a substantial portion of the funds made available was absorbed by a DM 1.5 billion development aid loan contributed by German industry. However, with the expectation of a continuing downward trend in long-term interest rates, the bond market improved further in February. These expectations were greatly strengthened during March as a result of further steps taken by the Bank to bring rates down. The several reductions in the Treasury bill and bond rates were taken by the bond market as a signal that the lowering of long-term rates is not going to be halted.

Demand for mortgage bonds and bonds of the public authorities increased markedly during the month. Six per cent mortgage bonds were selling at the end of March at 101, up 1-1/4 per cent from the end of February, while 5-1/2 per cent mortgage bonds were up approximately 1 point to 97-1/2.

Prices of both public and industrial issues rose generally by 1 to 1-1/2 points during March. (February end-of-month prices for public and industrial bonds had been approximately 1 point above the level at the beginning of February.) Issues with various tax exemption privileges remained in strong demand, the 4 per cent Federal Redemption Loan of 1957 rising to 103-1/8, up 7/8 during March.

The latest Government issue, the Federal Railways DM 250 million 12-year 6% loan issued in February at 99, rose to 101-1/4 by the end of March and has since advanced to 101-5/8 (April 7). This loan was absorbed by the market as soon as sales opened and was placed, so far as is known, entirely in Germany. The President of the Federal Bank had pointed out at the time of issue that, for reasons of monetary and foreign exchange policy, it would be undesirable for any part of the loan to be placed abroad. However, foreign interest in the bond market was reported strong as of the end of March. The demand of industry for capital market funds remains very strong.

The strengthening of bond prices produced a decline in long-term interest rates during the month. The yield on industrial bonds (based on a composite yield of the German Federal Bank) had fallen in January to 5.8 per cent, the first time since late 1959 that yields were below 6 per cent. Yields on industrial bonds fell further in February to 5.7 per cent and an additional point or two in March.

Yields of Fixed-Interest-bearing securities (per cent)

	Mortgage bonds	Industrial bonds	Loans of public authorities
1959 Feb.	5.8	5.7	5.6
Dec.	5.9	6.2	6.2
1960 Jan.	6.0	6.5	6.5
April	6.2	6.0	6.4
July	6.5	6.5	6.7
Oct.	6.4	6.1	6.3
Dec.	6.2	6.1	6.2
1961 Jan.	6.2	5.8	6.1
Feb.	6.2	5.7	6.0

During the month the Federal Government announced its intention of going later in the year into the market for something in excess of DM 300 million. No details as to types and amounts of any planned issues were given.

Stock market. Share prices tended constantly upward during the last week of March, but did not quite regain the levels of March 6 just before the break in prices following revaluation (See Chart 5). International developments, notably the better climate for a Laos settlement, may have influenced the month-end improvement, but most reports indicated that investors, having adjusted to the revaluation, still found German equities a good buy in the still booming economy. More important factors giving the market a lift were the trend toward lower interest rates, rising dividends, principally the rise from 16 to 18 per cent in the dividend declared by Farbenfabrikan Bayer A. G. (one of the major successor firms to the former I. G. Farben complex), and the almost certain increase of the same magnitude in the dividends to be declared by the other two major chemical concerns--Hoechst and Badische Aniline und Soda Fabrike.

The Bayer dividend was of major significance since it dispelled the fears of investors that German manufacturers, especially those who export heavily, would use the revaluation as an excuse for not increasing their 1960 dividends although earnings in that year had not been affected by the revaluation. Earlier, when two of the three major banks--Commerzbank and Dresdner Bank--held their 1960 dividends at the 1959 levels, the fears had increased.

Following the post-revaluation fluctuations in the market one fact seems clear--in general, non-German investors have held their shares. After the market break following revaluation, the later return of foreign funds into the market was ascribed to speculation on a possible further upward revaluation of the mark. Market analysts now believe that a major part of the foreign funds invested are in the market to stay until it becomes less attractive as compared to other opportunities for investment.

The strength of the current market is general to most types of shares. Automotive stocks (especially Daimler-Benz), chemicals and electrical manufacturing stocks (particularly Siemens), were strong at the end of the month, almost regaining their pre-revaluation levels of early March. Stocks of the three major banks--Dresdner Bank, Deutsche Bank and Commerzbank--also closed stronger at approximately their highest levels of the month, despite no increase in the dividends of two of the banks, as noted.

Well before March 15, the closing date for subscriptions, the Government's offering of Volkswagen shares was oversubscribed by more than 85 per cent. A total of 1.5 million individuals entered subscriptions for the available 3.6 million shares which were priced at DM 350 each (par value DM 100) minus certain special rebates based on family and income status. The shares were expected to be quoted at around DM 500-600 when trading opens. Trading was originally scheduled to open shortly after April 7 but may be delayed if the Constitutional Court prevents issue of the shares as scheduled. Several cases are now before the Court arguing that the preferential treatment of Volkswagen employees and low-income groups is unconstitutional. Considerable "under-counter" dealings have reportedly taken place, however, since the middle of March with "gray" quotations rising from around 600 to a peak of around

800 on March 28, declining thereafter to around 650 as fears increased that the Court would delay the issuance of the shares.

The March activity in the German stock market continued the movement which has persisted since the middle of 1960. The upsurge began in the first half of 1960 with the industrial share index reaching its peak of 330 (1958 = 100) in late August, declining to a lower level of 288 in late November. The index of industrial shares has remained at roughly this level in succeeding months, as shown in the monthly averages below. At the end of 1960, however, strong support from the banks had been required to maintain this level.

Index of industrial share prices
(1958 = 100)

1960	
January	217
February	220
March	216
April	223
May	241
June	277
July	300
August	330
September	327
October	313
November	297
December	288
1961	
January	286

European Section.

II. Five Charts on Financial Markets Abroad

Chart 1 - Interest Arbitrage US/Canada
Chart 2 - Interest Arbitrage New York/London
Chart 3 - Interest Arbitrage Frankfurt/New York
Chart 4 - Short-term Interest Rates
Chart 5 - Industrial Stock Indices

Chart 1

CANADA - UNITED STATES

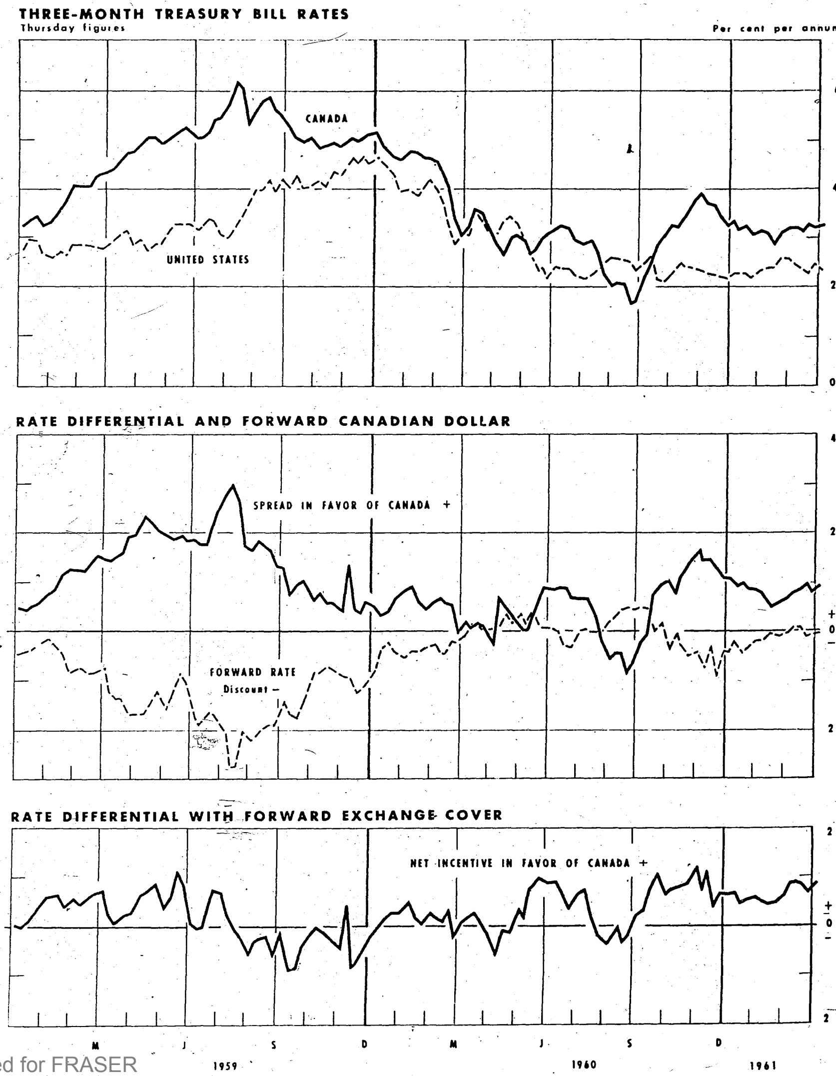


Chart 2

INTEREST ARBITRAGE, NEW YORK / LONDON

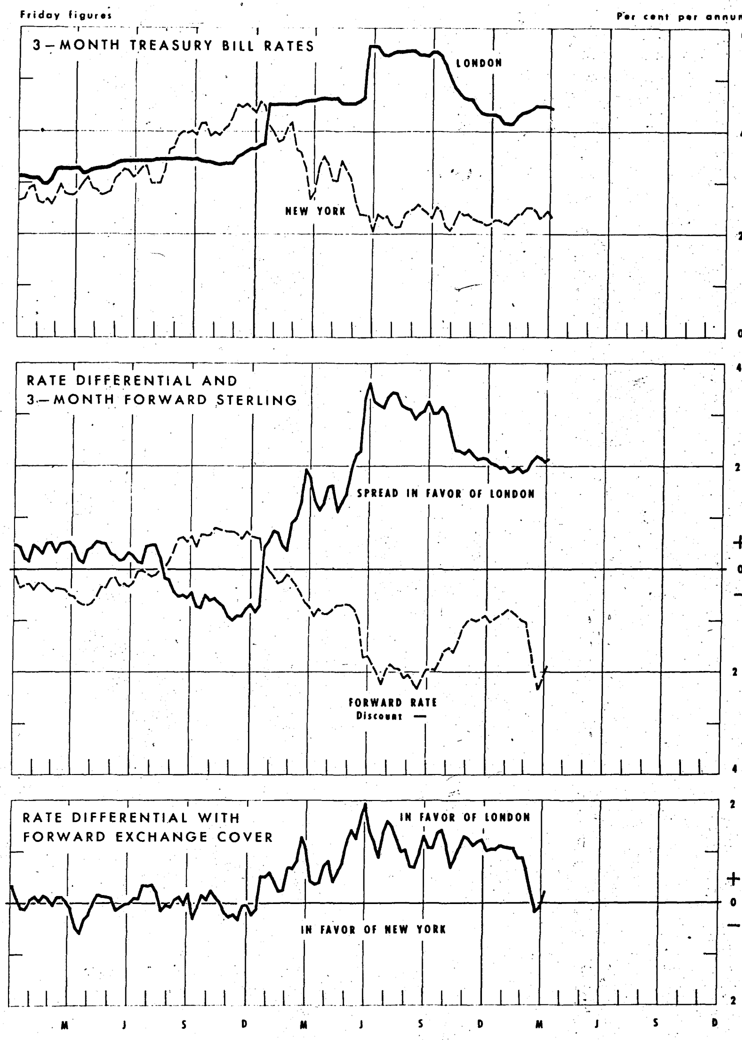
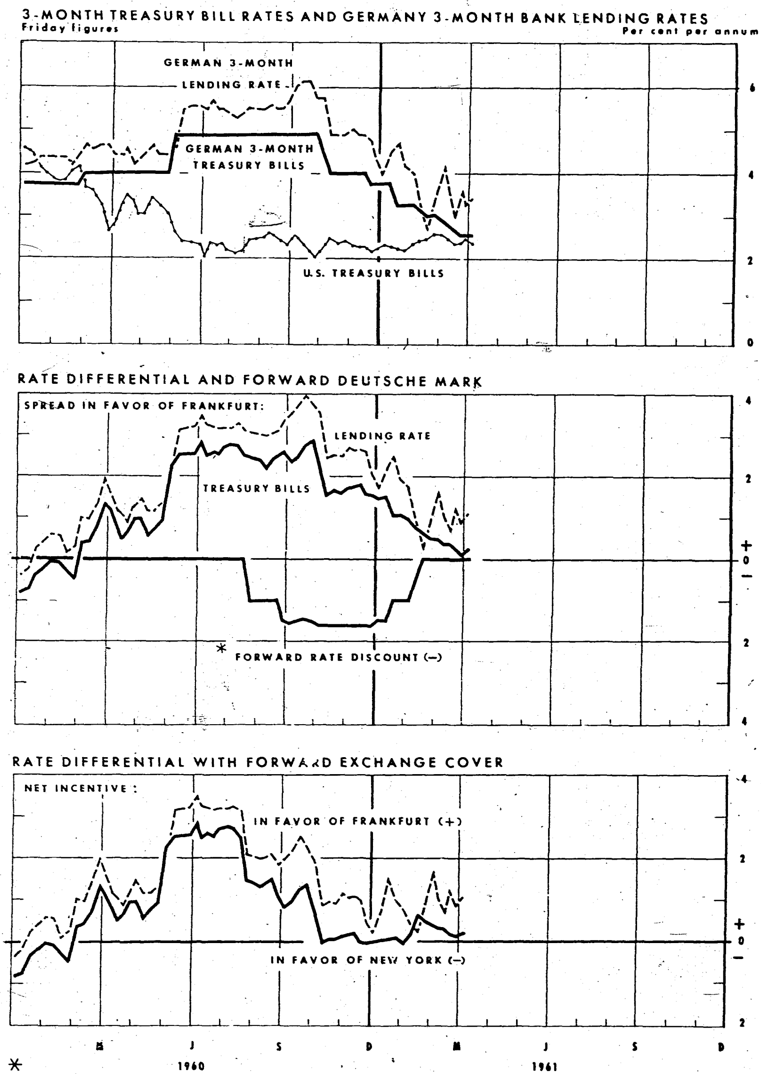


Chart 3

INTEREST ARBITRAGE, NEW YORK/FRANKFURT



* Note: Special forward dollar rate (either flat or premium on spot) available to German commercial banks.

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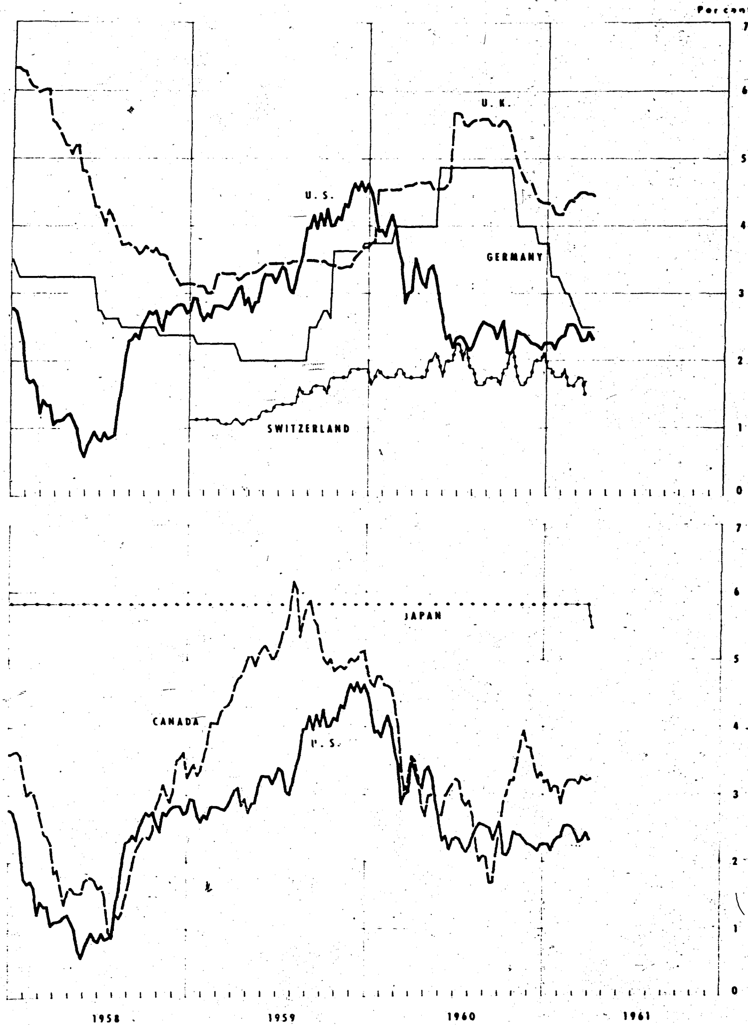
Chart 4

SHORT-TERM INTEREST RATES *



* Note: 3 month treasury bill rates for all countries except Japan (over 3 month interbank deposit rates) and Switzerland (3 month deposit rate).

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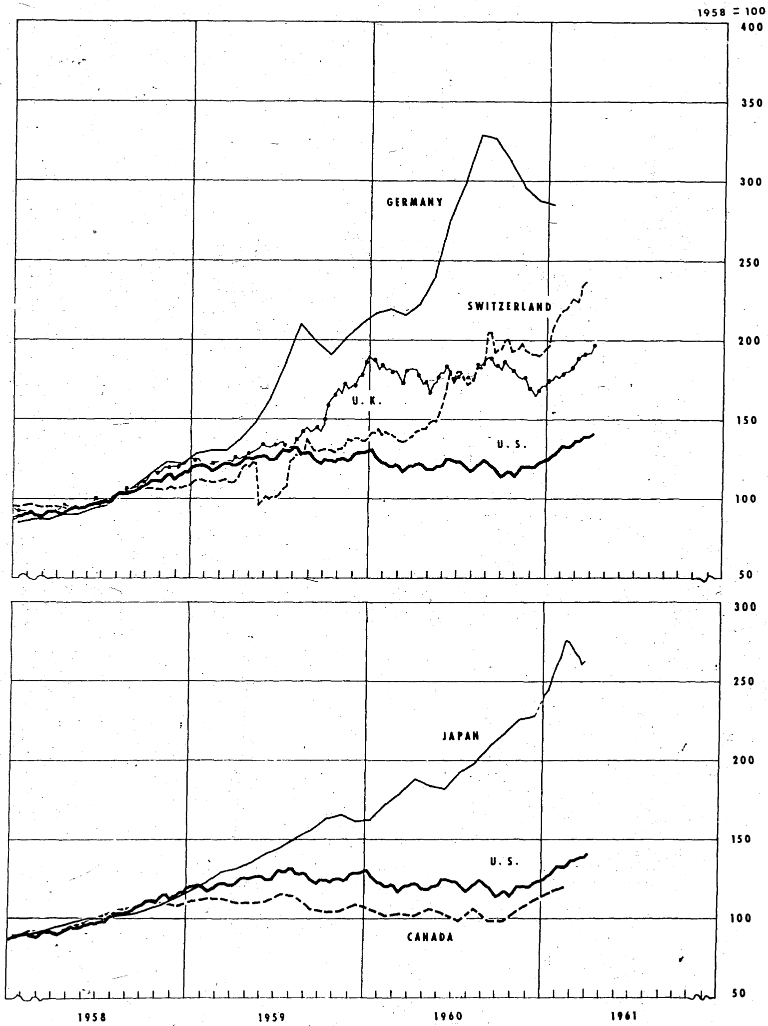
Chart 5

INDUSTRIAL STOCK INDICES *



*

Note: Japan: Index of all stocks traded on Tokyo exchange.