

September 29, 1961

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1961 27 OCT 9 1961 FEDERAL RESERVE BANK OF ST. LOUIS
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CAPITAL MARKET DEVELOPMENTS ABROAD

- I. Germany
- II. Nine Charts on Financial Markets Abroad

I. Germany: Money and Capital Markets During August

After remaining tight for almost two months the German money market eased noticeably just before the middle of August and remained very liquid until early in September when it tightened again, mainly because of a September 10 tax deadline. Reduced reserve requirements, lower private exports of funds, and increased public expenditures helped to supply the money market with funds. In addition to twice reducing reserve requirements, the Federal Bank also contributed to the easing tendencies by releasing the "Blessing loan" and channeling special funds temporarily to the money market.

Except for some selling by foreign holders, the bond market was relatively inactive during August. Industrial bond prices ended the month at about the end-of-July level, but prices of public authority and mortgage bonds declined further. Long-term yields are now in the neighborhood of 6 per cent. after having declined for about a year to around 5.5 per cent in June.

Political tension continued to be a dominant influence on the German stock market as well as on the bond market. Following the closing of the crossing points between East and West Berlin on August 11, German shares declined sharply and a week later the market suffered its most severe setback since last March. In the face of the international situation the German banks preferred to keep their liquidity high and abstained from market support operations. There has been some improvement in market prices in September.

Money Market. After mid-August the German money market was unusually liquid. On several occasions during the latter half of the month call money rates fell as low as 1 3/4 per cent, or more than one per cent below the rediscount rate. One-month money was as low as 2 3/4 per cent in the latter half of the month and generally below 3 per cent throughout the month. The main factors contributing to the ease were the August 10 reduction (retroactive to August 1) of the minimum reserve requirements for the banks, an increase in public expenditures, and a decrease in private money exports.

* Please change the September 11 issue from No. 23 to No. 24.

NOT FOR PUBLICATION

DECONTROLLED AFTER SIX MONTHS

Private money exports were influenced by the Federal Bank's action of August 11 abolishing the arrangement under which the Bank had provided the German commercial banks with free forward cover for their dollar holdings. The banks are now charged 1/4 of one per cent per annum on forward dollar swaps with the Federal Bank. The Federal Bank apparently decided that private money exports needed no further encouragement, especially in view of the withdrawal of foreign funds from Germany, which were stimulated by the Berlin situation. The Federal Bank also saw the need to ease the market in anticipation of the large tax payments coming due on September 10.

In the latter part of August the Federal Bank took further action to bring about an easing in the market. On August 24 it agreed to permit the German commercial banks to liquidate their DM 1 billion (\$250 million) "Blessing loan." Under its original terms this loan, taken up in the form of Treasury bonds in August 1960, was not to be liquidated prior to expiration of a two-year period, the commercial banks having agreed to hold the bonds off the market until maturity in August 1962. In its desire to increase money market liquidity the Federal Bank last month not only agreed to the immediate disposal of these bonds by the banks; it also offered a special inducement to the banks to cash them in. The banks had paid a price of 89 which yielded 5 1/2 per cent. The Federal Bank offered to take the bonds back at a price of 97 although the price on the basis of their maturity of one year would be only 94 1/2. The banks were thus enabled to realize an interest of 8 per cent on their loan for the one year elapsed. Moreover, sales to the Bundesbank rather than in the market would bring about an increase in bank liquidity, at the same time keeping out of the market a highly liquid instrument yielding 5 1/2 per cent as against the rate of around 2 1/2 per cent on comparable money-market securities.

A further aid to the money market in August was the Federal Bank's action in making available to the money market approximately DM 100 million (\$25 million) of the DM 470 million proceeds from the Volkswagen share sale. These funds, which eventually are to be used for foreign aid, were lying idle in the account of the Kreditanstalt fuer Wiederaufbau (Reconstruction Loan Corporation). According to press reports the DM 100 million were channeled to the money market by the end of August. The amount thus made available is equivalent to one-fourth of the amount provided by the August 10 reduction in reserve requirements, which released about DM 400 million to the banking system.

In the first week of September the money market tightened moderately and rates rose markedly as had been expected in view of the September 10 tax deadline. The rise brought short-term almost to the levels of early August. The Federal Bank reacted by announcing on September 7 another reduction in the minimum reserve requirements, thus releasing another DM 400 million to the commercial banks. Rates eased after the September 10 tax payment, although rates on call and one-month money remained above the mid-August levels.

Frankfurt Inter-bank Money Rates

	Day-to-day money		One-month loans	Three-month loans
	Lowest rate	Highest rate		
<u>1961</u>				
May (monthly range)	2.38	3.13	2.75 - 3.13	2.88 - 3.25
June "	1.75	3.13	2.75 - 3.13	3.00 - 3.25
July "	2.38	3.13	2.88 - 3.00	3.00 - 3.13
Aug. (weekly range) 1-6	3.00	3.13	3.00	3.13
" 7-13	2.13	2.88	2.88 - 3.00	3.00 - 3.13
" 14-20	1.75	2.25	2.88 - 3.00	3.00 - 3.13
" 21-27	1.75	2.00	2.75 - 2.88	2.88 - 3.00
" 28-31	1.75	1.88	2.75 - 2.88	2.88 - 3.00
Sept. " 1-10	2.75	3.00	2.88 - 3.00	2.88 - 3.00
" " 11-17	2.25	2.63	2.63 - 3.00	2.75 - 3.00
" " 18-24	2.25	2.75	2.75 - 3.00	2.88 - 3.13

There was no change during August in the rates at which the Federal Bank is prepared to sell Treasury bills and short-term bonds in the open market; and as of September 28, they still remained at the levels set on May 5.

From	60-90 days	6-month
	<u>Treasury bills</u>	<u>Treasury bonds</u>
Dec. 20, 1960	3.75	4.00
<u>1961</u>		
Jan. 20	3.75	3.50
Mar. 23	2.50	2.75
Apr. 26	2.38	2.63
May 5	2.25	2.50

Throughout August and during the first three weeks of September the margin of advantage between the Frankfurt money market and London Euro-dollar call rates continued to shift back and forth but the spread on either side remained small, almost continuously below 1/2 a percentage point. The spread between the Frankfurt three-month loan rate and the London three-month rate on Euro-dollars rose slightly toward the end of August but continued to be quite small. There has not been a significant spread between these rates since mid-June. Nevertheless, German banks continued to hold most of their foreign assets in the three-month Euro-dollar accounts as they thereby availed themselves of the privilege of offsetting their foreign assets against their foreign liabilities for purposes of determining required reserves. (The reserve ratios against foreign liabilities have for some time been at the maximum legal rates.) However, the tendency of some foreigners to reduce their DM balances in view of the Berlin situation, and the strengthening of the dollar and sterling against the mark, are said to be operating to reduce the opportunities of the German commercial banks to profit from this reserve-requirement advantage in keeping balances abroad. The private banks reportedly have generally exhausted this possibility of reducing their minimum reserve requirements, and there are

reports that German banks have recently been repatriating funds, thus helping to ease the domestic money market.

German money-market rates vs. London Euro-dollar rates

	Rate for U.S. dollar	Incentive in favor of London Euro-dollar call rate	Rate for U.S. dollar deposits on 3 months basis	Incentive in favor of London Euro-dollar 3-month rate		
Day-to-day money in Frankfurt	deposits at call in London	3 months money in Frankfurt	3 months in London			
July 7	2.63	2.75	0.12	3.13	3.31	0.18
14	3.07	2.63	-0.44	3.13	3.25	0.12
21	2.94	2.63	-0.31	3.07	3.25	0.18
28	2.44	2.75	0.31	3.07	3.31	0.24
Aug. 4	3.07	2.75	-0.32	3.13	3.25	0.12
11	2.38	2.75	0.37	3.07	3.25	0.18
18	2.07	2.50	0.43	3.07	3.19	0.12
25	1.82	2.38	0.56	2.94	3.19	0.25
Sept. 1	2.94	2.50	-0.44	3.00	3.19	0.19
8	2.75	2.50	-0.25	2.94	3.19	0.25
15	2.31	2.50	0.19	2.94	3.25	0.31
22	2.56	2.50	-0.06	3.00	3.25	0.25

In early August the spread between Treasury bill yields in the United States and Germany on a net incentive basis favored the U.S. bill but only negligibly. With the Bundesbank's imposition on August 14 of the charge of 0.25 per cent per annum on its forward dollar swap operations with German commercial banks the spread shifted to favor the German Treasury bill on a net incentive basis, but again only negligibly. After having been reduced on August 11 to 0.63 in favor of the German 3-months' interbank loan rate on a net incentive basis, the spread between this rate and the U.S. Treasury bill rate increased again to about its July magnitude, between 0.85 and 0.90, and increased further on September 22 to 1.00 per cent per annum in favor of the German inter-bank loan rate.

German Inter-bank loan rate vs. U.S. bill rate					Bundesbank's Treasury bill selling rate vs. U.S. bill rate			
		Net covered			Net covered			
		German 3 mos. inter-bank loan rate	U.S. bill rate	Spread over U.S. of German rate ^{1/}	incentive in favor of German rate ^{1/}	German 3 mos. bill rate	Spread over U.S. bill	incentive in favor of German rate ^{1/}
1961								
July	7	3.13	2.30	0.83	0.83	2.25	-0.05	-0.05
	14	3.13	2.20	0.93	0.93	2.25	0.05	0.05
	21	3.07	2.16	0.91	0.91	2.25	0.09	0.09
	28	3.07	2.24	0.83	0.83	2.25	0.01	0.01
Aug.	4	3.13	2.29	0.84	0.84	2.25	-0.04	-0.04
	11	3.07	2.44	0.63	0.63	2.25	-0.19	-0.19
	18	3.07	2.47	0.60	0.85	2.25	-0.22	0.03
	25	2.94	2.34	0.60	0.85	2.25	-0.09	0.16
Sept.	1	3.00	2.35	0.65	0.90	2.25	-0.10	0.15
	8	2.94	2.31	0.63	0.88	2.25	-0.06	0.19
	15	2.94	2.27	0.67	0.92	2.25	-0.02	0.23
	22	3.00	2.25	0.75	1.00	2.25	--	0.25

^{1/} To encourage capital outflow the Bundesbank provided forward dollars flat to German banks until August 14. After that date a charge of 0.25 per cent per annum was imposed on such dollar swap operations.

Foreign Trade. Seasonally adjusted West German trade figures for the periods indicated are as shown below.

		Exports	Imports	Trade balance
		(in millions of U.S. dollars)		
1960		11,374	10,129	1,245
1961	- I	3,141	2,556	585
	- II	3,231	2,807	424
	April	1,181	971	210
	May	1,003	932	71
	June	1,050	904	146
	July	1,108	955	153

Foreign Exchange. On the foreign exchange market the strengthening of all major currencies against the mark continued during August but was not markedly accelerated as a result of the tensions over Berlin. Spot dollars were quoted on August 29 at DM 3.9975, just fractionally below parity, and towards the end of the month the discount on three-months' forward dollars was below one per cent as against 1.5 per cent early in August. During August, expectations of the continued strengthening of the

dollar against the mark led to a shift in the terms of payment which operated to realize the expectations indicated. In September the rate on the spot dollar eased somewhat but remained around DM 3.99 as of the 21st.

<u>DM-Dollar middle rate</u>	<u>par (DM 4.00 = \$1)</u>
July 31	3.9832
Aug. 3	3.9844
" 9	3.9938
" 14	3.9930
" 15	3.9950
" 29	3.9975
Sept. 15	3.9878
" 21	3.9885

The discount on three-months' forward sterling declined moderate during August and almost negligibly further in September, and remained sufficiently high to make a covered movement of German banks funds into U.K. Treasury bills unprofitable, despite high bill rates in London.

Bond Market. The bond market continued at a low level of activity during August and September. Bond prices generally fluctuated within a narrow range throughout August. Issues of public authorities weakened in price during the month; the 1959 German Railways 5% Loan was selling at 93 3/4 while the 1959 Equalization of Burdens issue at 5 1/2 per cent was selling at 97 1/2 per cent, down from 97 and 98 1/2 per cent respectively a month earlier. After weakening in mid-August, prices of industrial bonds improved slightly at the end of the month but generally rose only to end-of-July levels. The bond market improved slightly in early September as commercial banks reportedly used some of their liquid funds to support bond prices.

Throughout August and September, mortgage bond activity continued at very low levels. Mortgage rates continued to rise during August and the early part of September. First mortgages are now being issued at 6 and 6 1/4 per cent with an issue price of around 95, while in June, before long-term rates began their upward movement, mortgages issued at 5 1/2 per cent were also being sold at 95. Mortgage banks have experienced increasing difficulty in selling bonds on the market. On the other hand, the demand for mortgage money has slackened as interested borrowers are postponing taking up mortgage credits in the hope of lower rates on long-term capital later this year.

German banking circles believe that the bond market will improve substantially once political tensions subside and the money market becomes more liquid in response to the Federal Bank's continuing relaxation of monetary restrictions. Moreover, it has been pointed out that domestic savings are rising, especially in institutions which traditionally invest in the bond market.

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

		<u>Mortgage bonds</u>	<u>Industrial bonds</u>	<u>Loans of public authorities</u>
1960	July	6.5	6.5	6.7
	Oct.	6.4	6.1	6.3
	Dec.	6.2	6.1	6.1
1961	Jan.	6.2	5.8	6.1
	Feb.	6.2	5.7	6.0
	Mar.	6.1	5.8	5.9
	Apr.	5.9	5.7	5.7
	May	5.8	5.6	5.6
	June	5.8	5.6	5.6
	July	5.8	5.8	5.7

Stock Market. The German stock market in recent weeks has been called a political market. International tension over the Berlin situation has generally been blamed for the decline in German share prices during August, almost to the exclusion of other causes. The market had improved somewhat early in August but on August 14, the day following the sealing off of East Berlin, stock prices, especially prices of internationally-known German chemical and electrical shares, declined by up to 10 per cent.

The decline persisted and a week later, on August 23 and 24, German exchanges suffered their sharpest setbacks since March of this year. Stock prices fell generally to a level slightly more than 30 per cent below the September 1960 peak. While political tensions were a major cause of the decline, the banks' desire to increase liquidity to prepare for a possibly serious crisis was a contributory factor. The banks refrained from the price-supporting operations they generally engage in, preferring to put money out on call even though the call rate had fallen to around 1 3/4 to 1 7/8 per cent as against 3 per cent at the beginning of the month. There was some movement out of German shares into U.S. shares resulting from the comparative firmness of the New York stock exchange at that time. The then-forthcoming Bundestag elections of September 17 also contributed to the uneasiness of the German exchanges. The German markets improved just prior to the elections but weakened slightly afterward. As of September 22, stock prices were at their levels of September 1, still about 9 per cent below their levels of a month earlier.

If the application of a banking consortium headed by the Dresdner Bank is approved by the Frankfurt stock exchange, an American stock, International Telephone and Telegraph, will be listed officially on a German exchange for the first time since 1932, when trading in foreign shares on German stock exchanges ceased. Shares of fifteen other U.S. corporations are now traded on the German curb markets. Of the 67 foreign shares now

traded in Germany, only 17 are officially listed (Fiat, Montecatini, Philips, Unilever among them), the other 50 being traded "unofficially."

Frankfurt Allgemeine Zeitung Index of Industrial Share Prices
(Dec. 31, 1954 = 100)

<u>1961</u>	June 16	477.88
	July 13	440.85
	21	398.85
	28	422.05
Aug.	4	425.39
	11	429.65
	18	422.40
	25	384.58
Sept.	1	388.29
	8	377.83
	15	397.40
	22	389.04

European Section.

II. Nine Charts on Financial Markets Abroad

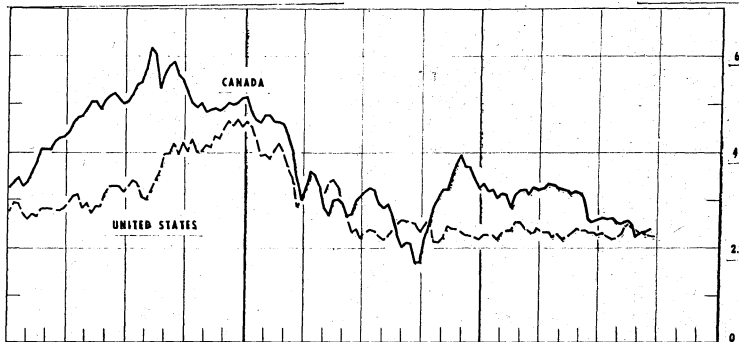
- Chart 1 - Interest Arbitrage U.S./Canada
- Chart 2 - Interest Arbitrage New York/London
- Chart 3 - Interest Arbitrage New York/Frankfurt
- Chart 4 - Interest Arbitrage Frankfurt/London
- Chart 5 - Short-term Interest Rates
- Chart 6 - Long-term Bond Yields
- Chart 7 - Industrial Stock Indices
- Chart 8 - Major Currencies in Terms of
Spot United States Dollar
- Chart 9 - 3-month Forward Rate--London Quotations

INTEREST ARBITRAGE, UNITED STATES / CANADA

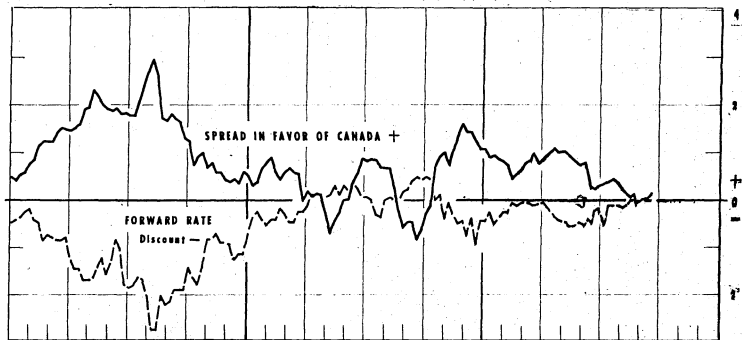
Thursday figures

THREE-MONTH TREASURY BILL RATES

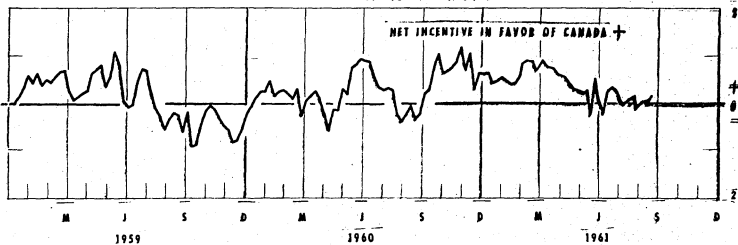
Per cent per annum



RATE DIFFERENTIAL AND FORWARD CANADIAN DOLLAR



RATE DIFFERENTIAL WITH FORWARD EXCHANGE COVER



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Chart 2

INTEREST ARBITRAGE, NEW YORK / LONDON

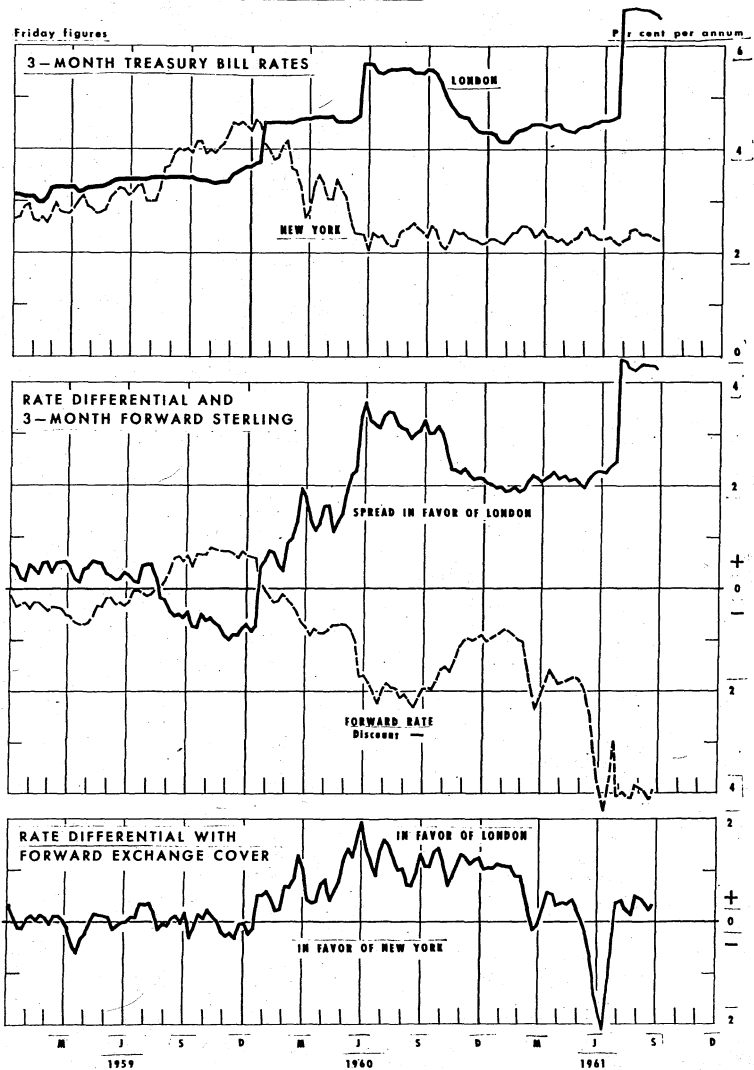


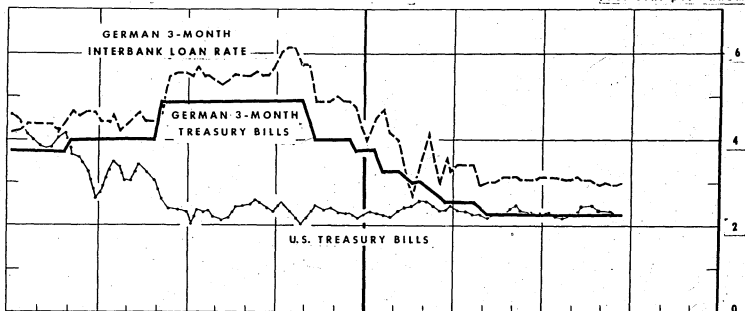
Chart 3

INTEREST ARBITRAGE, NEW YORK/FRANKFURT

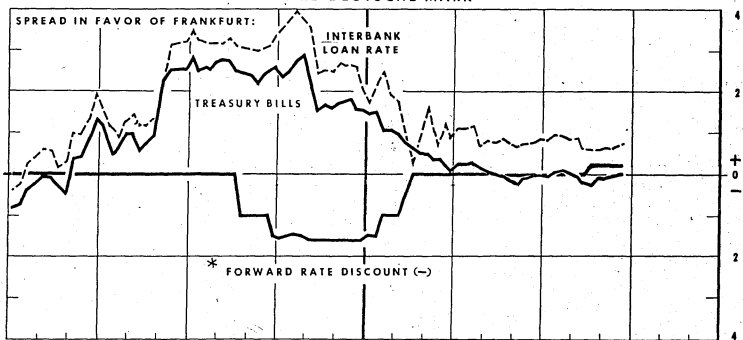
Friday figures

3-MONTH TREASURY BILL RATES AND GERMAN 3-MONTH INTERBANK LOAN RATES

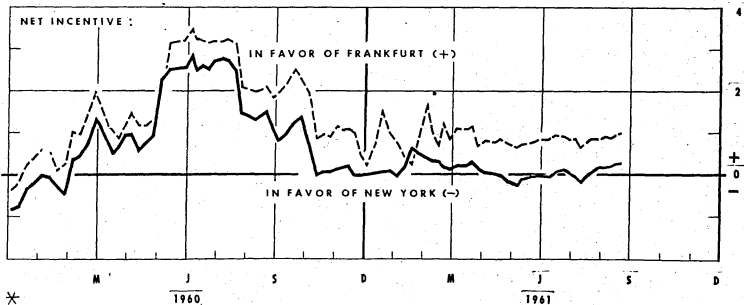
Per cent per annum



RATE DIFFERENTIAL AND FORWARD DEUTSCHE MARK



RATE DIFFERENTIAL WITH FORWARD EXCHANGE COVER



Note: Special forward dollar rate available to German commercial banks.

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Chart 4

INTEREST ARBITRAGE, FRANKFURT/LONDON

Friday figures

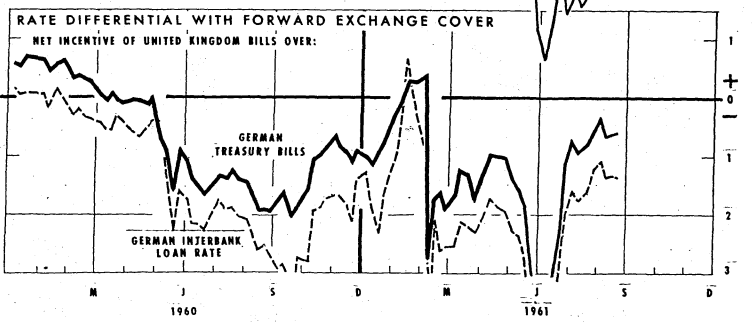
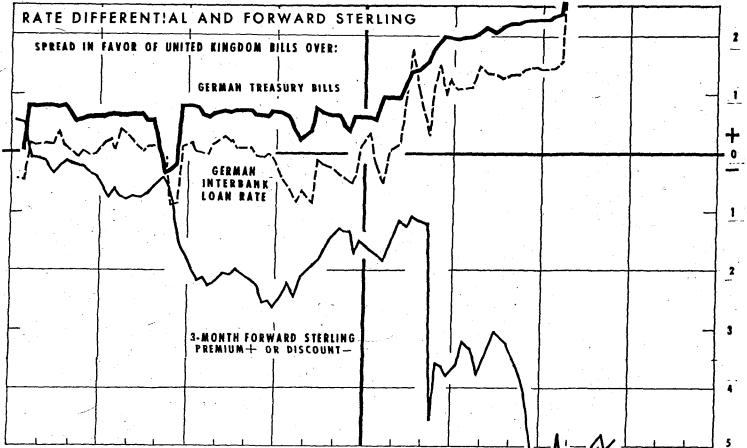
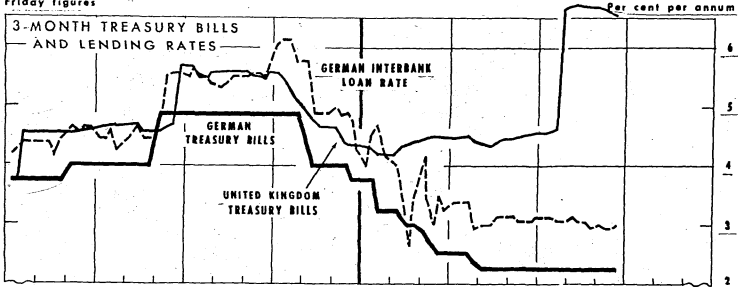
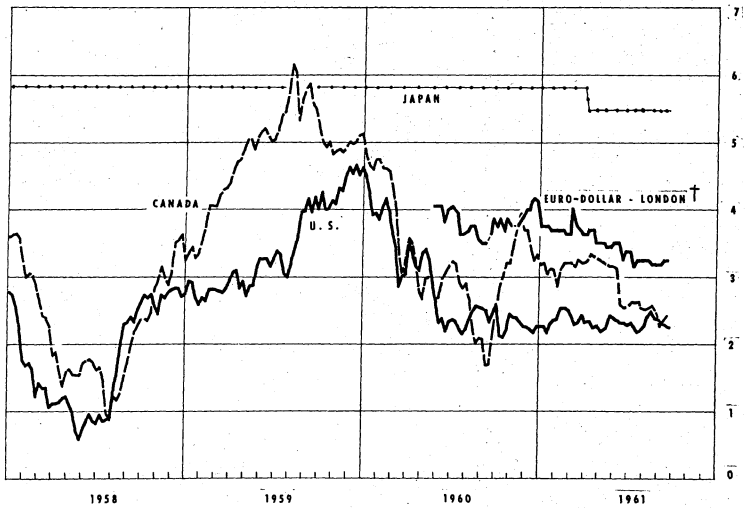
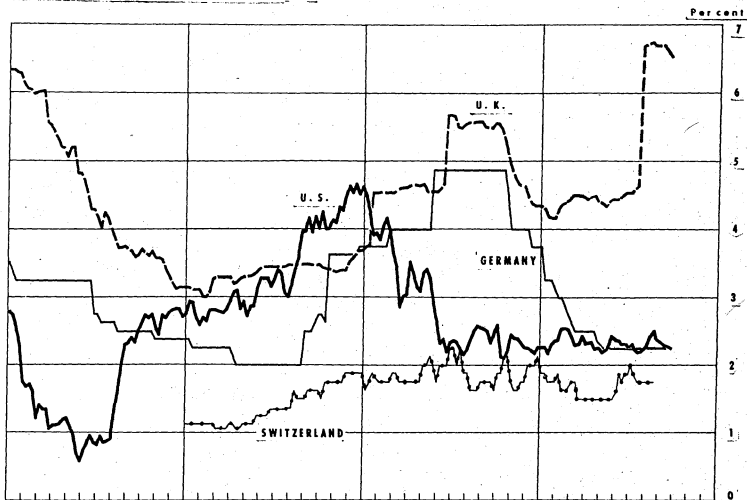


Chart 5
SHORT-TERM INTEREST RATES *

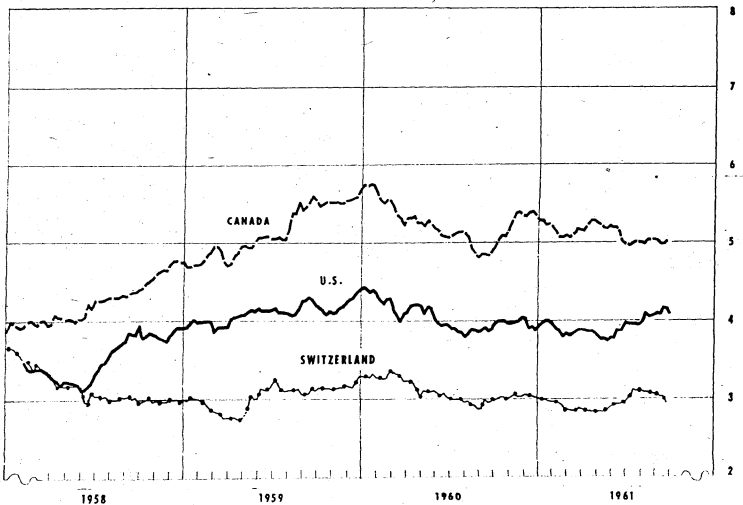
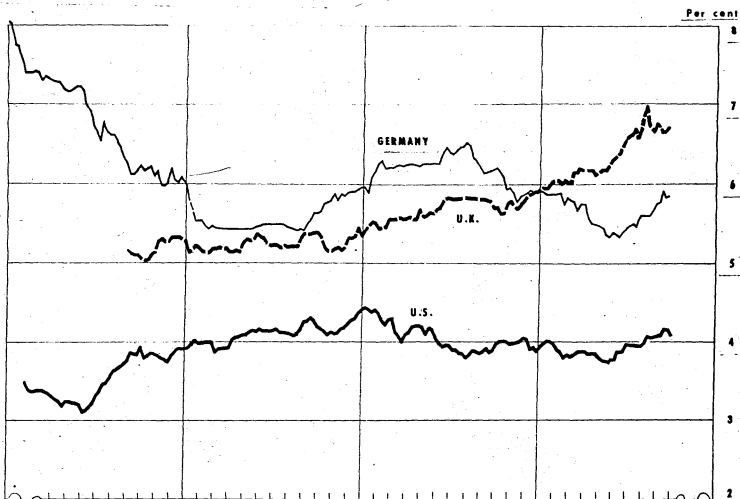


* 3-month treasury bill rates for all countries except Japan (1-month interbank deposit rate) and Switzerland (3-month deposit rate)
 † 3-month rate for U.S. dollar deposits in London

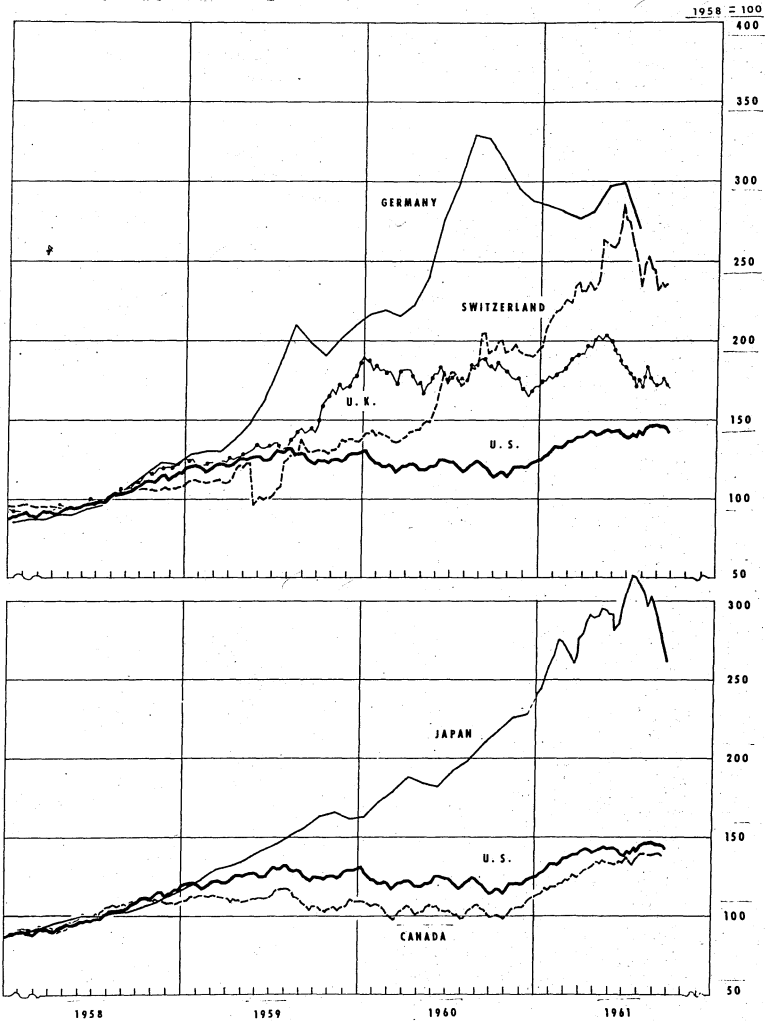
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Chart 6

LONG-TERM BOND YIELDS



INDUSTRIAL STOCK INDICES *



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

Chart 8

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

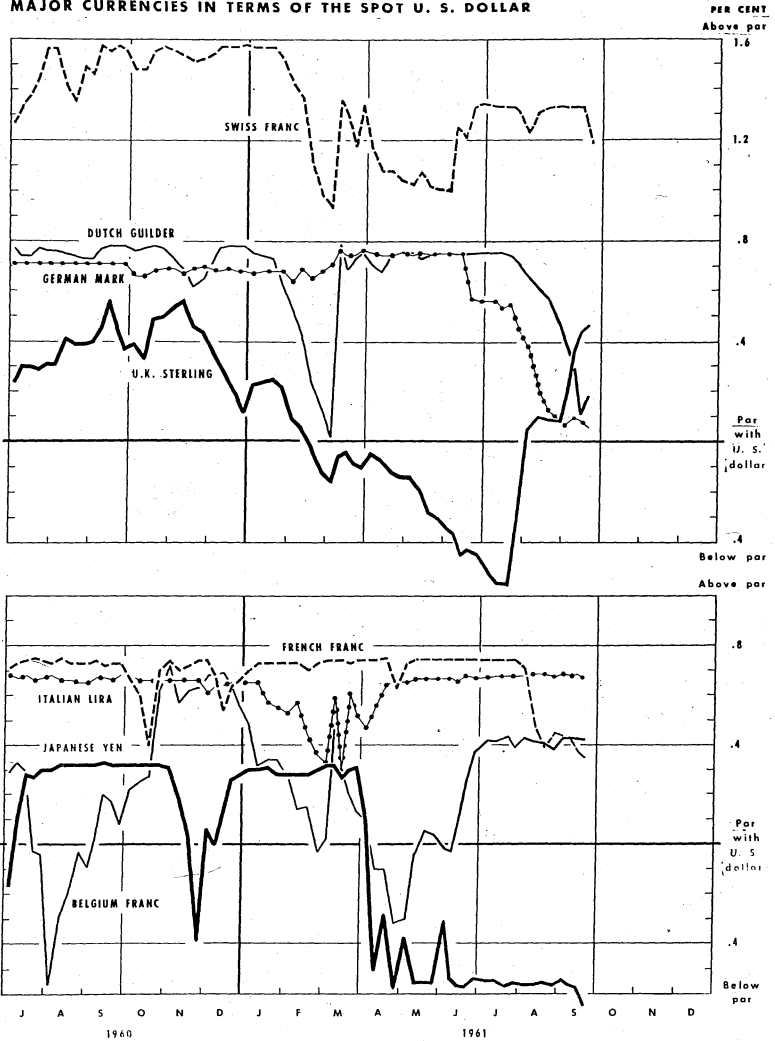


Chart 9

3-MONTH FORWARD RATES - LONDON QUOTATIONS

