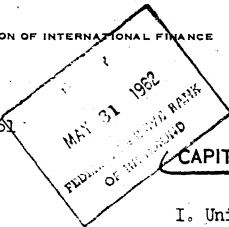


H. 13
No. 61

May 25, 1962

CAPITAL MARKET DEVELOPMENTS ABROAD

- I. United Kingdom
- II. Nine Charts on Financial Markets Abroad

I. United Kingdom: Money and Capital Markets in April

British interest rates continued to move to lower levels during April, especially in the shorter-term sectors. The Treasury bill rate was substantially reduced and the Bank of England followed two Bank rate reductions in March by a further cut from 5 per cent to 4-1/2 per cent on April 26. This decision to lower Bank rate was motivated primarily to stem the inflow of foreign funds but the slow pace of business recovery was an additional consideration.

Despite the sluggish domestic recovery, the British authorities reaffirmed both their willingness to allow money rates to decline and their determination to keep a firm hand on credit availabilities under present circumstances. This consideration led them to reduce Bank rate rather than to make releases of reserves to the clearing banks out of their Special Deposits.

The budget for 1962-63 presented on April 9 also reflected the official desire to keep credit supplies under control. The Chancellor reported that the Treasury had been able to obtain its net borrowing requirements by sales of nonmarketable securities during the past two years and expected to do so again in 1962-63. As a result, the cash obtained from market sales of Treasury securities by the Government Broker had been used to reduce the volume of outstanding Treasury bills. He stated that in 1960-61 the Treasury had virtually met its cash needs outside financial markets and had used the nearly £300 million from sales of gilt-edged securities largely to retire Treasury bills. In 1961-62, nonmarket cash receipts, especially from National Savings, enabled the Treasury to retire around £250 million of Treasury bills. Sales of bonds to the market had "been just about enough to meet our liabilities on the two maturities which occurred during the year" (Hansard, April 9, 1962, col. 961).

The Treasury's improved cash position helps to explain why bank deposits have increased only modestly during the past two years. In 1960-61, a £428 million reduction in bank loans to the public sector was offset by a £419 million expansion in loans to the private sector. In 1961-62, a smaller cut in public sector financing was counterbalanced by a smaller reduction in private loans, as the following aggregate changes (in millions of pounds, April to March fiscal year) indicate:

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DECONTROLLED AFTER SIX MONTHS

	<u>1960-61</u>	<u>1961-62</u>
Net deposits	+ 71	+185
Liquid assets (per cent)	= 30 (30.4)	+229 (32.9)
Loans to public sector:		
Treasury bills	-151	+ 4
Call loans	- 28	+56
Government securities	-294	- 90
Nationalized industries	<u>- 11</u>	<u>+ 3</u>
Total	-428	+ 73
Loans to private sector:		
Commercial bills	+ 60	+ 60
Advances	<u>+359</u>	<u>+ 18</u>
Total	+419	+ 78

The heavy sales of bonds by the banks must have been offset by substantial reductions of Treasury bills held by nonclearing bank investors in view of the Chancellor's statement that the bulk of the Treasury surplus had been used to retire bills. If this hypothesis is accurate, it would be consistent with the marked shift in foreign and domestic funds into the local authorities loan market reported during the past 8 months.

The pound continued strong in the foreign exchange market during April although the spot rate eased somewhat after the Bank rate change. There were further reserve accruals earlier in the month as foreign funds continued to flow in. The improved foreign trade position in March and again in April contributed to the pound's strength in the market.

Money market. The rapid decline in short money rates which took place in March was continued during April. The after-tender market rate for Treasury bills dropped from 4.34 per cent on March 30 to 3.97 per cent on May 4 (see Table and Chart 2). Because of the reduced discount on the forward pound, however, there remained an insignificant incentive to hold U.S. rather than U.K. Treasury bills. The rates offered on three-months' local-authority deposits declined steadily during April. In March the rates had remained firm as local treasurers were bidding for funds to meet seasonal payments of principal and interest to the Public Works Loan Board. In April, however, there was a steady supply of foreign funds flowing through merchant banks and the overseas banks; and the demand for funds was somewhat lower than normal, because the local authorities reportedly acquired substantial deposits in February on a three-month term. The authorities have also discovered that clearing bank overdrafts were then as cheap as 7-days' deposit money.

Despite the declining rate of return on the local authorities deposit and the reduced forward discount on sterling the yield on local-authority deposits became fractionally higher in late April than the return on Euro-dollar deposits in London, as the following differentials (in per cent per annum) indicate:

April 6	-0.02	April 27	+0.02
12	-0.08	May 4	+0.06
20	+0.10	11	+0.13

Gilt-edged market. The downward drift in gilt-edged yields continued in April, especially in the short- and long-dated sectors of the market. In early April, the market was characterized by uncertainty in anticipation of the budget and then after April 9 by fears that the proposed tax on speculative gains might materially reduce switching operations in bonds. In the second half of the month, buyers became more active in a 1964-67 bond which passed into the under-five-year category on May 1 to become a short-dated bond handled by the discount houses.

In early May, the Government Broker's supplies of a 5-1/2 per cent 1982-84 bond were exhausted and were replaced on the same day by an additional tranche of £300 million of a 5 per cent 1986-89 offering. These securities were offered at a price of 84 at a time when the market quotation was 84-1/2; thus, the authorities seemed intent on exerting their efforts to check and perhaps to turn the downward drift in bond yields.

Recent changes in assets (in millions of pounds)

	Net deposits	Liquid assets		Loans to public sector			Loans to private sector	
		Amount	Per cent	Govt. securities	Treas. bills	Total a/	Advances	Total b/
<u>1960</u>								
(March)	(6,073)	(2,217)	(31.5)	(1,368)	(941)	(2,937)	(2,933)	(3,086)
June	+103	+ 36	(31.4)	-123	+ 17	-122	+137	+129
Sept.	+101	+ 23	(31.6)	- 62	+ 24	- 4	+ 64	+ 51
Dec.	- 15	+123	(31.9)	- 24	+ 24	+ 47	+ 25	+ 48
<u>1961</u>								
March	-118	-212	(30.4)	- 85	-216	-349	+133	+191
June	+216	+207	(32.2)	-102	+177	+ 81	+144	+158
Sept.	- 44	+128	(34.3)	- 36	+112	+ 72	-180	-151
Dec.	+ 24	+144	(35.3)	+ 71	+ 2	+200	-115	-119
<u>1962</u>								
Mar.	- 11	-250	(32.6)	- 23	-287	-280	+169	+190
Apr.	- 85	+ 14	(32.6)	+ 14	+ 52	+ 21	- 5	- 6

a/ Includes loans to nationalized industries and call loans.

b/ Includes commercial and other bills.

Installment credit. Installment credit outstanding declined during February and March. During the first quarter of 1962, the fall in this debt was the largest quarterly decline since restrictions in hire-purchase credit were reimposed in July 1961. Most of the reduction during February and March was attributed to the sluggish automobile market. Potential buyers delayed their purchases until after the budget (April 9), on the possibility that the purchase tax on motor vehicles would be reduced. During March many retailers found that consumers were purchasing a larger proportion of durable goods with cash rather than on credit. However, a pick-up in auto sales in April has been reported in the press. Quarterly changes in credit outstanding (in millions of pounds) were:

	Total Dec. 1960	Changes				
		1961				
		Jan.- Mar.	Apr.- June	July- Sept.	Oct.- Dec.	Jan.- Mar.
Shops	325	-13	- 6	- 3	+ 6	-13
Finance houses	<u>610</u>	<u>+12</u>	<u>+29</u>	<u>- 1</u>	<u>-32</u>	<u>-26</u>
Total	935	- 1	+23	- 4	- 26	-39

The conflict among the hire-purchase finance firms over commissions to dealers, which has been going on for a couple of months, was terminated in early May in an agreement by all participants to hold to 15 per cent the commission paid to motor dealers. Formerly, a 10 per cent rate had been in effect but the largest firm in the industry introduced a 20 per cent figure in February.

Foreign trade. Britain's foreign trade balance, seasonally adjusted, showed a further modest improvement in April above the first-quarter average. However, the April figures for both exports and imports in April were about the same as for March. Recent seasonally-adjusted trade figures (monthly averages in millions of pounds) were:

	1960	1961				1962	
		I - II	III	IV	I	Mar.	Apr.
Imports, c.i.f.	-380	-374	-357	-362	-367	-358	-359
Exports, f.o.b.	296	307	309	304	306	312	314
Re-exports	<u>12</u>	<u>12</u>	<u>13</u>	<u>15</u>	<u>12</u>	<u>11</u>	<u>14</u>
Trade balance	- 72	- 55	- 35	- 43	- 49	- 35	- 31

Foreign exchange reserves. The gold and foreign exchange reserves continued to rise in March and April. The reported figures should be adjusted for the special prepayments to the IMF by Britain of £75 million in February and £25 million in April and by Australia of £62 million in March. (The Australian repurchase was made with dollars held by the U.K.) The explanation for the increase in reserves can be attributed in part to the improved trade balance but chiefly to the continued inflow of capital to the U.K. Recent monthly changes in reserves (in millions of pounds) are as follows:

Reported figure Adjusted for special transactions	1961		1962			
	Nov. +9	Dec. -85	Jan. +33	Feb. +5	Mar. +10	Apr. +7
	+59	-18	+33	+80	+72	+32

Foreign exchange market. The improvement in the trade balance and the inflows of capital helped to maintain a strong position for sterling during April (see Chart 9). After declining in late March, the spot rate moved up after the budget speech but declined late in April after the cut in Bank Rate. Selected daily rates for spot sterling from February through April (in U.S. cents per pound) were:

Feb. 2	281.27	Mar. 2	281.60	Apr. 6	281.38
9	281.45	9	281.61	13	281.52
16	281.55	16	281.71	20	281.45
23	281.54	23	281.32	27	281.25
		30	281.39		

The discount on the forward pound declined in late April and early May (see Table).

Bullion market. The London gold market was fairly quiet during the months of March and April. The prices at the London fixing during the month were (in U.S. dollars per ounce):

Mar. 2	35.086	Apr. 6	35.074	May 1	35.073
9	35.078	13	35.081	8	35.082
16	35.095	19	35.075	15	35.079
23	35.087	27	35.074		
30	35.083				

An article in a Swiss newspaper, the *Journal de Genève*, purports to report on a discussion about gold policies among central bankers at Basle on April 10. According to this report, each central bank would commit limited amounts of gold into a central pool which could be used for counterspeculative sales on the gold markets. When the price of gold falls, the syndicate would replenish its supplies. Pending the working out of details by the central banks, the *London Times* reported that "it was agreed to give the Bank of England full authority to buy gold -- on their collective responsibility -- so as to keep the market in order should the occasion arise." (May 2, 1962, p. 17).

Stock market. The price of industrial stocks remained fairly steady, taking the period of March and April as a whole. (See table and Chart 7.) After remaining at 298.8 during the first half of March the index of share prices declined during the third and fourth weeks of March, to 292.6 at the end of the month. Prices recovered during the first week of April. The index remained around 300 during the first half of April, and the market was quiet due to uncertainty about the budget and the possible effects of the capital gains tax. During the latter part of April, the share price index rose to around 305, a level attained during the early February.

II. Nine Charts on Financial Markets Abroad

- Chart 1 - Interest Arbitrage, United States/Canada
- Chart 2 - Interest Arbitrage, New York/London
- Chart 3 - Interest Arbitrage for German Commercial Banks
- Chart 4 - Interest Arbitrage, Frankfurt/London
- Chart 5 - Short-term Interest Rates
- Chart 6 - Long-term Bond Yields
- Chart 7 - Industrial Stock Indices
- Chart 8 - Spot Exchange Rates -- Major Currencies
Against U.S. Dollar
- Chart 9 - 3-month Forward Exchange Rates

Europe and British Commonwealth Section.

United Kingdom: Treasury Bill Yields and Exchange Rates

	<u>3-mo. Treasury bill arbitrage calculation</u>					<u>Spot pound (U.S. cents)</u>	<u>London deposit rates</u>	
	<u>U.K. a/</u>	<u>U.S. b/</u>	<u>Differ- ence</u>	<u>3-mo. pound^{b/}</u>	<u>In favor U.K. bill^{c/}</u>		<u>U.S. dollar (3-mo.)</u>	<u>Local authority (3 mo.)</u>
1961 - High	6.74	2.74	4.45	-0.79	1.13	281.62	4.00	7.50
Low	4.17	2.16	1.88	-4.36	-2.12	278.47	3.13	6.00
Mar. 2	5.44	2.69	2.75	-2.60	+0.15	281.60	3.56	6.47
9	5.03	2.76	2.27	-2.43	-0.16	281.61	3.69	6.22
16	4.81	2.72	2.09	-2.45	-0.36	281.71	3.69	6.13
23	4.38	2.70	1.68	-2.08	-0.40	281.32	3.63	5.69
30	4.34	2.75	1.59	-1.93	-0.34	281.39	3.69	5.69
Apr. 6	4.28	2.70	1.58	-1.86	-0.28	281.38	3.63	5.50
13	4.25	2.74	1.51	-1.92	-0.41	281.52	3.50	5.34
20	4.19	2.73	1.46	-1.71	-0.25	281.45	3.50	5.31
27	4.03	2.74	1.29	-1.48	-0.19	281.25	3.50	5.00
May 14	3.97	2.73	1.24	-1.32	-0.08	281.28	3.56	4.94
11	3.88	2.63	1.25	-1.07	+0.18	281.24	3.63	4.6
18	3.78	2.68	1.10	-1.04	+0.06	281.29	3.56	4.70

- a/ Market quotation for Friday.
- b/ Spread between spot and 3-month forward rate in per cent per annum. Discount equals (-).
- c/ Net of difference in bill yield less discount on 3-month sterling.

United Kingdom: Selected Capital Market Yields

	<u>U.K. Government bond yields</u>					<u>Share yield a/</u>	<u>Yield gap b/</u>	<u>Share prices c/</u>
	<u>4-1/2% 1964</u>	<u>3% 1965-75</u>	<u>5-1/2% 2008-12</u>	<u>3-1/2% War Loan</u>	<u>2-1/2% Consols</u>			
1961 - High	6.65	6.68	--	6.92	6.78	5.48	1.90	365.3
Low	5.15	5.95	--	5.95	5.70	4.22	0.86	287.7
Mar. 1	5.51	6.22	6.35	6.45	6.26	5.19	1.07	298.0
8	5.43	6.23	6.30	6.43	6.25	5.27	0.98	294.7
15	5.28	6.23	6.25	6.30	6.15	5.19	0.96	298.8
22	5.08	6.24	6.25	6.33	6.16	5.25	0.91	295.2
29	5.18	6.25	6.30	6.38	6.23	5.37	0.86	292.6
Apr. 5	5.27	6.25	6.30	6.38	6.22	5.21	1.01	301.5
12	5.25	6.24	6.30	6.43	6.26	5.22	1.04	300.9
19	5.07	6.22	6.20	6.31	6.15	5.25	0.90	298.6
26	4.95	6.22	6.20	6.27	6.13	5.15	0.98	305.1
May 3	5.02	6.23	6.20	6.25	6.13	5.17	0.96	305.5
10	4.95	6.25	6.20	6.30	6.20	5.31	0.91	297.5
17	4.84	6.22	6.20	6.30	6.15	5.28	0.87	296.5

- a/ Financial Times.
- b/ Difference between yield on 2-1/2 per cent Consols and share yield.

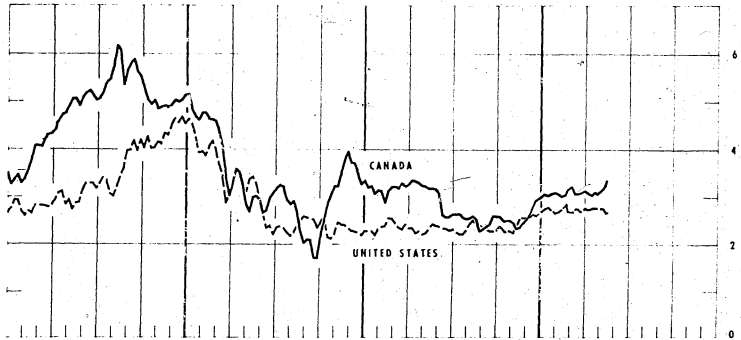
Chart 1

INTEREST ARBITRAGE, UNITED STATES / CANADA

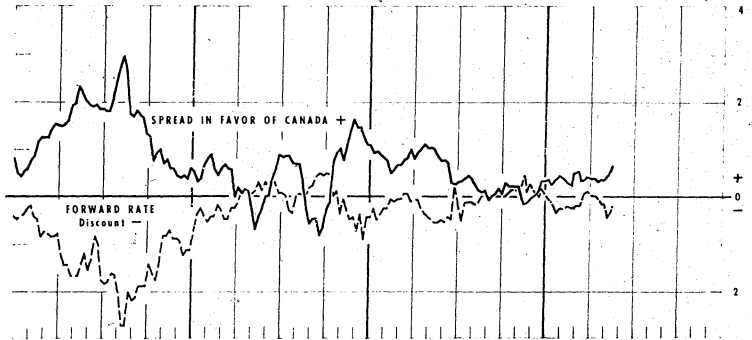
Thursday figures

THREE-MONTH TREASURY BILL RATES

Per cent per annum



RATE DIFFERENTIAL AND FORWARD CANADIAN DOLLAR



RATE DIFFERENTIAL WITH FORWARD EXCHANGE COVER

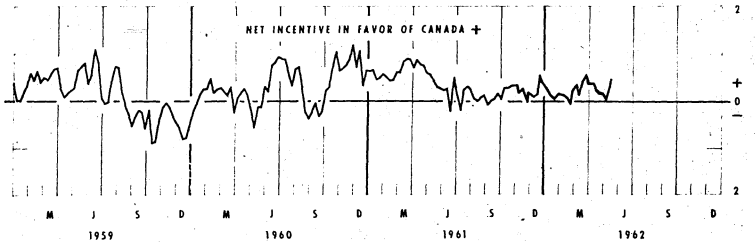


Chart 2

INTEREST ARBITRAGE, NEW YORK/LONDON

Friday figures

Per cent per annum

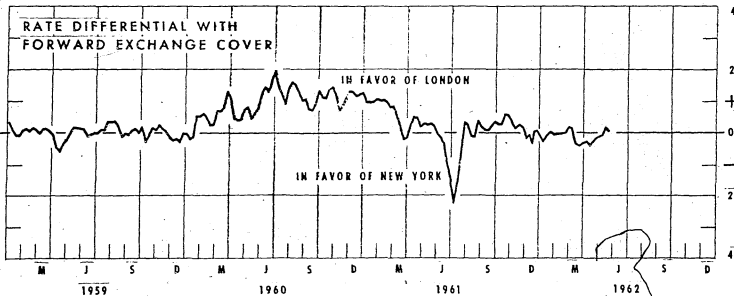
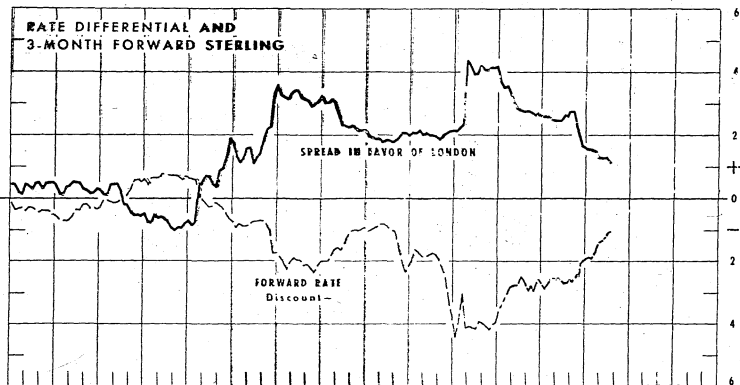
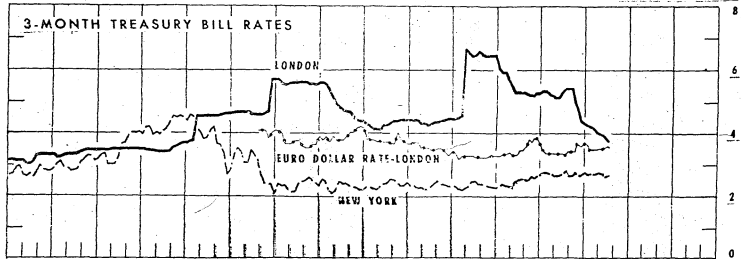
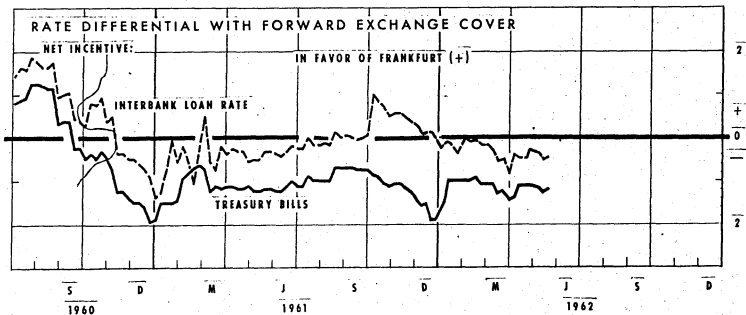
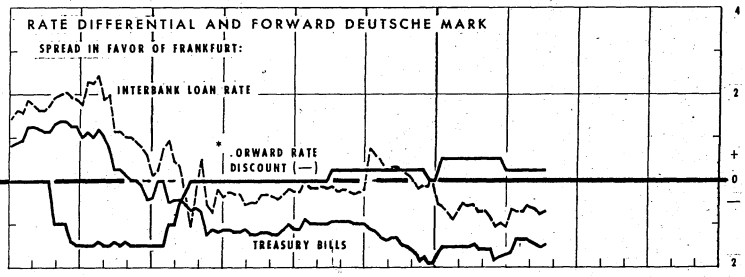
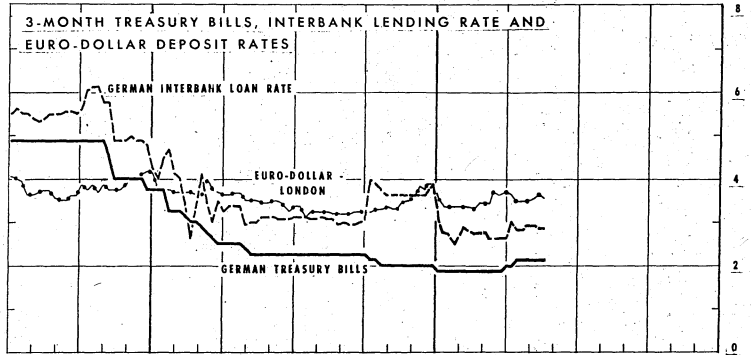


Chart 3

INTEREST ARBITRAGE FOR GERMAN COMMERCIAL BANKS

Friday figures

Per cent per annum



Note: Special forward rate available to German commercial banks

Chart 4

INTEREST ARBITRAGE, FRANKFURT/LONDON

Friday figures

Per cent per annum

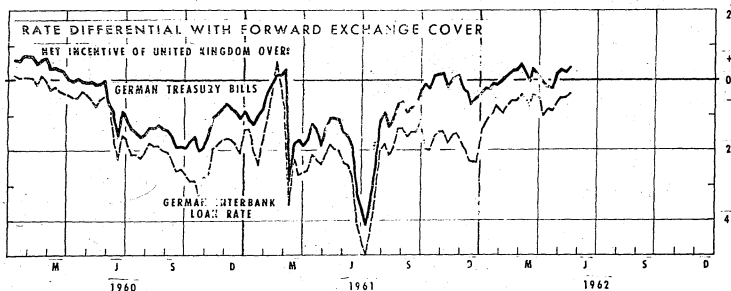
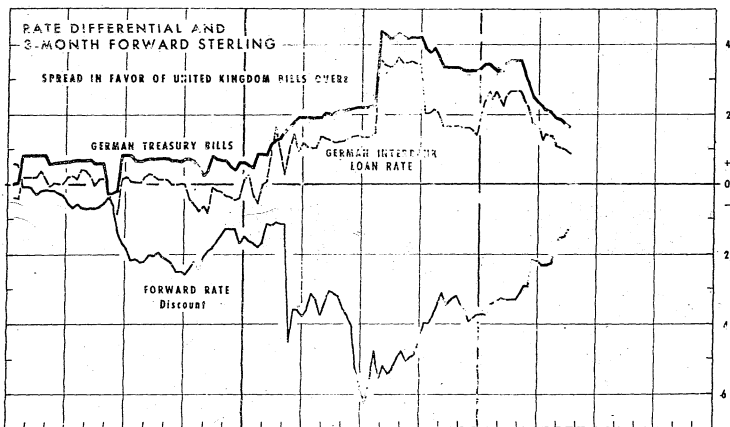
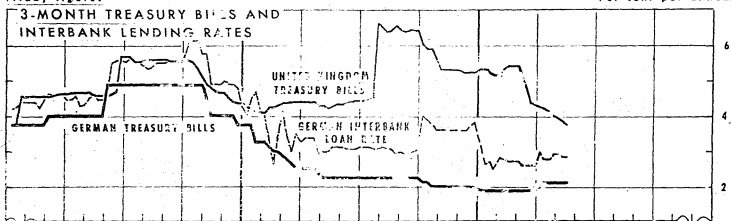
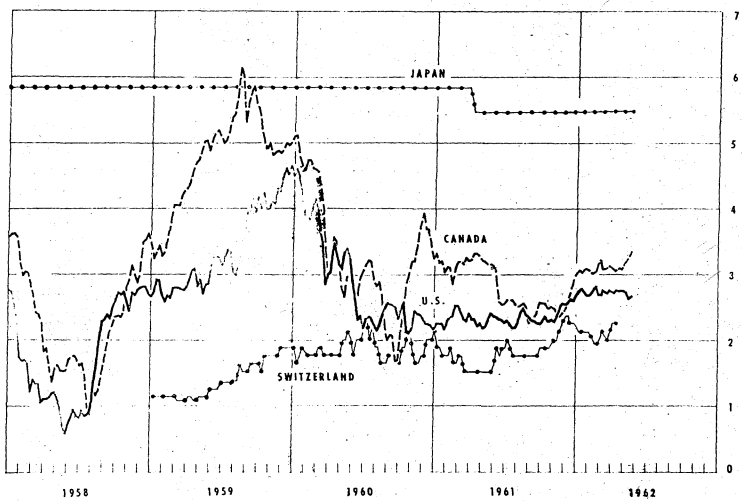
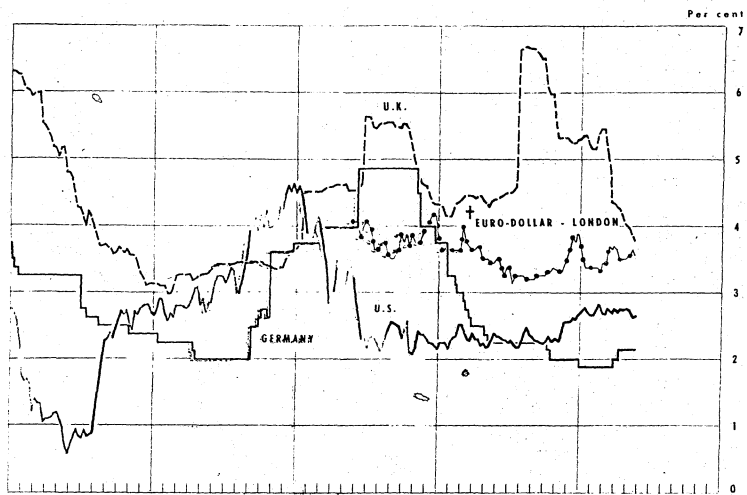


Chart 5
SHORT-TERM INTEREST RATES *



* 3 month treasury bill rates for all countries except Japan (3 month interbank deposit rate) and Switzerland (3 month deposit rate)
 † 3 month rate for U.S. dollar deposits in London.

Chart 6
LONG-TERM BOND YIELDS

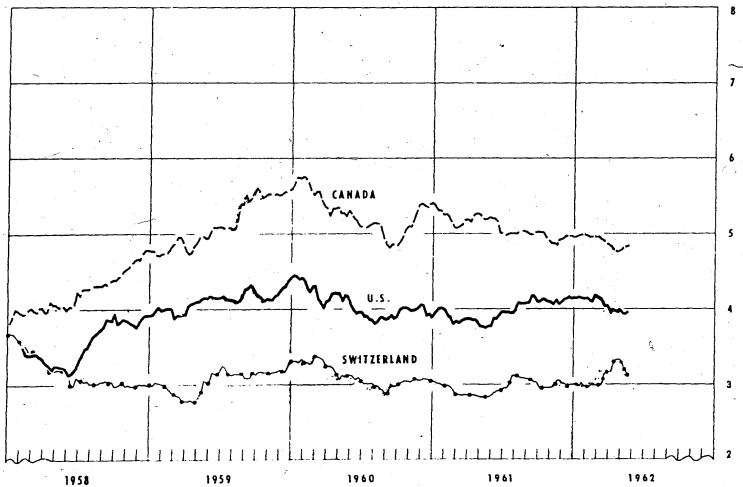
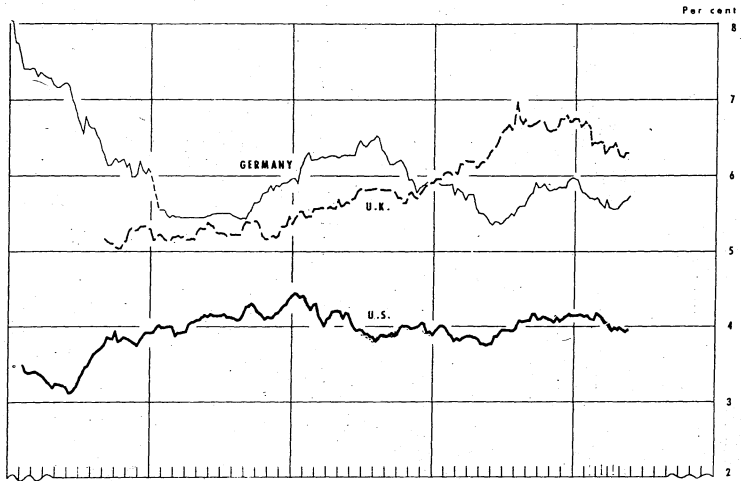
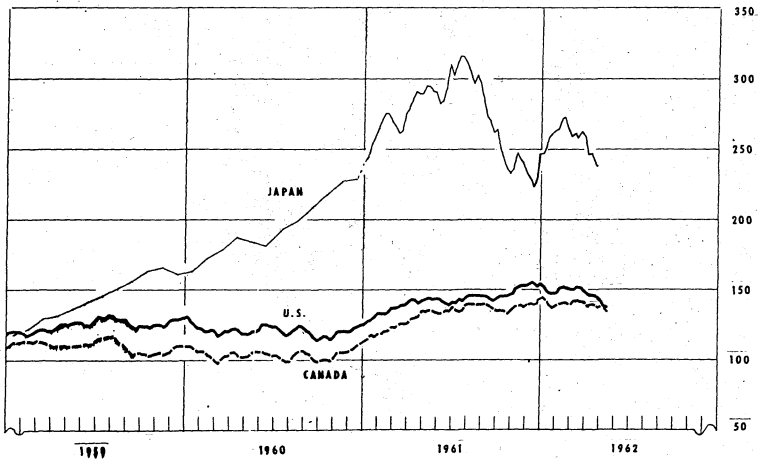
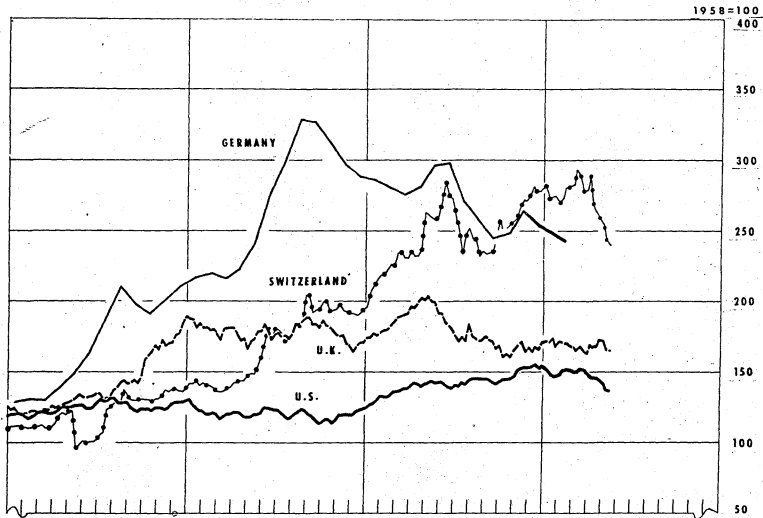


Chart 7

INDUSTRIAL STOCK INDICES*



*Note: Japan index of all stocks traded on Tokyo exchange

Chart 8

SPOT EXCHANGE RATES - MAJOR CURRENCIES AGAINST U.S. DOLLAR

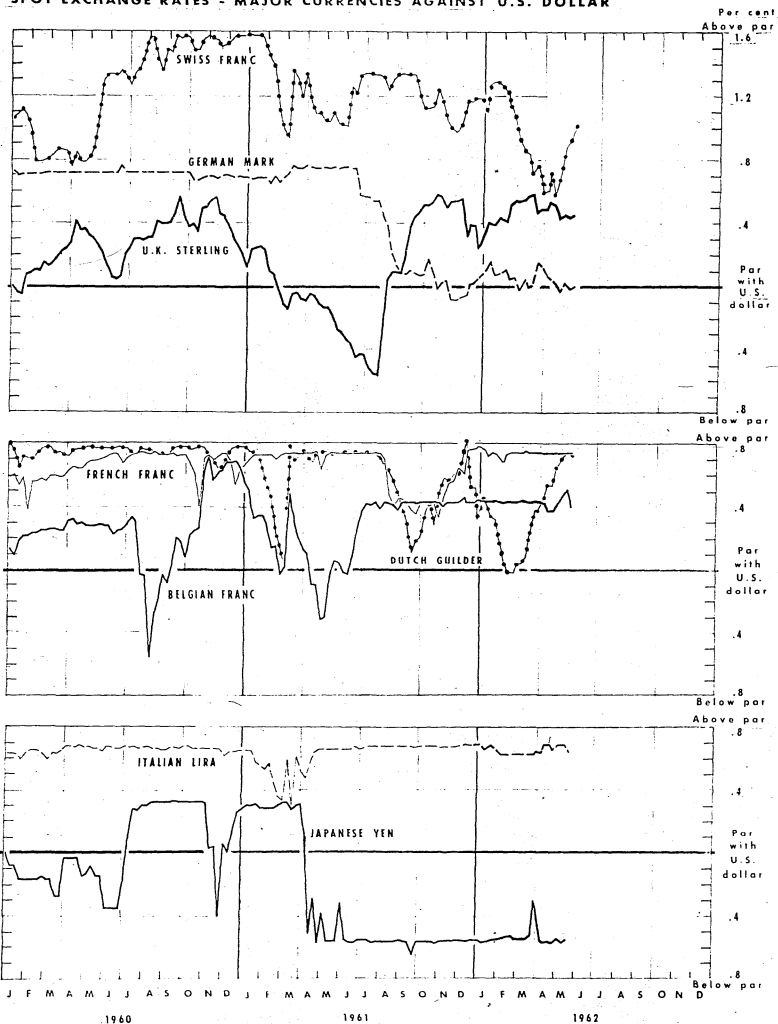


Chart 9

3-MONTH FORWARD EXCHANGE RATES

Per cent per annum

