DIVISION OF INTERNATIONAL FINANCE

BOARD OF GOVERNORS OF THE FEDERAL RESERVE SYSTEM

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CAPITAL MARKET DEVELOPMENTS ABROAD

I. Canada
II. Nine Charts on Financial Markets Abroad

I. Canada: Money and Capital Markets, March-April 1964

Fiscal developments provided the highlights of a continuing period of relative quietude in Canadian money and capital markets. Long-term yields fluctuated within narrow limits but Treasury bill rates eased in early April. The emergence of a slight premium on the forward Canadian dollar in late March materially widened the covered Treasury bill arbitrage in favor of Canada to over 30 basis points; some funds are reported to have moved into Canadian finance paper. (See Table 5.) On March 16, the Minister of Finance introduced a featureless budget, primarily notable for a one-third reduction in the projected deficit. (See Table 1.) From March 31-April 2, there was a renewal of the continuing dialogue between federal and provincial authorities concerning their respective sources of fiscal revenues and areas of financial responsibility.

Table 1. Canada: Budget Revenues, Expenditures, and Deficits 1960-65
(millions of dollars)

Fiscal year ended March 31.	Budgetary Revenues	Budget Expends.	Deficit	Overall Cash Reqrs. 1/	Deficit on nat. inc. accts. basis
1960	5289.8	5702.9	413.1	375.5	
1961	5617.7	5958.1	340.4	294.3	
1962	5729.6	6520.6	791.0	477.6	536
1963	5878.7	6570.3	691.6	1463.9	369
1964 (est'd)	6207.0	6892.0	685.0	518.9	221
1965 (projected)	6700.0	7155.0	455.0	895.0	40

1/ Including various non-budgetary receipts and disbursements.
Source: Budget Papers (1964-65) and Bank of Canada Statistical Summary.

No change in general tax policy.

The Canadian budget statement is noteworthy for its moderation, particularly in comparison with the budget presented a year ago. With anticipated expenditures already some 6 per cent in excess of revenues, and high levels of unemployment largely confined to the Atlantic Provinces and Eastern Quebec, the

Government decided against proposing any general reduction in income tax analogous to recent U.S. legislation. The punitive 20 per cent rate of withholding tax proposed for dividends paid non-residents by foreign-owned companies has been withdrawn, but the favorable 10 per cent rate for companies meeting designated criteria of Canadian ownership continues in effect. There is no further mention of a Canadian Development Corporation to encourage the repatriation of Canadian equities; instead, increasing reliance is to be placed on private investment trusts, pension funds, and life insurance companies.

Overall cash requirements in 1964-65 are estimated at $895 million, up considerably from the preliminary figure of $518.9 million for 1963-64 though much below the $1463.9 million level of the preceding year, when advances to the exchange fund account absorbed $943 million. On a national-income accounts basis, the deficit is expected to be a nominal $40 million, after falling steadily from $536 million recorded in fiscal 1962.

Over one-third of the expected budget expenditures is in the defence ($1.6 billion) and public debt charges ($1.0 billion) categories. Personal and corporate income taxes together will continue to contribute about one-half of budgetary revenues.

Government security yields moderately lower.

The gradual hardening of Treasury bill yields that began in mid-January had run its course by early March. (See Table 2.) In the succeeding five weeks, the yield on the 3-month bill recorded a net decline of 8 basis points, while that on the six-month bill fell even more sharply. Yields on longer-term bonds, however, continued to stiffen until early April, before moderate declines set in.

The Honourable Walter L. Gordon, Minister of Finance, announced details of a cash offering on April 14 of $400 million Government of Canada non-callable bonds to be dated and delivered on May 1, 1964 as follows:

(1) $325 million, open as to maturity, in the form of

(a) 1 year 2 month 3-1/2 per cent bonds due July 1, 1965 at a price of 98.90 per cent to yield about 4.47 per cent to maturity,

(b) 2 year 7-1/2 month 4-1/2 per cent bonds due December 15, 1966 at a price of 99.65 per cent to yield about 4.64 per cent to maturity, and

(c) 5 year 2 month 5 per cent bonds due July 1, 1969 at a price of 99-3/4 per cent to yield about 5.05 per cent to maturity;

(2) $75 million of 26 year 5-1/4 per cent bonds due May 1, 1990 at a price of 98-5/8 per cent to yield about 5.35 per cent to maturity.

Table 2. Canada: Market Yields on Government Securities
Selected Dates January 1963 - April 1964

Dates		Treasury Bills 3-mos.	Treasury Bills 6-mos.	Bonds Sept. 1965	Bonds June 1967-68	Bonds Jan. 1975-78	Bonds Sept. 1996-March 1998
1963							
Jan.	2	3.94	4.06	4.48	4.48	5.12	5.10
June	12	3.19	3.30	4.07	4.07	4.88	4.90
Sept.	11	3.78	3.98	4.60	4.48	5.27	5.14
Oct.	16	3.54	3.69	4.00	4.29	5.03	5.04
Dec.	31	3.74	3.93	4.20	4.42	5.16	5.02
1964							
Jan.	8	3.80	3.96	4.31	4.43	5.17	5.01
	22	3.74	3.92	4.25	4.50	5.18	5.01
	29	3.77	3.94	4.33	4.51	5.19	5.01
Feb.	26	3.88	4.02	4.29	4.48	5.20	5.02
March	5	3.90	4.06	4.43	4.56	5.25	5.04
	12	3.85	3.99	4.34	4.56	5.22	5.03
	19	3.88	4.03	4.42	4.56	5.22	5.04
	25	3.88	4.04	4.48	4.61	5.25	5.07
April	1	3.87	4.02	4.49	4.61	5.28	5.10
	8	3.82	3.88	4.40	4.60	5.26	5.07

The new 4-1/2 per cent bonds due December 15, 1966 are an addition to $250 million of 4-1/2 per cent bonds due December 15, 1966, dated September 15, 1961 and December 15, 1963.

The proceeds of this offering will be used to redeem $360 million of 4 per cent Government of Canada bonds maturing May 1, 1964 and for general purposes of the Government of Canada.

The Minister stated that the Bank of Canada has agreed to acquire $250 million of the new 5 year 2 month bond in exchange for an equal par value of 3-3/4 per cent bonds maturing September 1, 1965. This would be in addition to the cash offering. He noted that this exchange with the Bank of Canada would reduce the amount of the outstanding September 1, 1965 maturity to $750 million. This 1965 maturity was originally issued in the amount of $1267 million and this transaction with the Bank of Canada is the second step in a programme designed to reduce the amount of the ultimate refunding at maturity to more manageable proportions.

The differential yields on Canadian securities issued in Canadian markets over comparable Canadian issues in the U.S. had previously shown some indications of widening in the period immediately following the U.S. interest-equalization tax proposal. In four typical instances, however, the differential in recent weeks has slipped slightly below peak levels attained at various earlier dates. (See Table 3.)

Table 3. Differential Yields on Canadian Securities in U.S. and Canadian Markets, (in per cent per annum)

	1963 July 3	1963 Nov. 20	1964 Jan. 16	1964 Feb. 27	1964 March 12	1964 March 26	1964 April 9
Government of Canada							
Canada (1975)	4.99	5.19	5.21	5.17	5.19	5.27	5.25
United States (1974)	4.30	4.41	4.63	4.50	4.43	4.46	4.47
Differential	+.69	+.78	+.58	+.67	+.76	+.81	+.78
Province of Ontario							
Canada (1981)	5.21	5.37	5.48	5.40	5.40	5.45	5.45
United States (1984)	4.43	4.57	4.56	4.52	4.56	4.56	4.60
Differential	+.78	+.80	+.92	+.88	+.84	+.89	+.85
Quebec Hydro							
Canada (1982)	5.34	5.63	5.68	5.70	5.68	5.68	5.68
United States (1984)	4.62	4.68	4.68	4.65	4.65	4.69	4.67
Differential	+.72	+.95	+1.00	+1.05	+1.03	+.99	+1.01
Toronto Metro							
Canada (1982)	5.34	5.52	5.52	5.59	5.59	5.59	5.59
United States (1979)	4.44	4.55	4.58	4.58	4.49	4.51	4.56
Differential	+.90	+.97	+.94	+1.01	+1.10	+1.08	+1.03

Source: Nesbitt, Thompson & Co. Ltd. Financial Notes.

Little change in other bond yield averages.

At the end of March, the McLeod, Young, Weir index of bond yields remained at 5.59%, unchanged from the preceding month. (See Table 4.) A small decline in the provincial list was offset by lesser increases for public utilities and industrials, whereas the normally volatile municipal groups held steady. At its present level, the overall index remained 7 percentage points below its recent peak, attained at the end of August 1963.

Dominion-provincial fiscal negotiations renewed.

Particularly difficult problems of fiscal relationships between the Federal and Provincial governments came up for renewed discussion at a three-day conference at Quebec City, March 31-April 2, 1964. At issue are conflicting views concerning appropriate sources of funds and distribution of responsibilities among the respective jurisdictions, particularly as they involve shared-cost welfare programs aimed at creating nation-wide standards of performance in the face of uneven fiscal capacity of the various provinces. Programs are of two types: (a) those which provide current welfare services, of which by far the largest is hospital insurance, estimated to cost the federal Treasury over $400 million in fiscal 1965; and (b) conditional grants in support of various capital programs, such as the trans-Canada highway, which are an inevitable element of a flexible federal policy to promote general economic activity and higher levels of employment.

Table 4. Canada: 40 Bond Yield Average

End of Month	10 Provincial	10 Municipal	10 Public Utilities	10 Industrial	40 Average
1962					
April	5.19	5.38	5.17	5.15	5.22
July	5.87	6.17	5.74	5.77	5.89
1963					
January	5.36	5.54	5.43	5.29	5.41
March	5.39	5.51	5.49	5.42	5.45
May	5.29	5.39	5.34	5.26	5.32
August	5.67	5.88	5.61	5.49	5.66
October	5.51	5.66	5.48	5.40	5.51
December	5.53	5.67	5.50	5.39	5.52
1964					
January	5.58	5.72	5.52	5.48	5.57
February	5.61	5.71	5.55	5.49	5.59
March	5.57	5.71	5.57	5.52	5.59
Change since					
April 1962	+.38	+.33	+.40	+.37	+.37
July 1962	-.30	-.40	-.17	-.25	-.30
August 1963	-.10	-.17	-.04	+.03	-.07
October 1963	+.06	+.05	+.09	+.12	+.08

Source: McLeod, Young, Weir and Company.

The Quebec Premier detailed a plan for contracting-out of over 60 shared-cost programs involving federal payments to the provinces of over $1 billion in fiscal 1965, while wishing to remain a party to various of those programs that, though involving capital expenditures, are necessarily terminal in character. Quebec also jeopardized the future of the Canada Pension Plan by insisting on its intention of moving ahead on a provincial basis. Quebec's submission to the Conference re-emphasized its support for adoption of a "25-25-100" tax formula to cover the provincial portion, respectively, of personal income, corporate income, and inheritance taxation.

A rather bland communique, issued at the termination of the Conference, (a) indicated agreement that the federal government should immediately enter into negotiations with provinces concerning possible contracting-out from programs of a permanent nature involving fairly regular annual expenditures; and (b) "gave consideration" to the immediate establishment of a tax structure committee, that would deliver an interim report before the end of 1964.

Subsequently, on April 20, the Prime Minister announced an agreement on new tax-sharing arrangements that provides the basis for a new contributory Canadian Pension Plan, applied uniformly across Canada. The federal government will make available to the provinces an additional 2 per cent in personal income tax abatement for the fiscal year 1965-66 (estimated to represent some $60 million), and a further 2 per cent in 1966-67. Under existing agreements, the provinces receive 18 per cent of personal income tax collections, about 22 per cent of corporate income taxes, and 75 per cent of federally-collected succession duties.

New bond flotations below preceding year.

According to reports of A.E. Ames & Company, by the end of March new bond flotations in 1964 had reached a cumulative total of $906.33 million, as contrasted with the figure of $1320.91 million to the corresponding date a year ago. During this period, however, the amount of capital supplied from Canadian sources alone actually rose slightly, by contrast with the decline of $445 million of flotations in U.S. currency. Other information suggests that the current rate of new borrowing in the U.S. may be somewhat higher than these figures imply.

Stock markets active and strong.

Beginning in early March, the D.B.S. index of stock market prices hit record peaks for six successive weeks, rising from a weekly average of 148.0 to 158.3. Texas Gulf Sulphur's announcement of a major mineral discovery in the Timmins, Ontario, area spurred feverish activity on the Toronto Stock Exchange, where a record turnover of over 28 million shares changed hands on Friday, April 17.

Government of Canada deposits at chartered banks remain high.

The total money supply, as measured by chartered bank deposit liabilities and total currency outside banks, amounted to $16,942 million by mid-April. The increase over the past year was 8 per cent. A goodly portion of the rise continued to be immobilized in Government of Canada deposit balances, which were down from $1,026 million on February 26, 1964 to $721 million by April 15, but contrasted sharply with a level of $97 million at the end of April 1963. Outstanding general loans of the chartered banks, on a seasonally adjusted basis, averaged $7,393 million in March 1964, as compared with $6607 million a year ago. For the period April 1-22, 1964, the chartered banks cash ratio averaged 8.[illegible] per cent and liquid asset ratio, 17.02 per cent.

Stability continues in foreign exchange quotation.

The range in variation of the U.S. dollar quotation on Canadian currency, which has been exceedingly narrow since the beginning of the calendar year, has been even more limited during March and the first half of April.

Table 5. Large Issues Sold During March 1964
(in millions of dollars)

March			
Anglo American Molybdenite Mining Corp.	5	6-1/2%	March 1, 1973
*Simpsons Ltd. Debentures	10	5-3/4%	February 1, 1984
Toronto-Dominion Tower Ltd First Mortgage Sinking Fund Bonds	20	5-5/8%	April 1, 1989
*Simpsons Acceptance Co. Ltd. Secured Debentures	10	5-3/4%	April 1, 1984
Dominion Tar & Chemical Co. Ltd. Debentures	4	5-3/4%	April 1, 1966-70
	16	5-3/4	April 1, 1984
Canadian Breweries Ltd., Sinking Fund Debentures	25	5-1/2%	April 1, 1989
Province of Ontario	50	5%	April 15, 1973
		5-1/4%	April 15, 1984
Alberta Municipal Financing Corp.	15	3-1/2%	April 15, 1965
East Coast Smelting & Chemical Co. Ltd.	5	5.55%	March 15, 1968-72
	15	5.85%	March 15, 1986
Niagara Finance Co. Ltd.	10	5-3/4%	April 15, 1984

Source: A.E. Ames & Co.,Weekly Bond Sales Summary.
* Possibly duplicating items, though listed separately in source.

Offered rates in the New York market have held very close to the vicinity of 92.55 U.S. cents, despite the announcement of a further loss of $76.8 million in official reserves during March, the fourth successive month of minor decline:

End of month		Cdn. $ in U.S. funds (U.S. cents)	Cdn. official Reserves (million of U.S. dollars)
November	1963	92.76	2,631.0
December	1963	92.53	2,595.0
January	1964	92.57	2,582.4
February	1964	92.57	2,542.3
March	1964	92.54	2,465.5

Incentive for arbitrage inflows increases.

The small discount on the forward Canadian dollar that prevailed from mid-January through mid-March reduced the covered interest arbitrage on three-month Treasury bills to as little as .10 per cent per annum as of January 23. The margin widened to .34 per cent in late March, as the forward discount was converted into a comparably small premium. By April 16, the net incentive had narrowed somewhat, despite some upward pressure on the forward rate, as the Canadian bill rate declined in keeping with a lower rate on U.S. Treasury bills. (See Table 6.)

Table 6. Canadian-U.S. Arbitrage Computations on Three Month Paper, Selected Dates
(per cent per annum)

Dates Week of		Treasury Bill: Cdn. Bill N.Y.	U.S. Bill N.Y.	Spread Favor Canada	Fwd. Canada Dollar	Canada Bill Diff'l.	Prime Finance Company Paper: Cdn. Paper Cdn. $	Cdn. Paper Fully Hedged	U.S. Paper	Cdn. Paper Diff'l.
1963										
Dec.	13	3.59	3.49	+.10	--	+.10	4.25	4.20	3.75	+.45
1964										
Jan.	3	3.66	3.51	+.15	+.07	+.22	4.25	4.20	3.875	+.325
	24	3.66	3.49	+.17	-.07	+.10	4.00	3.85	3.75	+.10
Feb.	14	3.68	3.51	+.17	-.04	+.13	4.00	3.90	3.75	+.15
	28	3.79	3.55	+.24	-.04	+.20	4.125	4.02	3.75	+.27
March	5	3.81	3.55	+.26	-.04	+.22	4.125	4.02	3.875	+.145
	12	3.75	3.53	+.22	-.04	+.18	4.125	4.02	3.875	+.145
	19	3.73	3.53	+.20	+.04	+.24	4.125	4.125	3.875	+.25
	26	3.79	3.52	+.27	+.07	+.34	4.125	4.125	3.875	+.25
April	2	3.78	3.51	+.27	+.07	+.34	4.125	4.125	3.875	+.25
	9	3.76	3.46	+.28	+.07	+.35	4.125	4.125	3.75	+.25
	16	3.66	3.46	+.20	+.07	+.27	4.125	4.125	3.75	+.375

European and British Commonwealth Section.

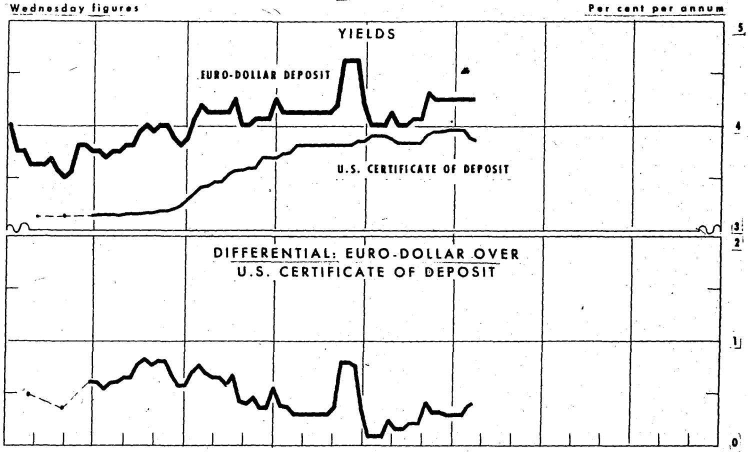
Chart 1

INTERNATIONAL MONEY MARKET YIELDS FOR U.S. DOLLAR INVESTORS

3-MONTH EURO-DOLLAR DEPOSIT VS. CERTIFICATE OF DEPOSIT

Wednesday figures

Per cent per annum



NEW YORK OFFER RATES ON SELECTED 3-MONTH INVESTMENTS

Friday figures

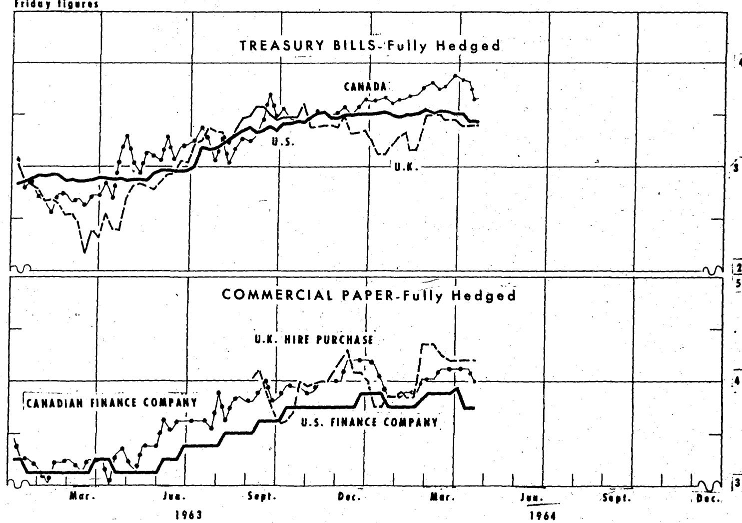


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Chart 2

INTEREST ARBITRAGE, UNITED STATES / CANADA

Thursday figures

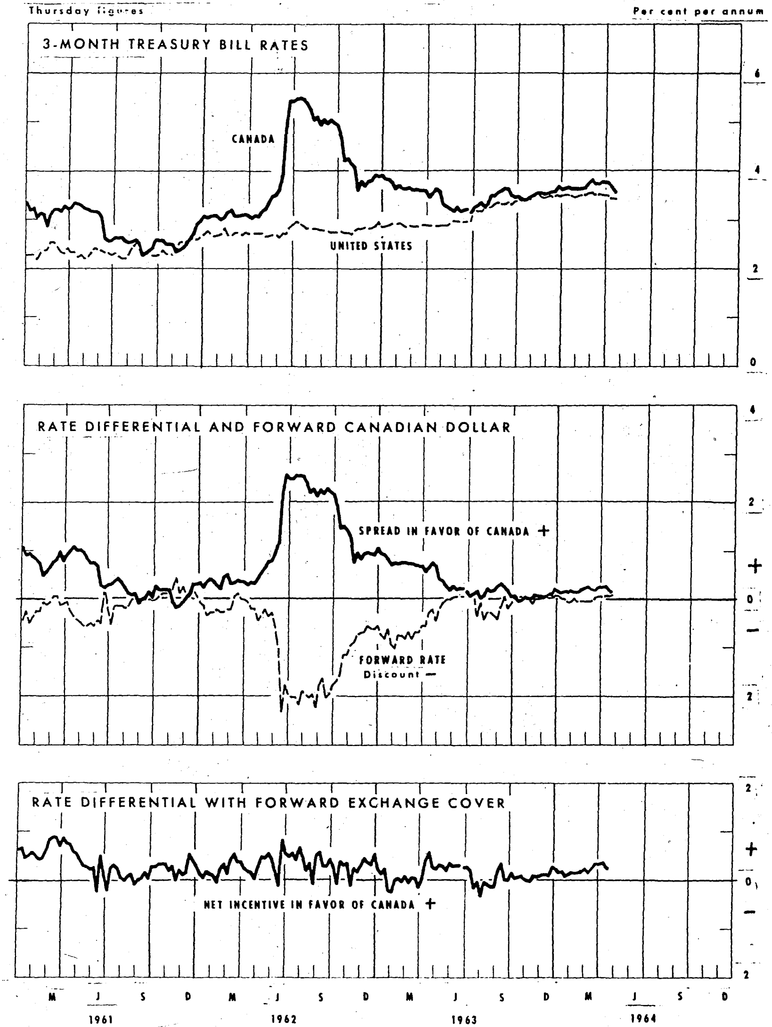

Chart 3

INTEREST ARBITRAGE, NEW YORK/LONDON

Friday figures

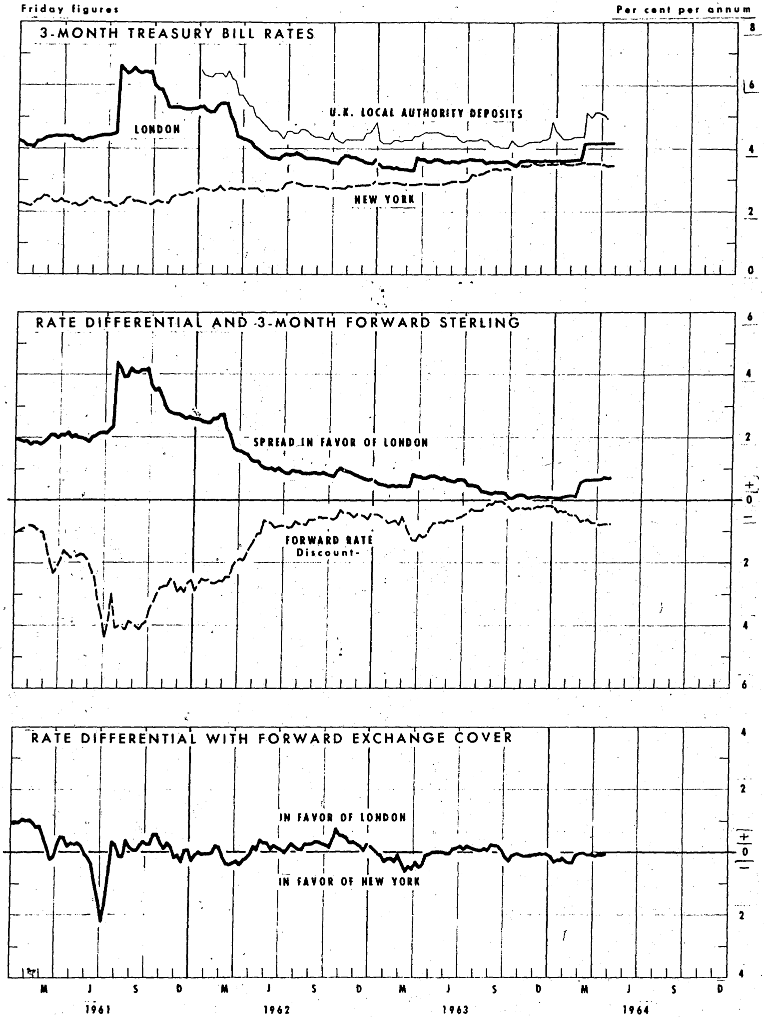

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Chart 4

INTEREST ARBITRAGE FOR GERMAN COMMERCIAL BANKS

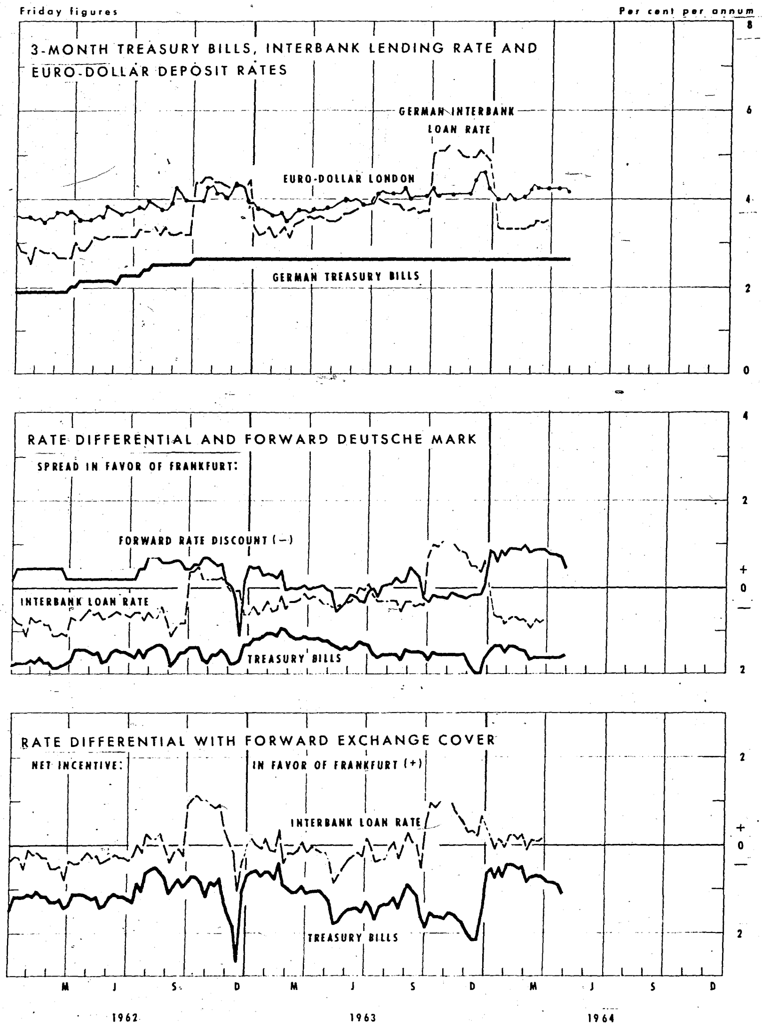
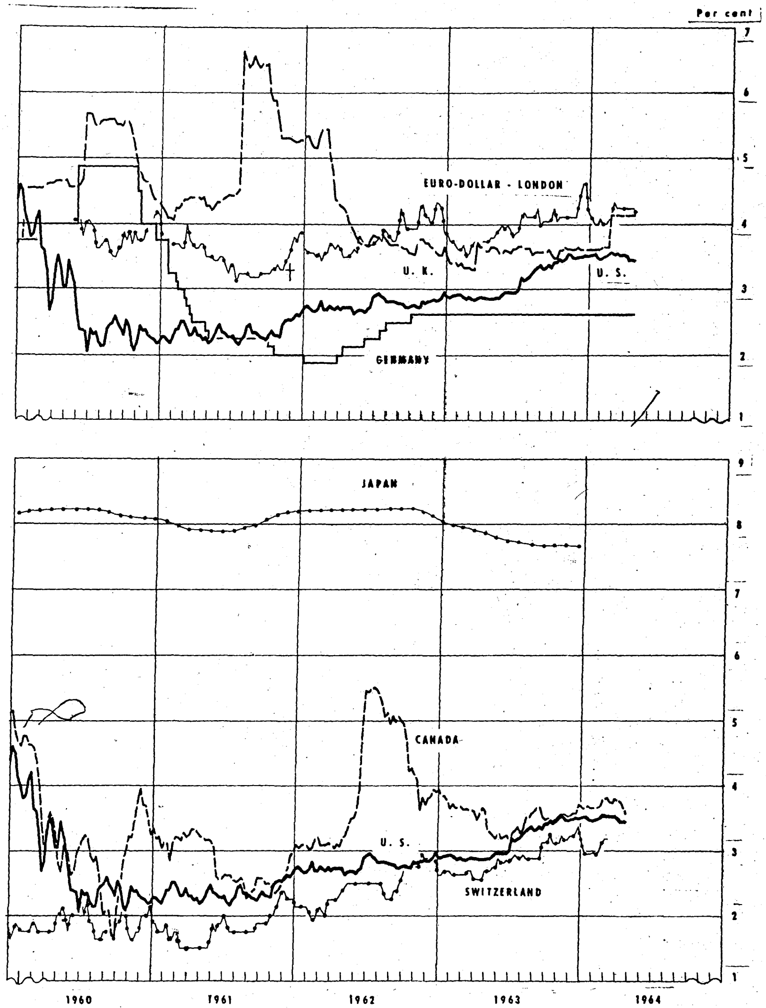


Chart 5
SHORT-TERM INTEREST RATES *



* 3-month treasury bill rates for all countries except Japan (Average rate on bank loans and discounts) and Switzerland (3 month deposit rate)
† 3 month rate for U. S. dollar deposits in London

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Chart 6

LONG-TERM BOND YIELDS

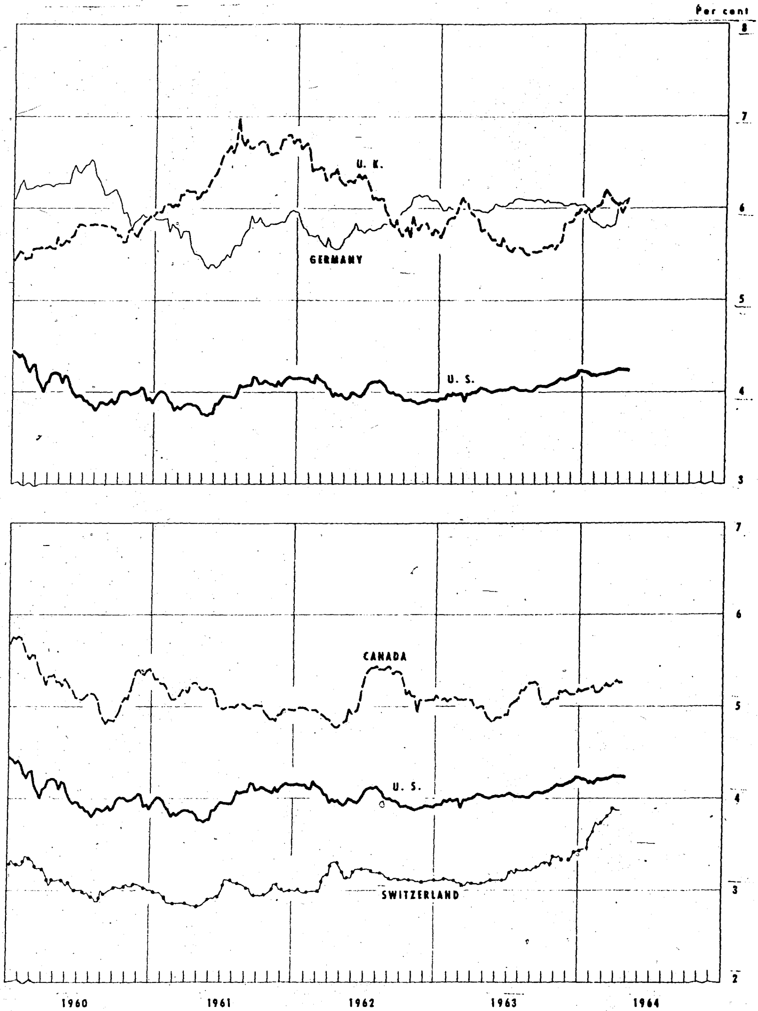
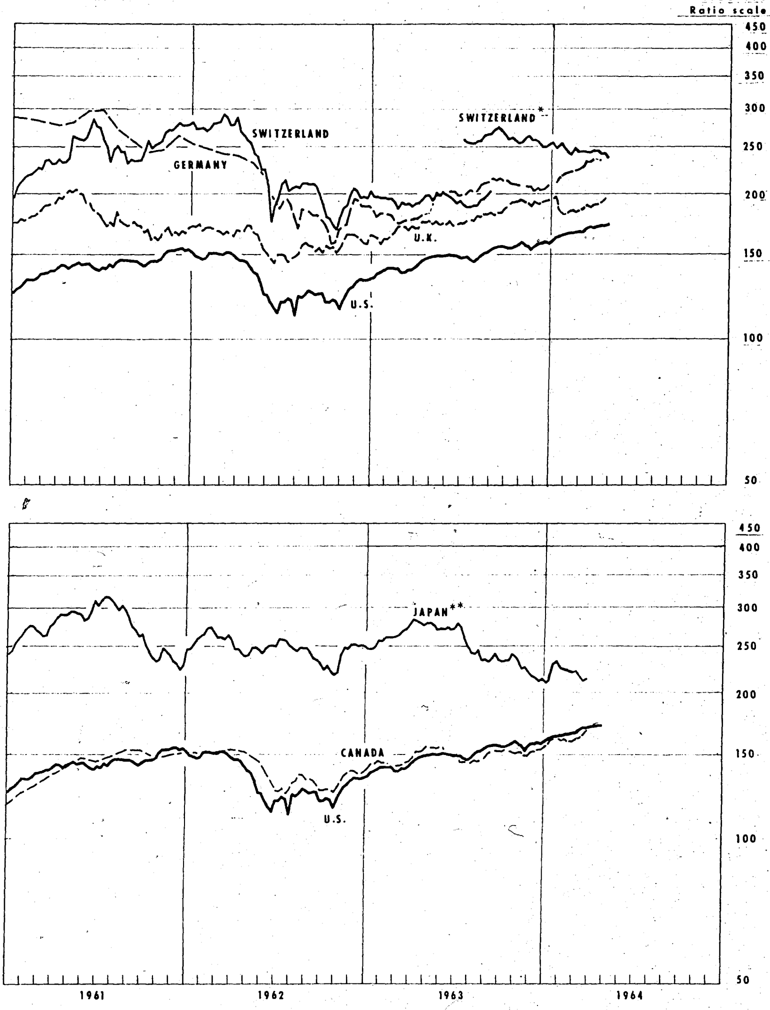


Chart 7

INDUSTRIAL STOCK INDICES



* New series. Swiss Bank Corporation industrial stock index

** Japan index of 225 industrial and other stocks traded on the Tokyo exchange

Chart 8
SPOT EXCHANGE RATES - MAJOR CURRENCIES AGAINST U.S. DOLLAR

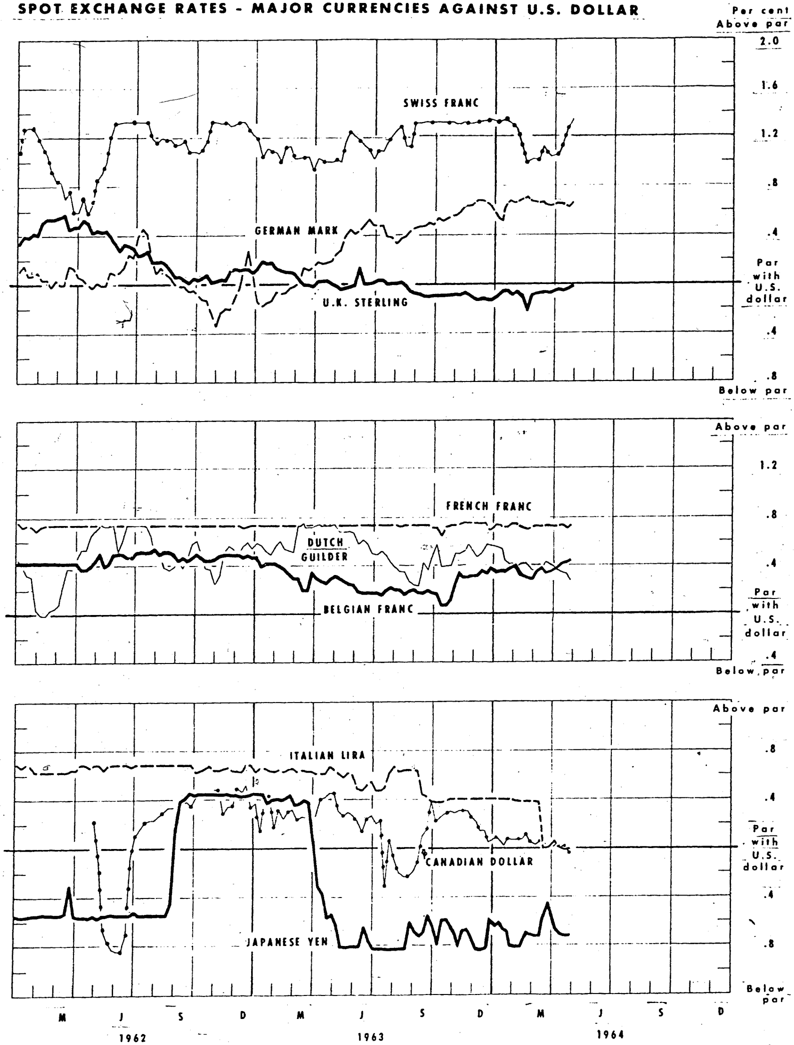


Chart 9

3-MONTH FORWARD EXCHANGE RATE

Friday figures