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CAPITAL MARKET DEVELOPMENTS ABROAD

I. United Kingdom
II. Netherlands
III. Nine Charts on Financial Markets Abroad

I. United Kingdom: Money and Capital Markets During April

The British budget for 1961-62, presented on April 17, was probably the dominant influence on money and capital markets in London during April. The budget, which provided for substantially reduced borrowing by the Treasury during the current fiscal year, was favorably received by the gilt-edged market. There was a general rise in prices after the Chancellor stated that the Treasury would not have to raise new money in the gilt-edged market this year. However, bond prices eased toward the end of the month and, by early May, long-term bond yields were close to pre-budget levels. Stock prices also rose rapidly to new record levels after the budget. Between April 14 and 28, the industrial price index rose from 349 to 363.

Short-term rates also declined after mid-April. The financial press has begun to discuss the prospects that Britain might follow Germany in reducing Bank rate. Between April 21 and May 5, the Treasury bill yield eased by 12 basis points. Despite the wide spread of the British Treasury bill over the New York bill, the widened discount on forward sterling kept the net incentive around one-half per cent during April.

Capital outflows continued in April after the heavy losses suffered in March. The official figures show a decline of $73 million in Britain's gold and dollar reserves in April but the amount of further temporary assistance received by Britain during the month is undisclosed. Indicative of pressures on the pound were the easing in the spot exchange rate and a widening of the discount on forward sterling during April. The trade returns for March show only a minor further improvement in the trade balance as a result of a further fall in the value of imports. Seasonally adjusted exports in March were below the January-February level and were about the same as in March a year ago.

Domestic credit continued to expand during the month. Bank loans increased by £70 million. Further bank sales of Treasury securities brought their security holdings to just over 15 per cent of deposits compared with 20 per cent a year ago. The liquidity ratio of the London clearing banks rose to 32 per cent in mid-April compared with 30.4 per cent in mid-March.

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Money market. The yield on the 3-month Treasury bill rose from 4.44 per cent on April 7 to 4.49 per cent on April 21 and then declined to 4.37 per cent on May 5 (see Table and Chart 2). During the past two weeks, the Bank of England has forced several of the discount houses to borrow at the penal rate as an indication of its resistance to a continued fall in the rate. Efforts of the discount houses to build up their portfolios against increased competition from outside bidders for a reduced total Treasury bill offering have contributed to the decline in bill rates. The London bill rate remained more than 2 per cent above the bill yield in New York. However, the incentive to move covered funds to London from New York declined from 0.59 per cent to 0.37 per cent because the discount on forward sterling widened in the latter part of April (see Table and Chart 2).

Bond market. After an initial decline in the latter part of April in response to the budget speech, bond yields rose somewhat in early May (see Table). War Loan 3-1/2 per cent reached a record high of 6.20 per cent on April 14 and stood at 6.19 per cent in early May.

The outlook for the gilt-edged market remains uncertain with many commentators believing it will remain at about its present level. The borrowing requirements of the Government in the coming year are substantially below those of recent years. The authorities will not have to raise any new money in the market this year because they expect to be able to cover the small over-all deficit through small savings and other nonmarket sources of Treasury cash. Because of this, the Chancellor expects to have more maneuverability in debt-management operations. With the final maturity of the large 2-1/2 per cent Funding Loan, 1956-61, on April 15, the next British Treasury bond maturity will be the £758 million, 4-1/2 per cent, Conversion Stock, 1962, which has a final redemption date of February 15, 1962.

The City of Glasgow offered a £10 million, 6 per cent issue, 1973-75, at a price of £99 on May 4 with a gross redemption yield of 6.10 per cent. The underwriters were left with 77 per cent of the issue. The City of Stirling offered a £5 million, 6 per cent issue, 1974-75 at a price of £99 on April 12.

The budget. The British budget for 1961-62, introduced in Parliament on April 17, provides for substantially reduced borrowing by the Treasury during the coming year. The current surplus is estimated to be £506 million, over three times as large as as that for the previous year, as the following summary estimates show (in millions of pounds):

	1961-62 (estimated)	1960-61 (actual)
Current reserve	6,408	5,934
Current expenditure	6,002	5,787
Current surplus	506	147
Net loans to nationalized industries, public works and overseas development	575	541
Over-all deficit	69	394

This increased current surplus combined with a capital account deficit similar in size to that of the previous year will reduce the Government's borrowing requirements to £69 million, less than one-fifth of last year's level. The authorities expect to be able to raise these new funds outside of the Government securities market through proceeds from the National Savings Movement, the usual growth in the fiduciary issue, sales of Tax Reserve Certificates and sterling accruals from any further decline in the gold and foreign exchange reserves.

There were several changes in the tax structure. In a major reduction in personal income taxes, the surtax was abolished on incomes between £2,000 and £5,000. As an offset, the corporation tax was raised from 12-1/2 to 15 per cent. Increased indirect taxes on heavy oils, TV advertising, pool betting and motor vehicle license duties are expected to bring in an additional £80 million this year.

Two new economic regulators were introduced in the budget as innovations in fiscal policy. One gives the Government the power to raise or lower the main revenue duties by 10 per cent without Parliamentary approval. This provision will give the authorities leverage to raise or lower purchasing power by as much as £200 million. Secondly, the Government is to have the authority to introduce a payroll charge on employers to discourage labor hoarding and to encourage labor saving investment. This tax, a weekly tax per employee, can be varied by the Treasury to a maximum of 4 shillings per head. Through this greater flexibility in tax rates, the authorities hope to rely more on fiscal, and less on monetary instruments as tools of economic stabilization.

London clearing banks. Net loans by the 11 London clearing banks rose £69.7 million to £3,423.4 million in the five weeks to mid-April. There was a rise of £67.2 million in loans to borrowers other than the nationalized industries. Investments fell by £72.6 million and, at £1,114 million, aggregate investments now have a ratio to deposits of 15.2 per cent compared with 20.0 per cent a year ago. Gross deposits are rising sharply. The banks have improved their average liquidity ratios from 30.4 per cent in mid-March to 32 per cent in mid-April. Attrition of 2-1/2 per cent Funding bond which had a final maturity date on April 15 contributed to the improved liquidity position.

Installment credit. Despite the January 20 relaxation in installment credit terms, total hire-purchase credit declined further in February. Recent figures in installment credit outstanding are (in millions of pounds):

	Household shops	Finance houses	Total	Change
1959: July	273	469	742	--
1960: July (peak)	332	639	971	+229
Sept.	324	628	952	- 19
Dec.	325	610	935	- 17
1961: Jan.	321	607	928	- 7
Feb.	315	607	922	- 6

The relaxation in credit terms is reflected in the fact that credit extended by finance houses did not decline in February. Their new credit extensions (mainly for automobiles) in February were only 10 per cent lower than a year ago when there were no controls.

Trade balance and export financing. The seasonally adjusted trade deficit showed a further slight reduction in March as a result of reduced imports. March exports were below January-February levels as the following monthly trade returns indicate (in millions of pounds):

	Exports[a/]	Imports	Trade deficit
1960: October	263	385	122
November	341	411	70
December	314	387	73
1961: January	331	401	70
February	318	383	65
March	313	375	62

a/ Includes re-exports.

To bolster the current export drive, the Export Credit Guarantee Department announced three measures on April 12: (a) the charges for medium credits were reduced by an average of 25 per cent; (b) guarantees will now be available for selected exports beyond the present 5-year period; and (c) simplified procedures are to be available for the small exporter of consumer goods with an annual turnover of less than £10,000 a year.

Foreign exchange reserves. The United Kingdom's gold and dollar reserves dropped $72.8 million in April to a total of $2,948 million. Since the end of January, reserves have fallen by $297 million. These figures do not include the substantial special assistance received by Britain from other central banks under the mid-March agreement of central banks "to cooperate closely in the exchange markets." The figures were not affected by West Germany's advance payment of $189 million on its postwar debt to the U.K. since the Germans drew $63 million from a sterling account originally set up in 1957 and $126 million from sterling balances held in London by the German central bank.

Foreign exchange rates. Spot sterling eased from 279.87 U.S. cents on April 7 to 279.55 U.S. cents by the end of the month and was at 279.61 U.S. cents on May 5 (see Table).

The discount on 3-month forward sterling declined from 1.89 per cent on April 7 to 1.59 per cent on April 14 but again widened later in the month and was at 1.82 per cent on May 5 (see Table).

The rate on security sterling strengthened throughout April from 275.875 U.S. cents on April 7 to 279.125 U.S. cents on May 5. The premium on the "soft" dollar (the currency used by British residents to purchase United States or continental securities) was in mid-April at the high rate of 9.63 per cent. Formerly, especially at the end of 1957, the dollar premium was high because of fears by British investors that sterling would be devalued against the dollar. The British financial press has reported that this high premium on the dollar reflects the increased interest of British investors in continental securities at the present time.

Stock market. The prices of industrial shares continued their rapid advance which began in early December. After the budget, stock prices rose sharply (see Table and Chart 7). The Financial Times Industrial Ordinary share index rose from 341 at the end of March to 363 at the end of April.

British Commonwealth Section.

Part II. Netherlands: Reopening of Capital Market for Foreign Issues

On April 18, the Netherlands Bank announced that it was prepared to issue a limited number of special licenses for the flotation of public foreign loans on the Dutch capital market. Under the approved arrangement, foreign governments can now seek the Bank's approval on individual flotations up to an equivalent of $14 million dollars (Fl. 50 million). Reportedly a lower limit of Fl. 10 million ($2.8 million) has also been established. It is expected that in the beginning licenses for a total of around Fl. 250-300 million will be granted, with a more liberal granting of licenses dependent upon the reaction of the market to the early flotations. Yields on these loans will be credited to accounts in convertible florin.

A general license permitting all types of foreign borrowers access to the Dutch market does not seem to be an early possibility.

The reopening of the market came as no surprise since Dutch financial officials had for some time called the reopening a necessity in view of the strong position of the florin. The market was closed to foreign borrowers in 1955 when the Dutch communes experienced great difficulty in raising both short-term and long-term funds and were unable to compete in the capital market as a result of Government action limiting the rate of interest they could offer.

The opening of the market may be expected to restrain liquidity by leading to an export of funds or by offsetting any renewed inflow of short-term funds from abroad. It is also expected to restrain any further decline in long-term interest rates.

The move, although limited both in scope and as to type of borrower, still represents an important further step in the expansion of European capital markets. The first loan is expected to be made shortly, possibly to either Belgium or Norway.

European Section.

III. Nine Charts on Financial Markets Abroad

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Chart 4 - Interest Arbitrage Frankfurt/London
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Chart 7 - Industrial Stock Indices
Chart 8 - Major Currencies in Terms of Spot United States Dollar
Chart 9 - 3-month Forward Rate -- London Quotations

United Kingdom: Treasury Bill Yields and Exchange Rates

Date	3-mo. Treasury bill U.K.[a]	3-mo. Treasury bill U.S.[b]	3-mo. Treasury bill Difference	Discount on 3-mo. sterling[c]	Net incentive to hold U.K. bill[d]	Exchange rate Spot sterling[e]	Exchange rate Discount on 3-mo. sterling[f]
1959 - High	3.6	4.7	-1.1	--	--	--	--
Low	3.0	2.6	0.4	--	--	--	--
1960 - High	5.68	4.59	3.63	(P).64	1.95	281.58	1.64
Low	2.13	2.05	-0.84	2.33	- .23	279.83	(P).47
Mar. 10	4.49	2.42	2.07	1.46	0.61	279.80	1.02
17	4.49	2.30	2.19	1.96	0.23	279.86	1.37
24	4.49	2.32	2.17	2.32	-0.15	279.77	1.62
30	4.48	2.42	2.06	2.13	-0.07	279.70	1.49
Apr. 7	4.44	2.30	2.14	1.89	0.25	279.87	1.32
14	4.48	2.30	2.18	1.59	0.59	279.80	1.11
21	4.49	2.23	2.26	1.72	0.54	279.65	1.20
28	4.41	2.27	2.14	1.83	0.31	279.55	1.28
May 5	4.37	2.18	2.19	1.82	0.37	279.61	1.27

a/ Average yield at Friday weekly tender.
b/ Closing market yield for Friday in New York.
c/ Spread between spot and forward rate in per cent per annum.
d/ Net of difference in bill yield less discount on 3-month sterling.
e/ Spot rate in New York market in U.S. cents.
f/ Spread between spot and forward rates in U.S. cents.

United Kingdom: Selected Capital Market Yields

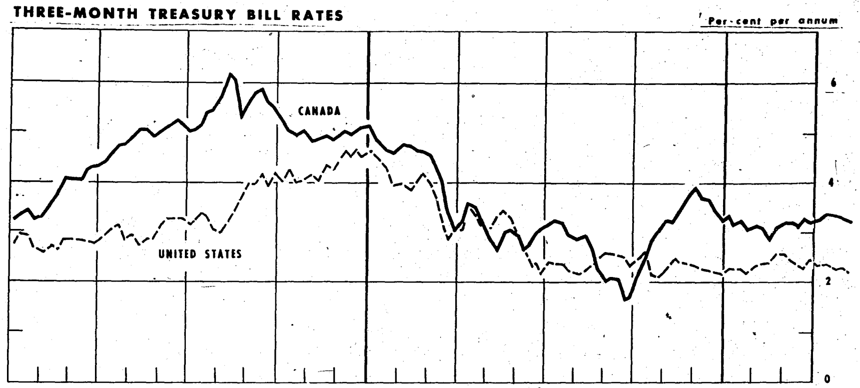
	6-year bond[a]	15-year bond[b]	War loan[c]	Consols[d]	Share yield[e]	Yield gap[f]	Share prices[g]
1960 - High	6.11	6.00	5.94	5.70	4.96	1.49	338.6
Low	4.93	5.33	5.53	5.02	3.74	0.63	294.6
Mar. 10	6.02	6.08	6.15	5.84	4.46	1.38	338.0
17	6.06	6.08	6.15	5.87	4.44	1.43	337.0
24	6.09	6.10	6.18	5.91	4.44	1.57	339.4
30	6.07	6.11	6.18	5.95	4.45	1.50	341.3
Apr. 7	6.05	6.11	6.19	5.97	4.33	1.64	351.4
14	6.03	6.11	6.20	5.98	4.39	1.59	348.8
21	5.96	6.11	6.15	5.92	4.32	1.60	356.7
28	5.97	6.12	6.15	5.90	4.24	1.66	362.8
May 5	5.99	6.13	6.19	5.94	4.30	1.64	359.1

a/ 5-1/2 per cent Exchequer, 1966.
b/ 3 per cent Savings Bond 1965-75.
c/ 3-1/2 per cent War Loan (undated).
d/ 2-1/2 per cent Consol (undated)
e/ *Financial Times*.
f/ Difference between yield on 2-1/2 per cent Consols and share yield.
g/ *Financial Times*.

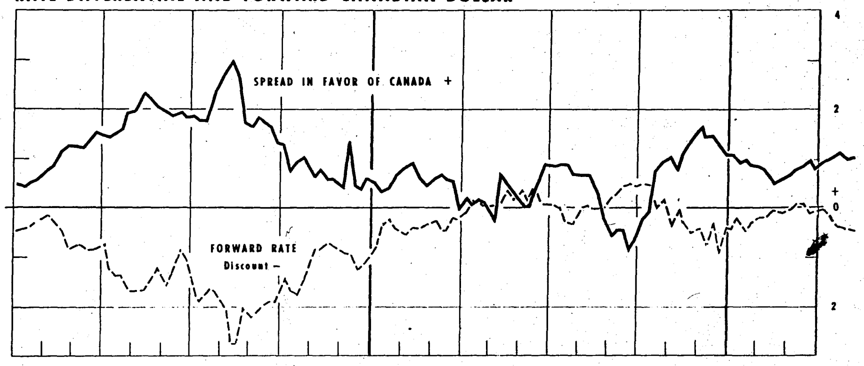
Chart 1

INTEREST ARBITRAGE, UNITED STATES / CANADA
Thursday figures

THREE-MONTH TREASURY BILL RATES



RATE DIFFERENTIAL AND FORWARD CANADIAN DOLLAR



RATE DIFFERENTIAL WITH FORWARD EXCHANGE COVER

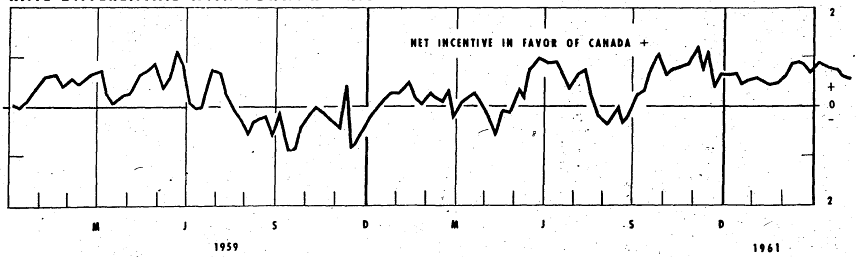


Chart 2

INTEREST ARBITRAGE, NEW YORK / LONDON

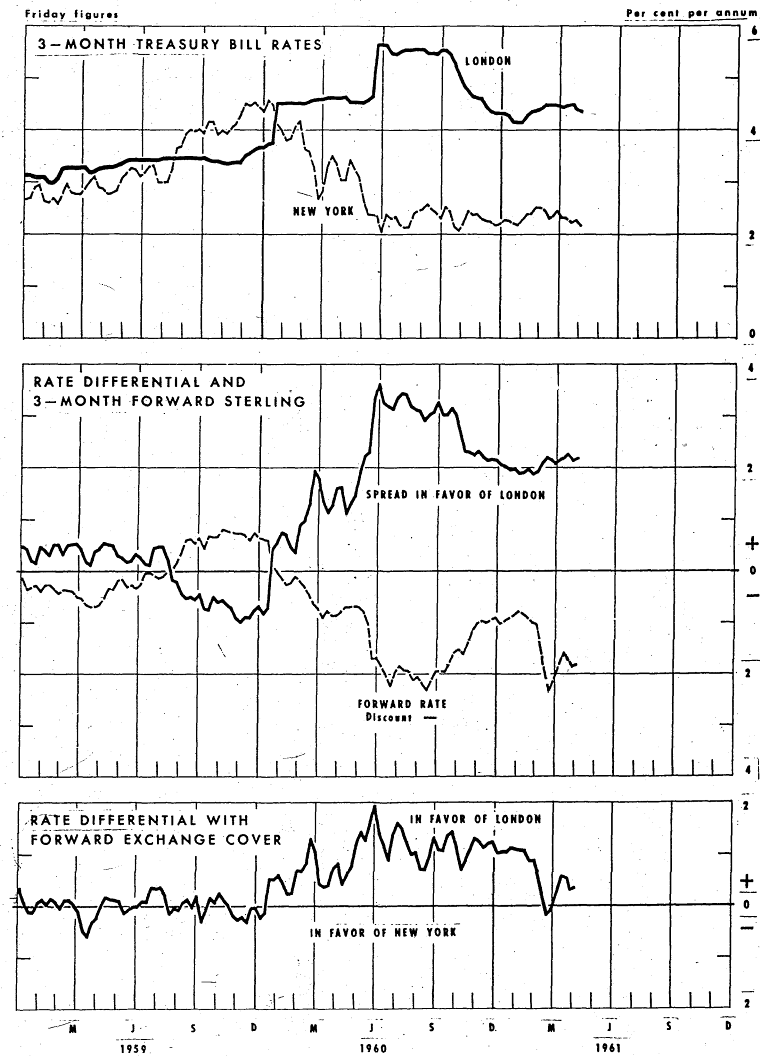
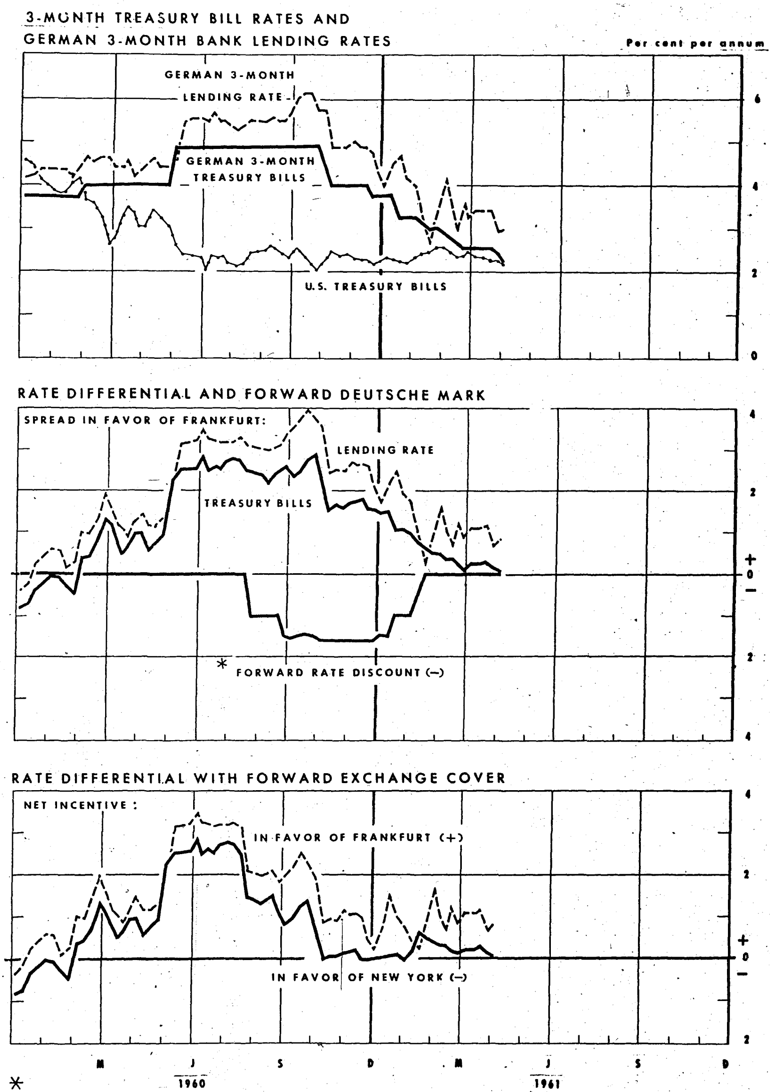


Chart 3

INTEREST ARBITRAGE, NEW YORK/FRANKFURT

Friday figures



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

Chart 4

INTEREST ARBITRAGE, FRANKFURT/LONDON

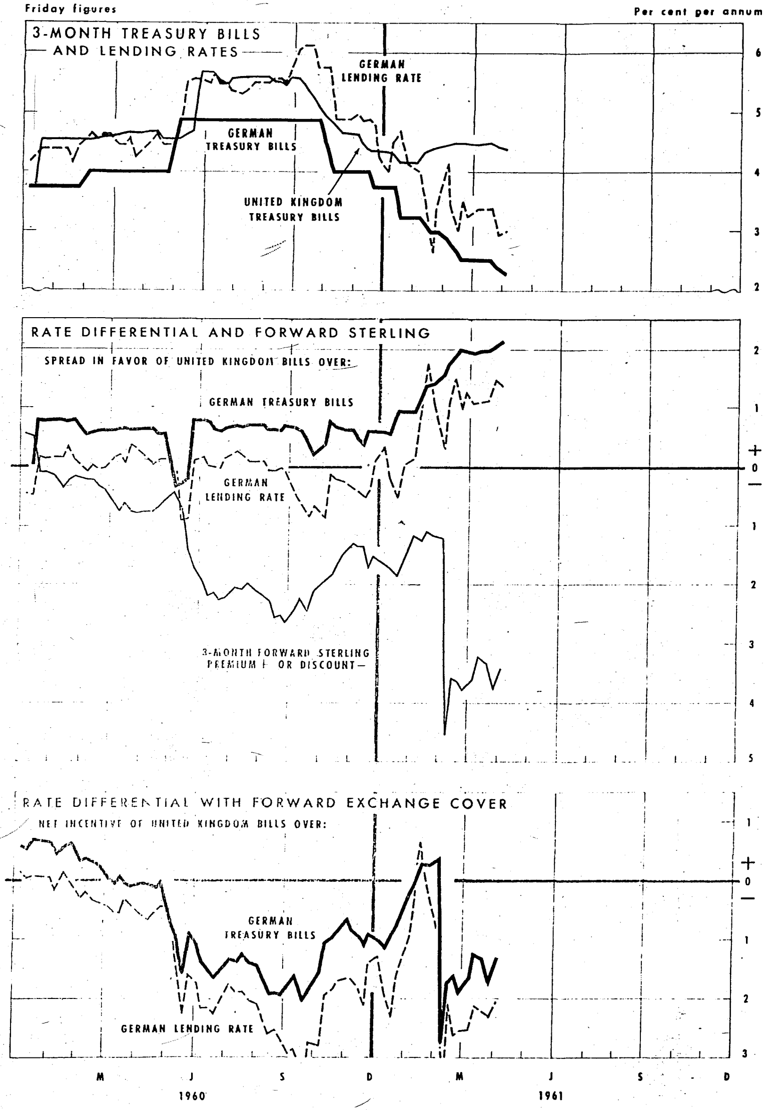
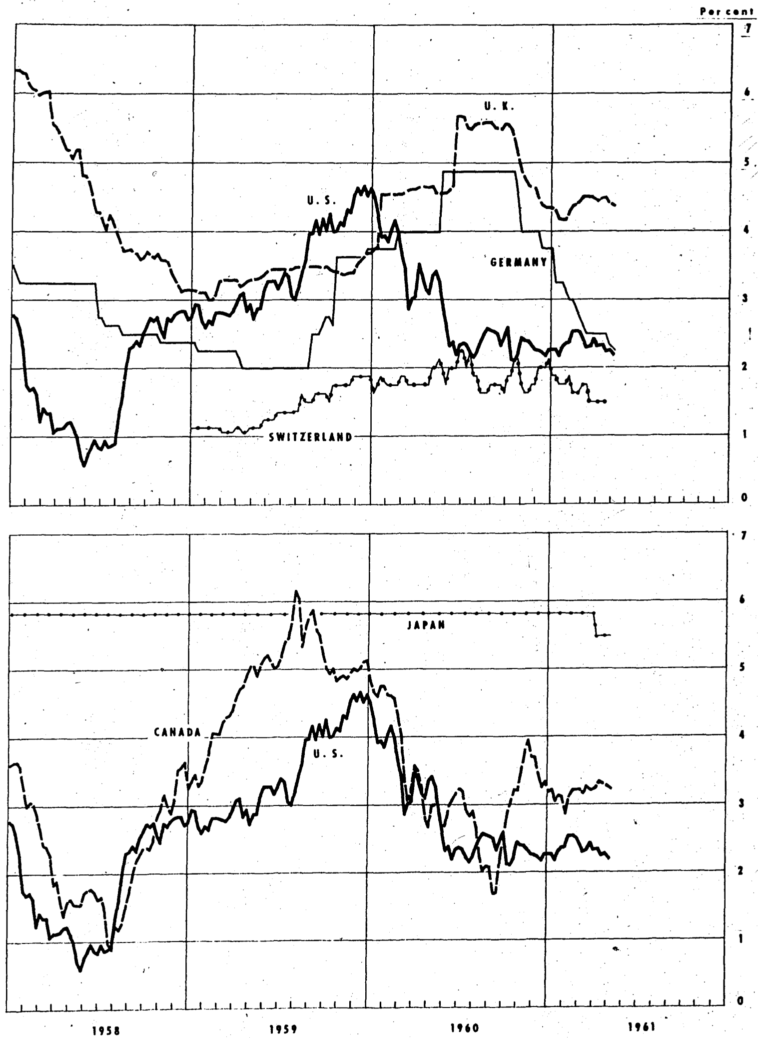


Chart 5

SHORT-TERM INTEREST RATES *



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

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Chart 6

LONG-TERM BOND YIELDS

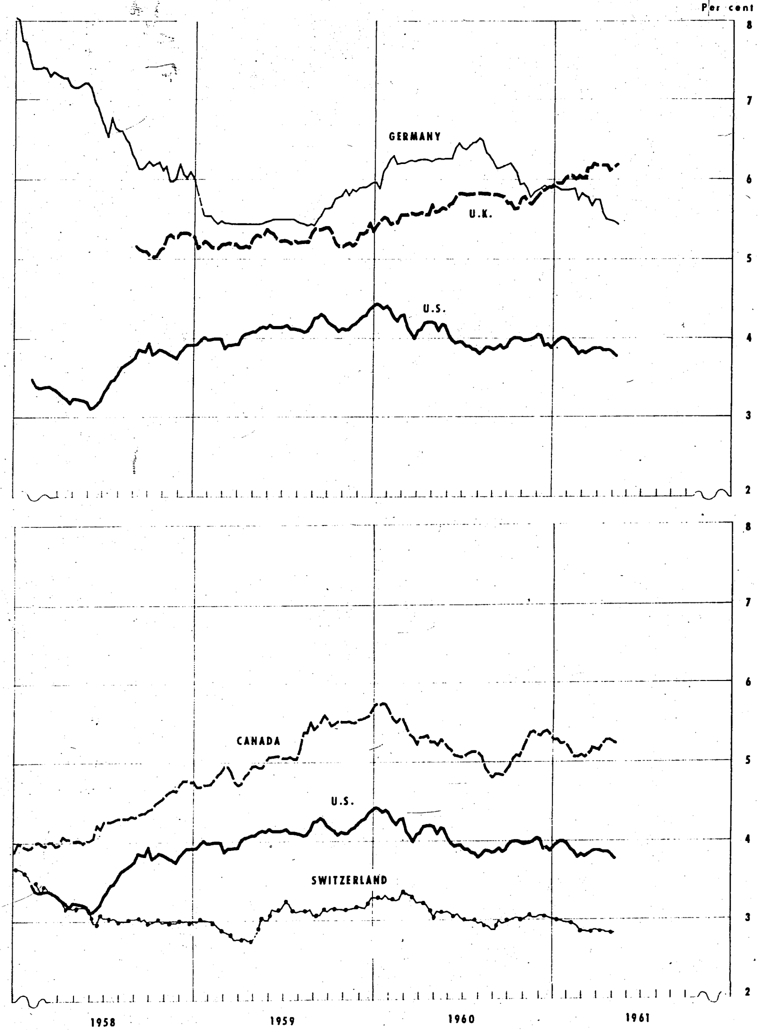
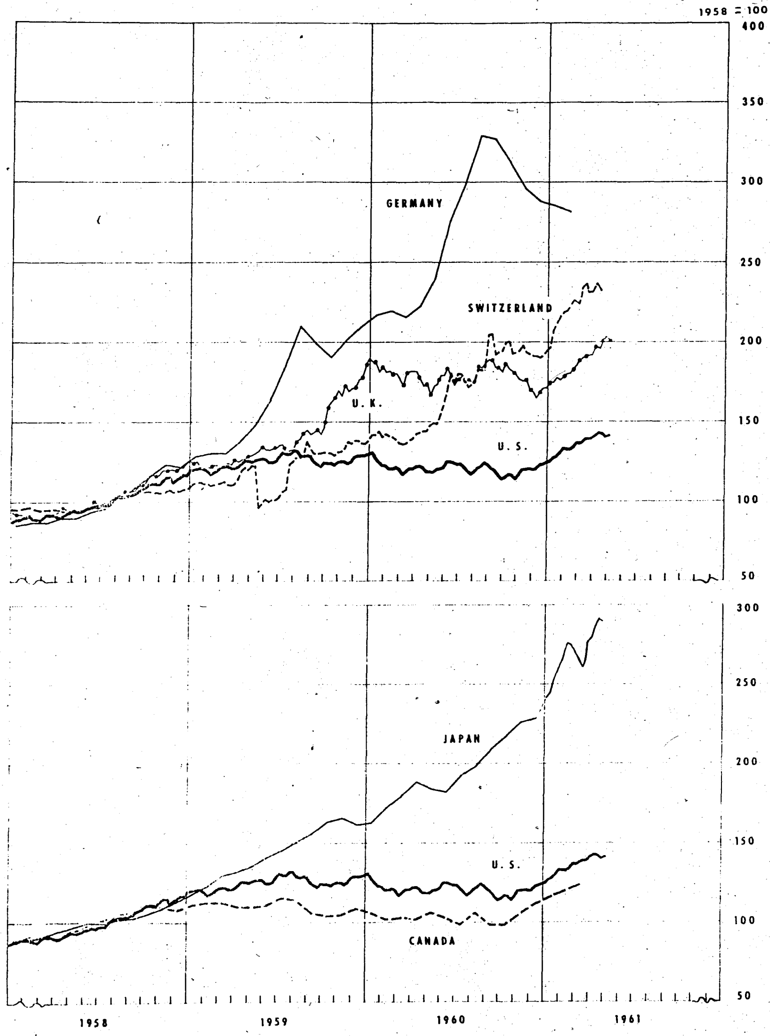


Chart 7

INDUSTRIAL STOCK INDICES *



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

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Chart 8

MAJOR CURRENCIES IN TERMS OF THE SPOT U. S. DOLLAR

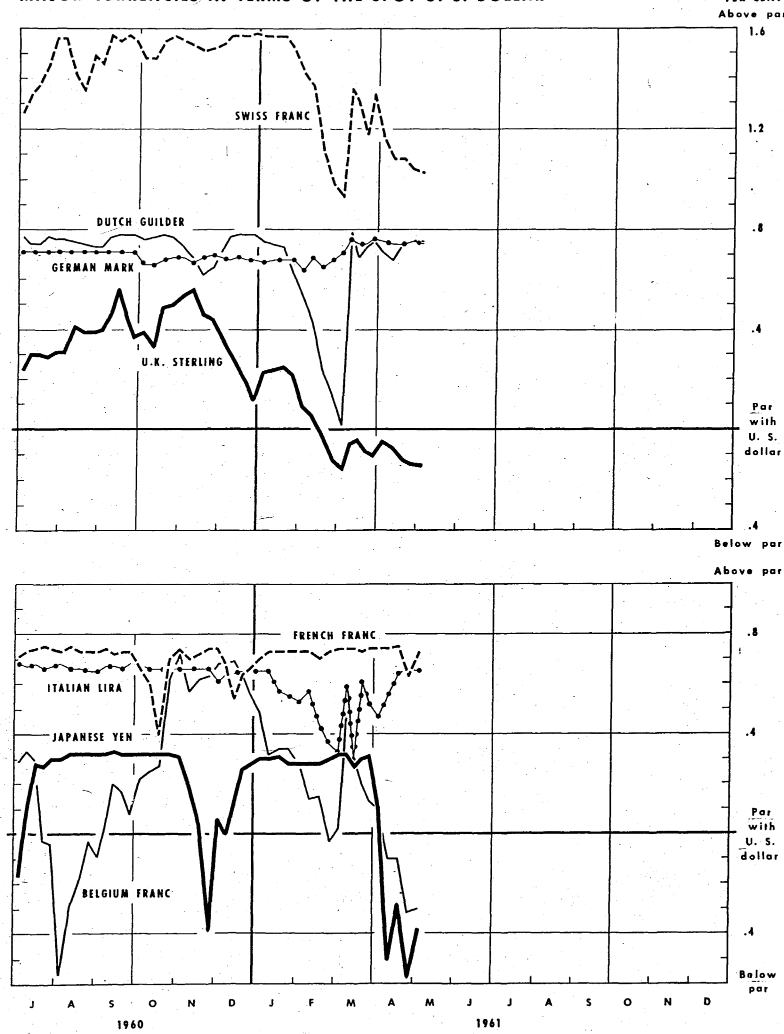

Chart 9

3-MONTH FORWARD RATES - LONDON QUOTATIONS