

H. 13

No. 33

November 9, 1961.

CAPITAL MARKET DEVELOPMENTS ABROAD

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

I. Canada: Money and Capital Markets During October

Canada's official foreign exchange holdings rose \$187 million during October as a result of official intervention to hold down the exchange rate. Purchases of U.S. dollars by the Exchange Fund materially increased the liquidity of the banking system. As a result, the banks increased their loans by \$121 million without reducing the current high level of bank liquidity.

This liquidity has given new momentum to the general downward trend in Canadian interest rates which began with the change in monetary policy in June. During October, interest rates declined further, especially in longer maturities. Money market rates declined fractionally, with the 3-month Treasury bill down 10 basis points. Bonds with maturities of 5 years and over were down as much as 33 basis points. These declines took place despite switches from longs to shorts by the Bank of Canada. Non-Government securities also showed a decline in yield of about 6 basis points for maturities of about 15 years.

In a recent speech, the Finance Minister commented on the success of the new accord between the Bank of Canada and the Government in the harmonious mixture of fiscal and monetary policies. He pointed to the reduced spread between Canadian and U.S. security yields as a sign of the success which the government's program has yielded. Between early June and November the yield advantage for Canadian securities over comparable U.S. securities have narrowed by the following amounts:

| | |
|-----------------------|-----------------|
| 3-month Treasury bill | 50 basis points |
| 8-year bond | 50 basis points |
| 20-year bond | 20 basis points |
| 35-year bond | 12 basis points |

Money market. Short-term interest rates eased only slightly in October. The average auction yield on the 3-month bill declined from 2.57 per cent on October 5 to 2.47 per cent on November 1, while the 6-month bill declined from 2.84 per cent to 2.69 per cent. (See Table and Chart 1.) On November 1, Treasury bill yields were still close to the lows reached in mid-June, as noted in the following table:

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DECONTROLLED AFTER SIX MONTHS

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| | <u>3-month</u> <u>Treas. bill</u> | <u>6-month</u> <u>Treas. bill</u> |
|---------|--------------------------------------|--------------------------------------|
| June 1 | 3.14 | 3.30 |
| 15 | 2.60 | 2.75 |
| Aug. 31 | 2.26 | 2.55 |
| Oct. 5 | 2.57 | 2.84 |
| Nov. 2 | 2.47 | 2.69 |

Day-to-day money rates declined through the month but rose 27 basis points during the last week when day-to-day loans went up \$37 million. Purchases of foreign exchange by the Exchange Fund swelled chartered bank liquidity and the banks expanded their Treasury bill holdings by \$109 million. The Bank of Canada sold \$105 million of bills.

The yield spread favoring the Canadian over the U.S. 3-month Treasury bill remained about constant through the month at about 20 basis points. The incentive to hold the Canadian bill on a covered basis reached 33 basis points in mid-October. (See Table.)

Bond market. Bond yields eased further during October in both the Government and non-Government sector. According to McLeod, Young, Weir, Ltd., the 40 bond yield average for non-Government bonds fell 6 basis points to 5.41 per cent, as noted in the following table:

| | <u>June 1</u> | <u>Sept. 1</u> | <u>Oct. 2</u> | <u>Nov. 1</u> |
|-----------------------|---------------|----------------|---------------|---------------|
| 10 Provincials | 5.62 | 5.38 | 5.45 | 5.36 |
| 10 Municipals | 5.82 | 5.60 | 5.63 | 5.56 |
| 10 Public Utilities | 5.48 | 5.39 | 5.37 | 5.37 |
| 10 Industrials | 5.60 | 5.43 | 5.42 | 5.35 |
| 40 Bond Yield Average | 5.63 | 5.45 | 5.47 | 5.41 |

Government bond yields declined as much as 33 basis points for 5-year maturities, and up to 15 basis points for longer terms. The following table compares some Canadian Government bond yields for maturities from 5 to 35 years:

| <u>Maturity</u> | <u>June 1</u> | <u>June 15</u> | <u>Oct. 4</u> | <u>Nov. 1</u> |
|-----------------|---------------|----------------|---------------|---------------|
| Sept. 1965 | 4.78 | 4.63 | 4.29 | 3.96 |
| Sept. 1972 | 5.08 | 4.98 | 4.87 | 4.75 |
| Jan. 1975-78 | 5.19 | 5.11 | 5.01 | 4.86 |
| Sept. 1983 | 5.20 | 5.10 | 5.02 | 4.91 |
| Sept. 1996-98 | 5.09 | 5.08 | 5.00 | 4.96 |

As a result of these declines, the spread between the yield on comparable Canadian and U.S. bonds narrowed considerably. The following table compares changes in yield spreads:

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| | <u>June 7</u> | <u>Oct. 4</u> | <u>Nov. 1</u> |
|--------------|---------------|---------------|---------------|
| 8-year bond | 0.81 | 0.45 | 0.30 |
| 20-year bond | 1.27 | 0.91 | 0.78 |
| 35-year bond | 1.34 | 1.23 | 1.21 |

By November 1, Canadian bond yields were well below those of early June, before the Government budget was presented and yield spreads narrowed significantly. The 40-bond yield average declined 22 basis points, while Government bond yields were down as much as 15 to 80 basis points. With rising yields in the U.S. during the June-September period, the wide spreads in favor of Canada on intermediate-term bonds were reduced 30 to 50 basis points.

Chartered bank expansion and money supply. The chartered banks continued to expand loans above seasonal requirements and there was no decline in their liquid asset ratio. General bank loans rose \$121 million, by 2.2 per cent, making the total seasonally-adjusted loan expansion 4.7 per cent since the end of June. Despite this expansion, bank liquid assets averaged 18.8 per cent of deposits in October, compared with a 15 per cent minimum requirement. The money supply rose 1/2 per cent in October and is up about 3 per cent over end June levels on a seasonally-adjusted basis.

Interest rates reduced on term notes. The Bank of Nova Scotia announced an interest rate reduction of 1/4 of 1 per cent on some term notes. The new rates are as follows:

- 2 to 3 year notes, 4-1/4 per cent
- 3 to 4 year notes, 4-1/2 per cent
- 4 to 5 year notes, 4-3/4 per cent

This is the first interest rate reduction announced by the bank since last July 5.

Government cash position. In August, the Federal Government ran a cash deficit (on budgetary and non-budgetary items) of \$97 million, compared with a \$76.8 deficit in August a year ago. For the April-August period, the first five months of the fiscal year, the cash deficit was \$246.2 million compared with \$78.3 million a year ago. In the last week of October, the Bank of Canada was also required to advance \$45 million to the Government to meet current cash needs. This advance probably reflects the need for increased Canadian resources for Exchange Fund operations.

Foreign exchange. As a result of official efforts to hold the Canadian dollar close to 97 U.S. cents, foreign exchange reserves rose \$187 million in October; they declined \$61 million between July and September. This increase reflected a growing demand for the Canadian dollar which produced pressure on the exchange rate. In late October, the Finance Minister stated that the general belief that the "... Exchange Fund will be used to keep the discount from rising above 3 per cent" is a "... mis-interpretation of the Government's intentions." The assurance that the

rate would not be lowered by official actions, combined with the upward pressure earlier in the month, brought an even sharper increase in Canadian dollar purchases toward the end of the month.

In the belief that misinterpretation of his speech had contributed to the inflow, the Minister issued a public statement the following day that he would not support the rate should any large outflow of funds result. The rate then declined slightly to 96.7 U.S. cents and has since remained around that level.

The 3-month forward rate on the Canadian dollar moved to a slight premium in October for the first time since early June. This movement probably reflected expectations that the authorities would not continue to off-set the recent large increases in the demand for the Canadian dollar.

Foreign trade. The seasonally-adjusted trade surplus rose in July despite rising imports. While imports for August rose to a record level, early estimates indicate exports also expanded beyond seasonal expectations. For the first seven months the trade surplus was \$144.2 million compared with a \$14.7 million deficit during the same period last year. The following table shows seasonally-adjusted monthly average trade figures for periods indicated:

| | <u>Exports</u> | <u>Imports</u> | <u>Trade balance</u> |
|----------|----------------|----------------|----------------------|
| 1960 | 451.1 | 458.0 | - 6.9 |
| 1961 - I | 463.6 | 463.8 | - 0.2 |
| II | 472.2 | 444.6 | + 27.6 |
| April | 523.0 | 4.6.1 | +106.9 |
| May | 406.4 | 455.1 | - 48.7 |
| June | 487.3 | 462.7 | + 24.6 |
| July | 528.1 | 476.2 | + 51.9 |
| Aug. | | 513.7 | |

Stock exchange. The Canadian industrial stock index declined some in October for the second straight month. The DBS index of industrials averaged 333.0 during the week ending October 19, about 1 per cent below the last week of September. During the same period, the Standard and Poor index of industrial stocks rose over 1.5 per cent. The following table compares Canadian and U.S. industrial price indices:

| <u>Average for week ending</u> | <u>DBS Industrials</u> | <u>NY Standard & Poor Industrials</u> |
|--------------------------------|------------------------|---|
| Sept. 29, 1960 | 243.6 | 55.69 |
| June 15, 1961 | 329.7 | 69.55 |
| Aug. 27 | 334.8 | 70.40 |
| Aug. 31 | 344.1 | 71.86 |
| Sept. 28 | 336.5 | 70.47 |
| Oct. 5 | 332.7 | 70.71 |
| 12 | 333.8 | 71.51 |
| 19 | 333.0 | 71.60 |

The total volume of all stock sold on the Canadian exchanges in October averaged \$15.4 million per week, compared with \$14.2 million in September and less than \$8 million in July-August.

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 Bond Yields
- Chart 6 - Long-term 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

Selected Canadian Money Market and Related Data

| | <u>6-mo. Treas. bills</u> | | | <u>Canadian dollar</u> | | | <u>Net incentive to hold Can. bills/</u> |
|-------------|---------------------------|----------------|-------------------------|------------------------|----------------------|--------------------------------|--|
| | <u>Canada a/</u> | <u>U.S. b/</u> | <u>Spread over U.S.</u> | <u>Spgt c/</u> | <u>3-mo. forward</u> | <u>discount premium (+) d/</u> | |
| 1960 - High | 5.14 | 4.53 | 1.62 | 105.27 | -- | 0.99 | 1.99 |
| Low | 1.68 | 2.10 | -0.82 | 100.33 | -- | -0.91 | -0.57 |
| 1961 - High | 3.34 | 2.54 | 1.10 | 101.72 | -- | 0.26 | 0.89 |
| Low | 2.26 | 2.17 | -0.09 | 96.75 | -- | -0.56 | -0.20 |
| Sept. 28 | 2.59 | 2.25 | 0.34 | 97.06 | 97.08 | 0.0 | 0.34 |
| Oct. 5 | 2.57 | 2.29 | 0.28 | 97.08 | 97.08 | 0.0 | 0.28 |
| 12 | 2.57 | 2.37 | 0.20 | 97.08 | 97.09 | 0.07 | 0.27 |
| 19 | 2.49 | 2.29 | 0.20 | 97.08 | 97.11 | 0.13 | 0.33 |
| 26 | 2.50 | 2.30 | 0.20 | 97.08 | 97.11 | 0.13 | 0.33 |
| 2 | 2.47 | 2.27 | 0.20 | 96.75 | 96.78 | 0.13 | 0.33 |

a/ Average yield at weekly tender on Thursday.

b/ Composite market yield for the U.S. Treasury bill on Thursday close of business.

c/ In U.S. cents.

d/ Spread between spot rate and 3-month forward Canadian dollar on Thursday closing, expressed as per cent per annum.

e/ Spread over U.S. Treasury bill (column 3), plus 3-month forward discount or premium (column 6).

Selected Government of Canada Security Yields

| | <u>6-mo. Treas. bills</u> | | <u>Intermediate bonds (8 yr.)</u> | | <u>Long-term bonds</u> | | | |
|-------------|---------------------------|----------------------------|-----------------------------------|----------------------------|------------------------|----------------------------|------------------|----------------------------|
| | <u>Canada a/</u> | <u>Spread over U.S. b/</u> | <u>Canada c/</u> | <u>Spread over U.S. d/</u> | <u>(20 year)</u> | | <u>(35 year)</u> | |
| | | | | | <u>Canada e/</u> | <u>Spread over U.S. f/</u> | <u>Canada g/</u> | <u>Spread over U.S. h/</u> |
| 1960 - High | 5.33 | 1.37 | 5.55 | 1.11 | 5.42 | 1.36 | 5.28 | 1.61 |
| Low | 1.99 | -0.86 | 4.09 | 0.21 | 4.63 | 0.85 | 4.68 | 0.95 |
| 1961 - High | 3.63 | 1.15 | 4.75 | 1.16 | 5.19 | 1.40 | 5.23 | 1.59 |
| Low | 2.35 | -0.11 | 4.22 | 0.25 | 4.80 | 0.78 | 4.92 | 1.14 |
| Sept. 27 | 2.89 | 0.21 | 4.41 | 0.47 | 4.95 | 0.91 | 5.00 | 1.24 |
| Oct. 4 | 2.84 | 0.24 | 4.39 | 0.45 | 4.96 | 0.91 | 5.00 | 1.23 |
| 11 | 2.83 | 0.24 | 4.40 | 0.41 | 4.96 | 0.88 | 5.00 | 1.21 |
| 18 | 2.72 | 0.04 | 4.37 | 0.41 | 4.90 | 0.84 | 4.98 | 1.22 |
| 25 | 2.72 | 0.04 | 4.36 | 0.42 | 4.86 | 0.81 | 4.96 | 1.24 |
| Nov. 1 | 2.69 | 0.13 | 4.22 | 0.30 | 4.80 | 0.78 | 4.93 | 1.21 |

a/ Average yield at weekly tender on Thursday.

b/ Spread between Canadian auction rate and composite market yield of U.S. bill on close of business Thursday.

c/ Government of Canada 2-3/4 per cent of June 1967-68.

d/ Spread over U.S. Government 2-1/2 per cent of 1963-68.

e/ Government of Canada 3-1/4 per cent of October 1979.

f/ Spread over U.S. Government 3-1/4 per cent of 1978-83.

g/ Government of Canada 3-3/4 per cent of September 1996 - March 1998.

h/ Spread over U.S. Government of 1995.

**Canada: Changes in Distribution of Holdings of Canadian
Government Direct and Guaranteed Securities**
(millions of Canadian dollars, par value)

| | <u>Bank of Canada</u> | | <u>Government Total</u> | <u>Chartered banks</u> | | <u>General public</u> | | |
|-----------|-------------------------|--------------|-----------------------------|-------------------------|--------------|--------------------------|-------------------------|--------------|
| | <u>Treas. bills</u> | <u>Bonds</u> | | <u>Treas. bills</u> | <u>Bonds</u> | <u>Savings bonds</u> | <u>Treas. bills</u> | <u>Bonds</u> |
| 1961-Jan. | -41 | -38 | +15 | +111 | - 37 | - 2 | - 46 | +23 |
| Feb. | - 7 | -68 | -96 | + 67 | + 88 | - 6 | - 26 | +39 |
| Mar. | -47 | +120 | -25 | - 36 | + 50 | - 18 | + 30 | + 6 |
| April | + 9 | +59 | - 2 | - 70 | - 52 | - 37 | + 64 | -12 |
| May | +17 | -22 | - 1 | + 63 | + 24 | - 33 | - 80 | + 1 |
| June | -74 | +43 | + 5 | + 33 | + 62 | -22 | - 7 | +37 |
| July | +69 | +21 | +16 | + 16 | + 11 | - 23 | - 95 | -37 |
| Aug. | 0 | +21 | +32 | +107 | +148 | - 29 | - 87 | -35 |
| Sept. | +16 | +44 | + 9 | - 58 | + 72 | - 24 | + 40 | +42 |
| Oct. | -105 | +14 | -39 | +109 | + 4 | + 4 | - 3 | -31 |

Source: Bank of Canada, Weekly Financial Statistics.

Selected Canadian Financial Statistics
(in millions of Canadian dollars or per cent)

| | <u>April</u> | <u>May</u> | <u>June</u> | <u>July</u> | <u>Aug.</u> | <u>Sept.</u> | <u>Oct.</u> |
|--------------------------------------|--------------|------------|-------------|-------------|-------------|--------------|-------------|
| 1. Money supply ^{a/} | | | | | | | |
| Currency and deposits | 13,876 | 13,866 | 13,861 | 14,011 | 14,368 | 14,368 | 14,399 |
| Less: Govt. deposits | 253 | 153 | 200 | 179 | 312 | 473 | 312 |
| Equals: privately held | 13,623 | 13,713 | 13,661 | 13,832 | 14,056 | 14,013 | 14,087 |
| Change in period | - 29 | + 90 | - 52 | + 171 | + 224 | - 43 | + 74 |
| 2. General bank loans ^{a/} | 5,207 | 5,224 | 5,252 | 5,269 | 5,367 | 5,378 | 5,499 |
| Change in period | - 2 | + 17 | + 28 | + 17 | + 98 | + 11 | + 121 |
| 3. Total Govt. securities: | 17,780 | 17,695 | 17,763 | 17,739 | 17,885 | 18,061 | 18,018 |
| Of which: Treas. bills | 1,935 | 1,935 | 1,885 | 1,885 | 1,885 | 1,885 | 1,885 |
| Bonds | 12,308 | 12,258 | 12,404 | 12,402 | 12,577 | 12,776 | 12,729 |
| Savings bonds | 3,537 | 3,502 | 3,474 | 3,452 | 3,423 | 3,400 | 3,404 |
| 4. New security issues ^{b/} | 926 | 891 | 725 | 1,086 | 660 | 1,024 | 640 |
| Of which sold in U.S. | 0 | 95 | 11 | 12 | 0 | 0 | 6 |
| 5. Chartered bank liquidity: | | | | | | | |
| Cash reserve | 1,017 | 1,018 | 1,027 | 1,025 | 1,039 | 1,062 | 1,072 |
| Cash ratio | 8.1 | 8.1 | 8.1 | 8.1 | 8.1 | 8.1 | 8.2 |
| Liquid assets | 2,170 | 2,226 | 2,312 | 2,317 | 2,415 | 2,465 | 2,473 |
| Liquid asset ratio | 17.3 | 17.7 | 18.3 | 18.3 | 18.9 | 18.8 | 18.8 |

^{a/} Seasonally adjusted.

^{b/} Source: A. E. Ames & Co., Ltd. (Includes public and private securities.)

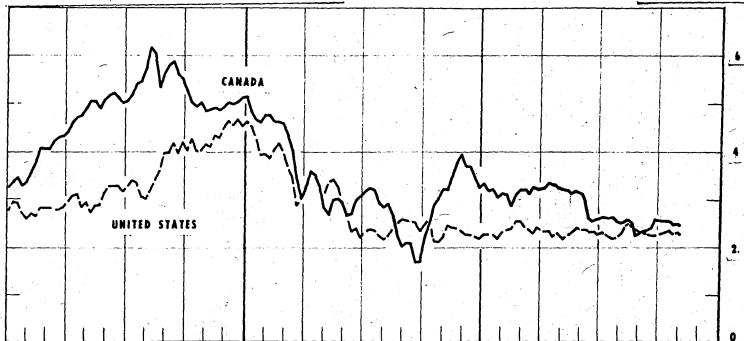
Chart 1

INTEREST ARBITRAGE, UNITED STATES / CANADA

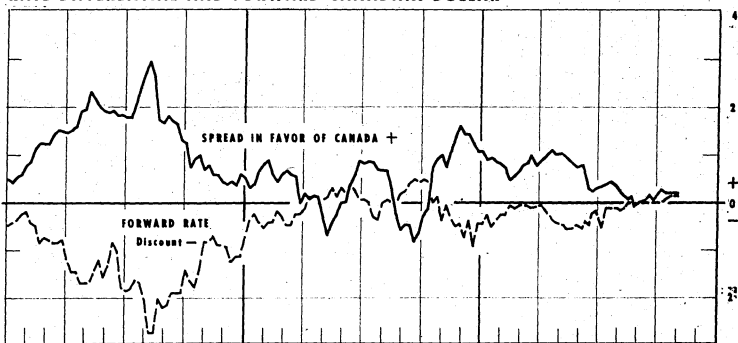
Thursday figures

THREE-MONTH TREASURY BILL RATES

Per cent per annum



RATE DIFFERENTIAL AND FORWARD CANADIAN DOLLAR



RATE DIFFERENTIAL WITH FORWARD EXCHANGE COVER

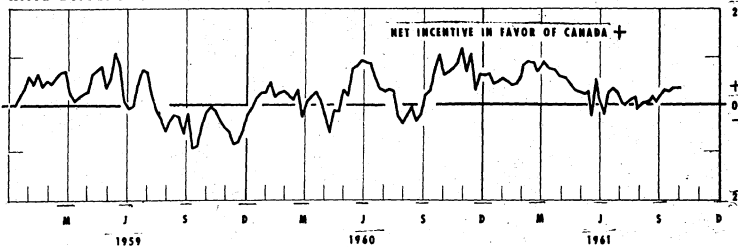


Chart 2

INTEREST ARBITRAGE, NEW YORK / LONDON

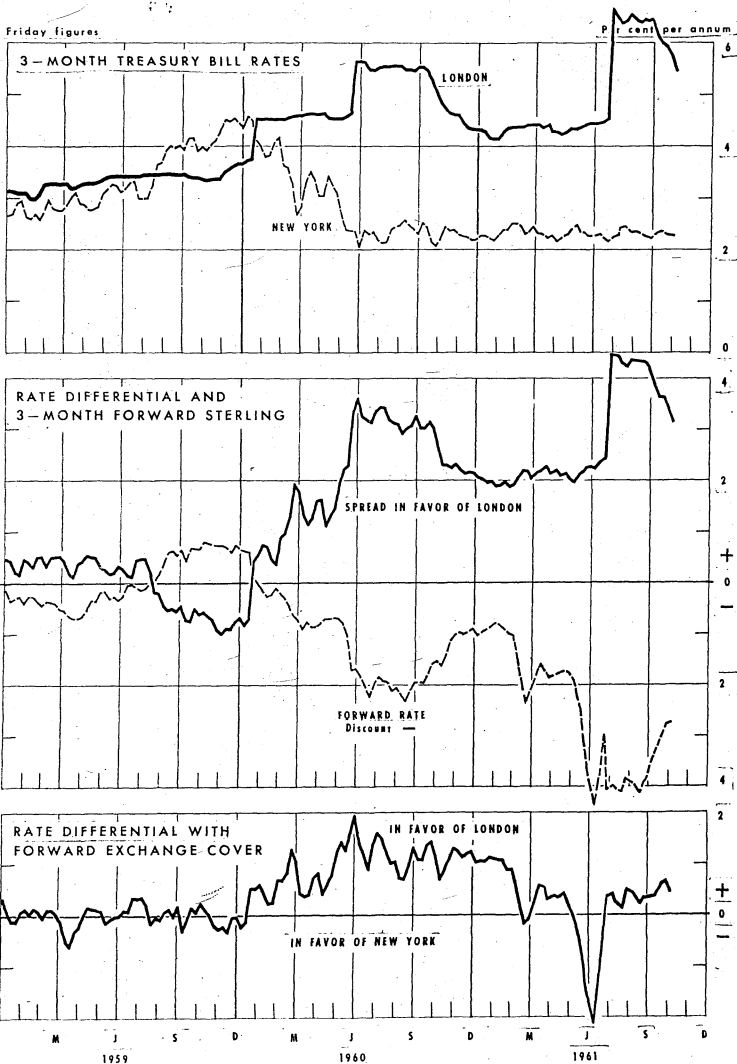


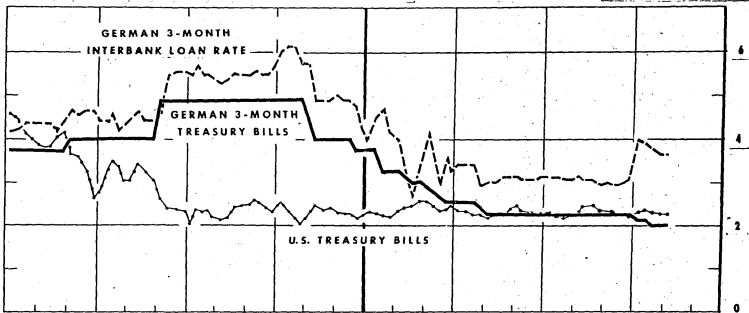
Chart 3

INTEREST ARBITRAGE, NEW YORK / FRANKFURT

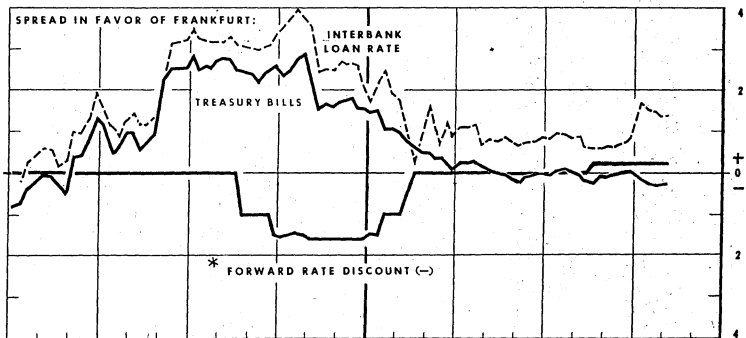
Friday figures

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

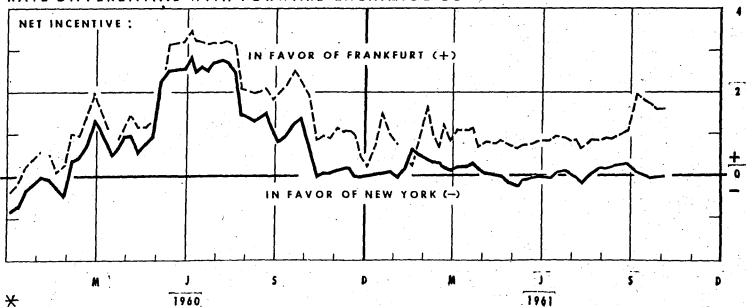
Per cent per annum



RATE DIFFERENTIAL AND FORWARD DEUTSCHE MARK



RATE DIFFERENTIAL WITH FORWARD EXCHANGE COVER



* Special forward dollar rate available to German commercial banks.

Chart 4

INTEREST ARBITRAGE, FRANKFURT/LONDON

Friday figures

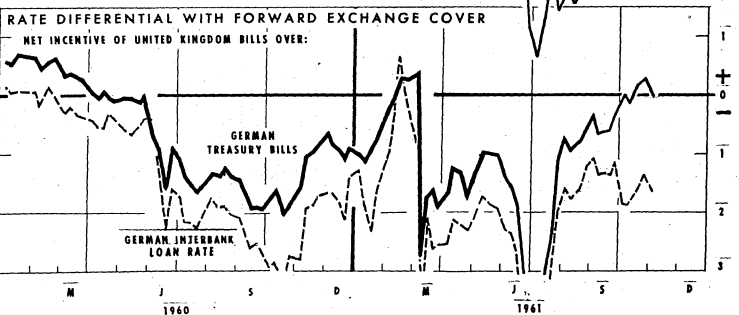
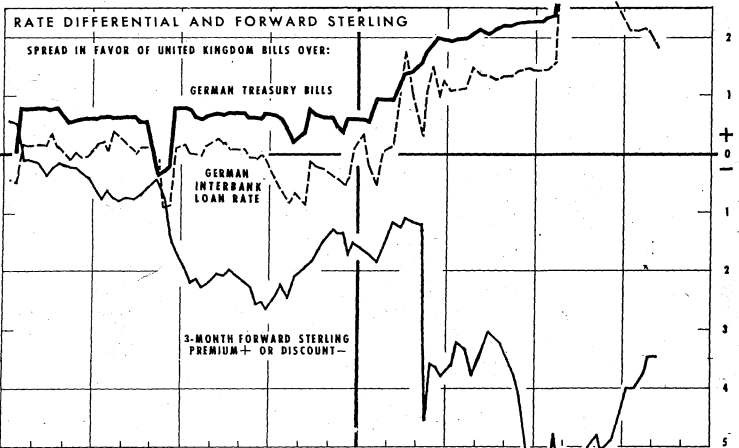
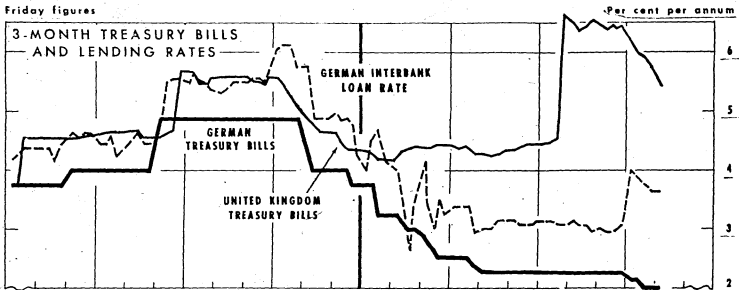
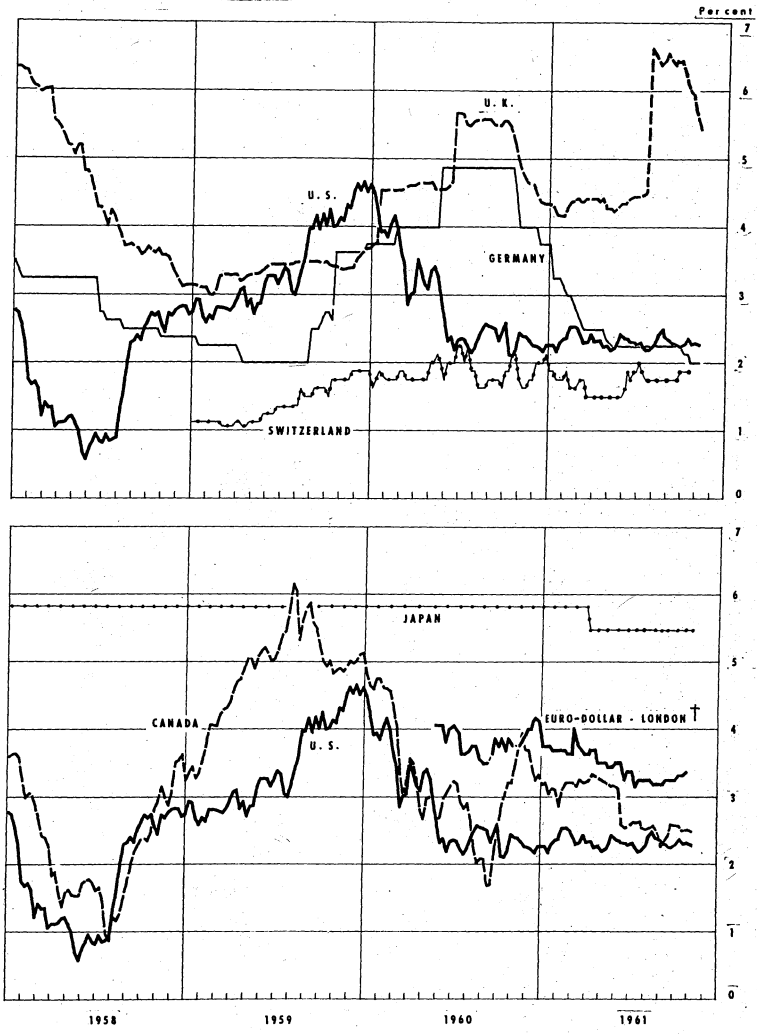


Chart 5

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

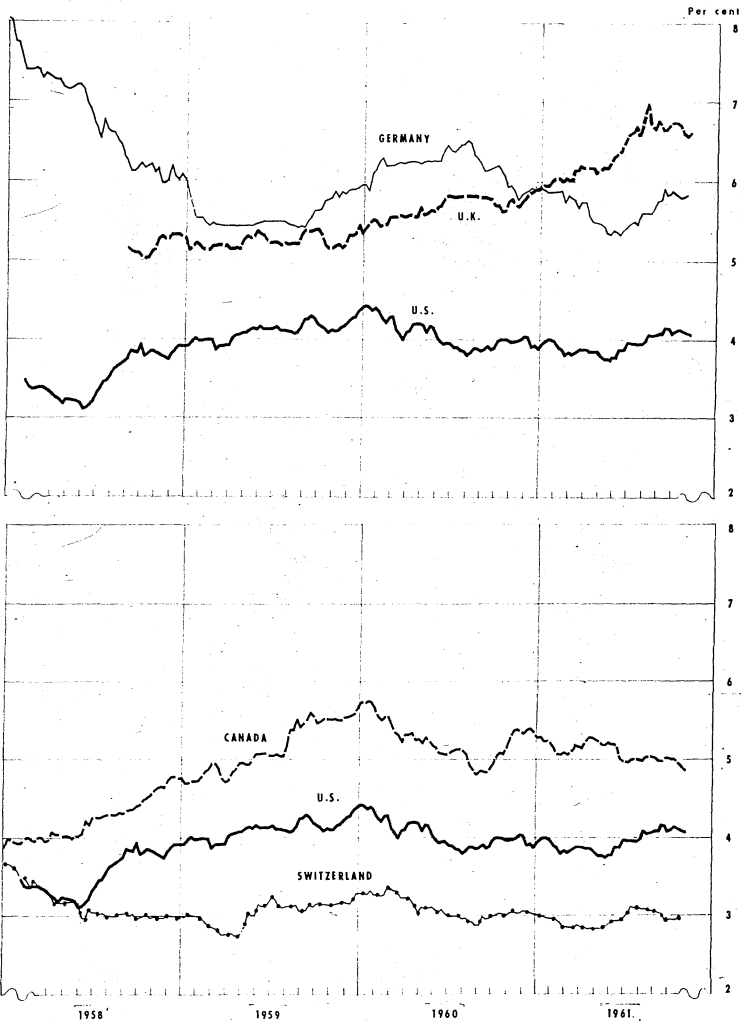
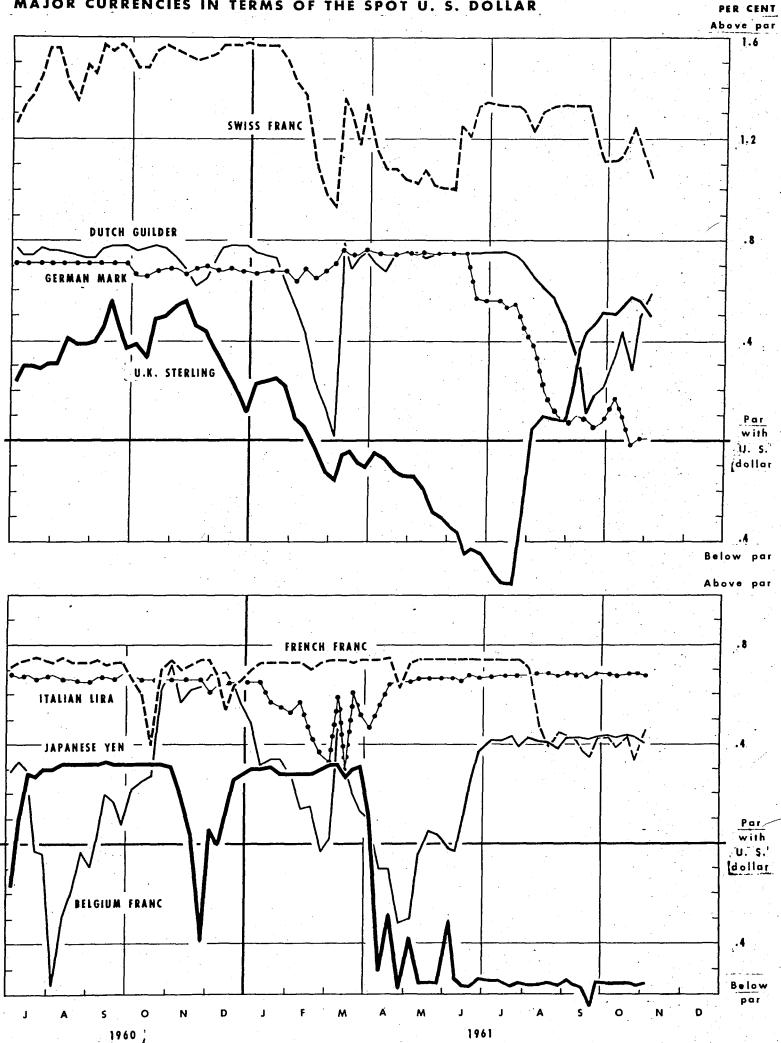


Chart 8

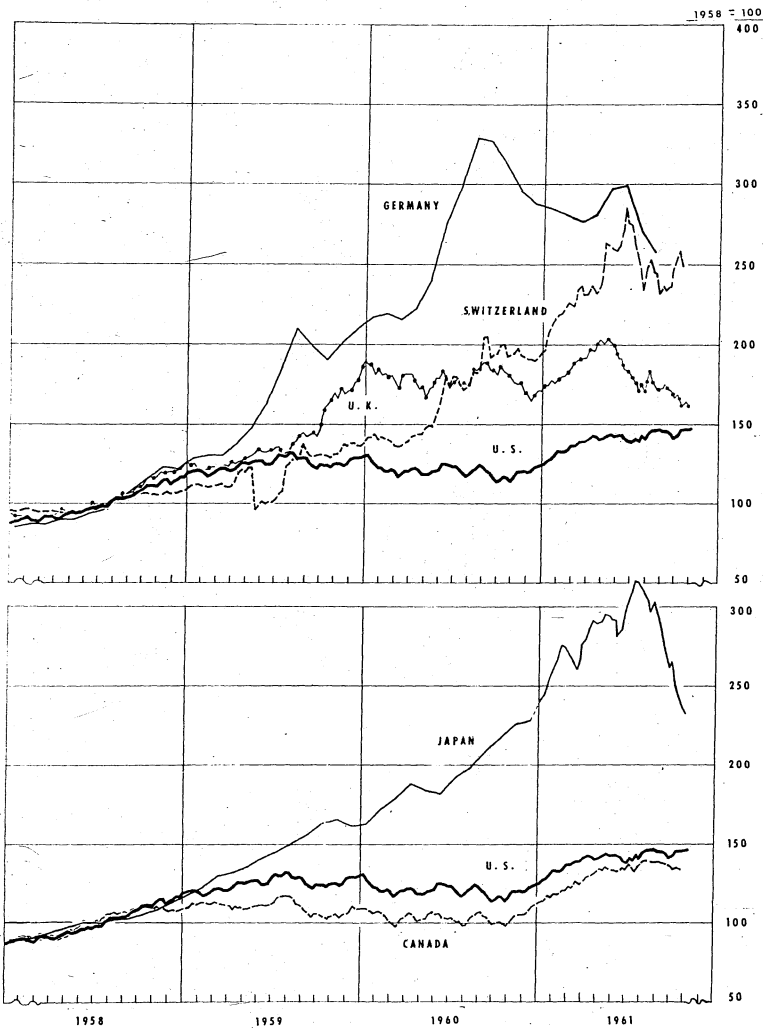
MAJOR CURRENCIES IN TERMS OF THE SPOT U. S. DOLLAR



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Chart 7

INDUSTRIAL STOCK INDICES *



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

Chart 9

3-MONTH FORWARD RATES - LONDON QUOTATIONS

