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CAPITAL MARKET DEVELOPMENTS ABROAD

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

I. Germany: Money and Capital Markets during October

There were substantial shifts of funds both away from, and into, German financial markets during October. In the short-term sector, German commercial banks built up their money-market assets abroad, as the Bundesbank took further steps in October to make the export of short-term funds attractive to them. In the latter part of the month, on the other hand, foreign investors began to return to the German stock market in appreciable volume and the index of stock prices increased from 206 in early October to 230 on November 10.

Short-money rates in Germany continued to decline as the Bundesbank lowered its selling rate for Treasury bills by 1/8 per cent on October 4 and again on October 20. The outflow of commercial bank short-term funds in October may have been as substantial as the repatriation of such funds during September. These funds are reportedly placed in the London money market on an uncovered basis where they can obtain yields close to 6 per cent and in Euro-dollar deposits where three-month money was quoted at 3.31 per cent in London with the Bundesbank providing forward cover at a cost of 0.25 per cent per annum. The Bundesbank is not taking steps to absorb the growth in bank liquidity which took place in September but is following a "defensive" monetary policy of stabilizing the level of liquidity by offsetting unwanted increases or decreases. The active Federal Bank encouragement of money exports by the commercial banks has the effect of reducing money-market liquidity as well as the level of published official reserves.

Conditions improved in the bond market in October. The long-term rate, which had been moving gradually upward since late June, leveled out in October at around 6 per cent. Six per cent coupons on new offerings became more numerous as the month progressed. Activity picked up in late October after several months of comparative inactivity, as an inflow of funds produced a slight rise in bond prices. The rate for fixed-interest securities is now believed to be stabilized, if only temporarily, in the neighborhood of 6 per cent and new offerings at this rate are now expected in the near future.

The effects of the investor reappraisal of the uncertainties about Berlin and the delayed formation of a new Federal Government, which underlay the inflow of funds from abroad, were more evident in the German stock market

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DECONTROLLED AFTER SIX MONTHS

than in the bond market. A sharp and uninterrupted rise in German stock prices occurred during October and early November with renewed domestic and foreign demand for German shares. Continental investors who had sold German shares at last summer's peak levels returned to the market at the lower levels presently prevailing. American investors are also reported to have resumed purchases.

German official reserves fell by \$255 million in October but the decline is thought to reflect primarily the outflow of short-term capital by German banks rather than any reduction in the current account surplus. In September, the seasonally-adjusted trade surplus was above the figure for August and exceeded the monthly average for the second and third quarters.

Money Market. The money market, which had become easy in late September, became increasingly liquid during October. Liquidity increased as a result of the large repatriation of funds by the commercial banks in September, the reflow into Germany of foreign and domestic funds resulting from a reappraisal of the Berlin situation, the effect of the most recent reduction, as of September 28, in reserve requirements, and continued high public expenditures. On several occasions during the month call money rates in the Frankfurt inter-bank money market fell to more than 1 per cent below the Bundesbank discount rate, and 30-day money declined to as low as 2 1/2 per cent. Three-month money, which had been very tight, eased slightly toward the end of the month but at 3 3/4 per cent its rate was only slightly below the 4 per cent average which had prevailed early in October.

Comparatively easy conditions have continued into November. Rates on call money have risen above end-of-October levels but 30-day and 90-day money remain generally at those levels.

Commercial banks were reported to have moved abroad in October amounts equivalent to the large sums brought back to Germany in September. German commercial banks are reported to be making uncovered transfers to London, thus enjoying yields of close to 6 per cent. (See chart 2.) The Bundesbank encouraged the banks to export funds by reducing the rates on its sales of open market paper by 1/8 per cent on October 4 and again on October 20.

Frankfurt Inter-bank Money Rates

	Day-to-day money		One-month	Three-month
	Lowest rate	Highest rate	loans	loans
1961				
July (monthly range)	2.38	3.13	2.88 - 3.00	3.00 - 3.13
August "	1.75	2.88	2.75 - 3.00	2.88 - 3.13
Sept. "	2.25	3.25	2.63 - 3.00	2.75 - 3.13
Oct. (weekly range)	1-8	2.75	2.75 - 3.00	3.75 - 4.25
"	9-15	2.00	2.63 - 3.00	3.63 - 4.25
"	16-23	1.75	2.00 - 2.78	3.50 - 3.88
"	24-31	1.88	2.50 - 2.88	3.50 - 3.88
Nov. "	1-5	2.50	2.50 - 2.75	3.50 - 3.75
"	6-12	2.50	2.63 - 2.75	3.50 - 3.75

The October 20 change in the rates at which the Federal Bank is prepared to sell Treasury bills and short-term bonds in the open market brought the yield on 60-90 day bills to 2.00 per cent and on 6-month Treasury bonds to 2.25 per cent.

<u>From</u>	<u>60-90 days Treasury bills</u>	<u>6-month Treasury bonds</u>
Dec. 20, 1960	3.75	4.00
<u>1961</u>		
Jan. 20	3.25	3.50
Mar. 23	2.50	2.75
Apr. 26	2.38	2.63
May 5	2.25	2.50
Oct. 4	2.13	2.38
Oct. 20	2.00	2.25

As a result of the Federal Bank's actions and market forces making for high liquidity, there was almost no incentive for the commercial banks to hold idle funds at home during October, with the yield on three-month Treasury bills falling to 2.00 per cent and call money rates fluctuating around 1 7/8 per cent. While there was no marked incentive for the German commercial banks to move into U.K. Treasury bills on a covered basis, it is understood that commercial banks were moving uncovered into short-term sterling securities, as well as into London Euro-dollars.

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

	Rate for U.S. dollar		Incentive in favor of London		Rate for U.S. dollar deposits on		Incentive in favor of London
	Day-to-day money in Frankfurt	at call in London	Euro-dollar call rate	3 months money in Frankfurt	3 months basis in London	Euro-dollar 3-month rate	
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	
29	3.13	2.50	-0.63	3.07	3.25	0.18	
Oct. 6	2.88	2.63	-0.25	4.00	3.25	-0.75	
13	2.13	2.50	0.37	3.88	3.31	-0.57	
20	2.00	2.63	0.63	3.75	3.31	-0.44	
27	1.88	2.75	0.87	3.63	3.38	-0.25	
Nov. 3	2.63	2.63	--	3.63	3.31	-0.32	
10	2.69	2.63	-0.06	3.63	3.31	-0.32	

In late October the spread between Treasury bill yields in the United States and Germany on a covered basis shifted slightly to favor the U.S. bill, but so negligibly as to constitute no encouragement to a movement into U.S.

bills, while the Frankfurt three-month inter-bank lending rate maintained its margin of advantage on a covered basis over the U.S. bill rate at more than 1 per cent (see chart 3). A major shift in the relation of German and U.S. short-term rates would, in the absence of any other incentives, be required for any movement of funds to New York, since German commercial banks can earn higher yields by investing in other foreign money markets, particularly London.

	German Inter-bank loan rate vs. U.S. bill rate				Bundesbank's Treasury bill selling rate vs. U.S. bill rate		
	Inter-bank loan rate	U.S. bill rate	Spread over U.S. bill	Net covered incentive of German rate ^{a/}	German 3 mos. bill rate	Spread over U.S. bill	Net covered incentive of German rate ^{a/}
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
29	3.07	2.23	0.84	1.09	2.25	0.02	0.27
Oct. 6	4.00	2.31	1.69	1.94	2.13	-0.18	0.07
13	3.88	2.37	1.51	1.76	2.13	-0.24	0.01
20	3.75	2.30	1.45	1.70	2.00	-0.30	-0.05
27	3.63	2.29	1.34	1.59	2.00	-0.29	-0.04
Nov. 3	3.63	2.28	1.35	1.60	2.00	-0.28	-0.03
10	3.63	2.47	1.16	1.41	2.00	-0.47	-0.22

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

Bond Market. After having been very quiet for several months, the German bond market showed new activity after the middle of October. The long-term rate, which had been moving gradually upward since late June, levelled out during October, with the yield on long-term bonds averaging around 6 per cent. (See Chart 5). German financial observers now believe that the long-term rate has stabilized at this level, at least for the time being, and expect prospective government offerings, possibly of the Federal Railroads and the Federal Post Office, and offerings of industrial corporations to carry a six per cent coupon. While borrowers in the German capital market have begun to offer the 6 per cent. coupon rate, the renewed inflow of funds into German markets in late October produced a slight fall in yields.

Mortgage bond activity was above recent levels and municipal bonds, especially those with tax incentive provisions, continued to sell well in October after the September rise in activity in such bonds. Of the mortgage and municipal bonds issued in September, 59 per cent carried a 6 per cent yield, and in October a larger percentage of such bonds has been issued at 6 per cent. In

August, only 16 per cent of the total mortgage and municipal bonds issued carried a rate as high as 6 per cent.

Six-per cent public and industrial bonds, which had been quoted at an average of around 98-99 at the end of September, moved up to a level of 100-101 late in October. There were roughly similar increases in the prices of 5 1/2 per cent bonds. German market circles now expect continued activity in the market that has had only one large placing in almost five months, a 5 per cent loan of the Federal Railroads which was offered in early July and was then only partly subscribed.

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
	August	5.9	6.0	5.9
	September	6.0	6.3	6.0

Stock Market. Beginning in late October, the German stock market showed strength after several weeks of low activity. (See Chart 6). Observers ascribed the rally in German stock prices to investor assumptions that the tensions over Berlin were "bearable" and not likely to depress German economic activity, and to the November 4 agreement on a new Adenauer government, after almost seven weeks of debate. It was reported that both foreign and domestic demand increased noticeably. Foreign investors who had sold at the higher price levels which had prevailed before the Berlin situation became more serious in mid-August were returning to the German market. These foreign investors reportedly had kept themselves liquid, and the opportunity to buy back into the German share market at lower price levels was an important factor in their return. The improvement that resulted from the combined foreign and domestic demand has since continued uninterruptedly. Americans were contributing to the foreign demand for German shares, according to market reports of November 10.

German market observers are crediting the German Government for the continuing increase in the number of domestic holders of German shares. The Bonn government has been sponsoring programs whereby citizens of limited incomes can purchase low-cost shares in de-nationalized companies. These programs, along with company sponsored incentive-share-buying programs for employees, have enlarged the German investing public. Many investors have

also gone into recently-established mutual funds, in some cases because individual German share prices are beyond their means. Installment buying of fund shares is a further recent innovation in Germany which is helping to increase the number of domestic share holders.

Frankfurter Allgemeine Zeitung Total Index of Share Prices
(12/31/58 = 100)

<u>1961</u>	July 31	223.80
	Aug. 31	203.38
	Sept. 29	205.03
	Oct. 6	205.91
	" 13	206.35
	" 31	219.36
	Nov. 3	221.65
	" 10	229.99

Foreign Trade. Monthly averages of seasonally adjusted West German trade figures for the periods indicated are as shown below.

	<u>Exports</u>	<u>Imports</u>	<u>Trade balance</u>
	(in millions of U.S. dollars)		
1960	948	844	104
1961 - I	1,047	852	195
- II	1,077	936	141
- III	1,060	911	151
July	1,108	955	153
August	1,005	870	135
September	1,068	909	159

German Gold and Foreign Exchange Reserves in 1961
(in millions of dollars)

	<u>Official gross reserves</u>	<u>Commercial bank holdings abroad</u>	<u>Total</u>	<u>Change from Previous Month</u>		
				<u>Official</u>	<u>Com'l. Bank</u>	<u>Total</u>
Jan.	7,483	653	8,136	-137	+340	+203
Feb.	7,491	740	8,231	+ 8	+ 87	+ 95
Mar.	7,920	792	8,712	+429	+ 52	+481
Apr.	7,476 ^{1/}	944	8,420	-444	+152	-292
May	7,507	1,080	8,587	+ 31	+136	+167
June	7,638	1,196	8,834	+131	+116	+247
July	7,532	1,311	8,843	-106	+115	+ 9
Aug.	7,059	1,359	8,418	-473	+ 48	-425
Sept.	7,068	1,109	8,177	+ 9	-250	-241
Oct.	6,813	n.a.	xxx	-255	n.a.	xxx

^{1/} After special debt prepayment of \$776 million to U.S. and U.K.

Foreign Exchange. On the foreign exchange market, most major currencies remained firm against the deutschemark throughout October and during the first three weeks of November. On October 20, for the first time since the revaluation of the mark last March, the spot dollar reached the parity rate of DM 4.00 per dollar. Since that date, the dollar has remained at or above parity with only slight and infrequent declines below the parity rate. Spot sterling, which had exceeded parity earlier than the dollar, has remained above the parity rate of DM 11.25 for the past several weeks. The discount on three-month sterling has continued to decline and has been below 4.00 per cent per annum since October 20. A covered movement of German bank funds into U.K. bills remains unprofitable, but some uncovered movement into such obligations has been reported, in addition to movements into the London Euro-dollar market.

The present lower rate of the deutschemark does not result from a weakening in the German basic balance of payments, which continues to show an undiminished surplus. The movement of the dollar-DM rate in favor of the dollar is, according to Frankfurt banking circles, a consequence partly of the large export of funds by the commercial banks and partly of the utilization by certain foreign countries of IMF drawings in deutschemarks. The return to a more normal "leads and lags" situation in current trade is also a cause of the strength of other currencies, following earlier speculation against some other currencies, notably sterling.

DM-Dollar middle rate par (DM 4.00 = \$1)

Sept. 15	3.9978
29	3.9922
Oct. 6	3.9928
13	3.9952
20	4.0000
23	4.0008
31	3.9968
Nov. 3	3.9992
10	4.0037

II. Eight 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 - Short-term Bond Yields
- Chart 5 - Long-term Yields
- Chart 6 - Industrial Stock Indices
- Chart 7 - Major Currencies in Terms of Spot
United States Dollar
- Chart 8 - 3-month Forward Rate--London Quotations

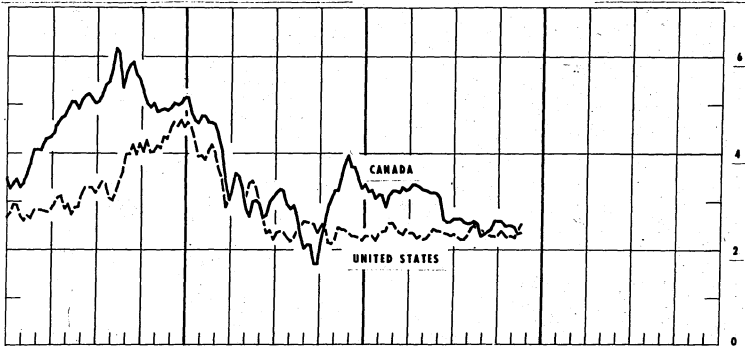
Chart 1

INTEREST ARBITRAGE, UNITED STATES / CANADA

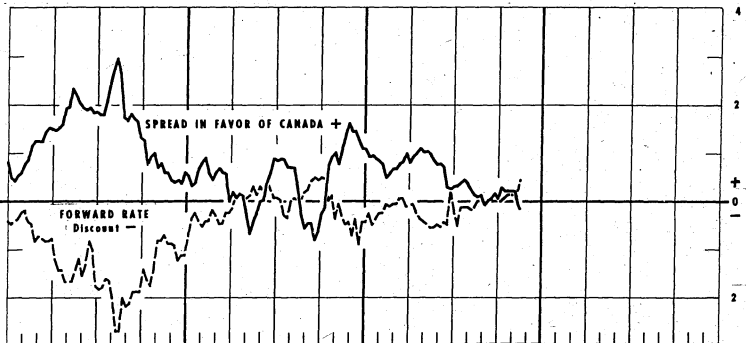
Thursday figures

THREE-MONTH TREASURY BILL RATES

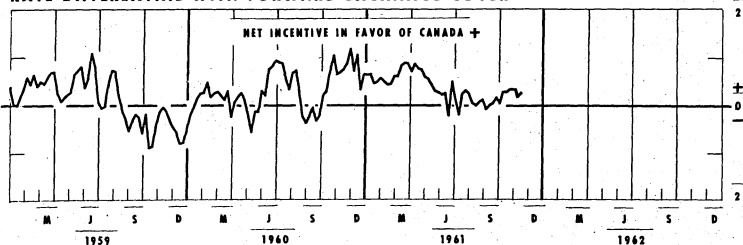
Per cent per annum



RATE DIFFERENTIAL AND FORWARD CANADIAN DOLLAR

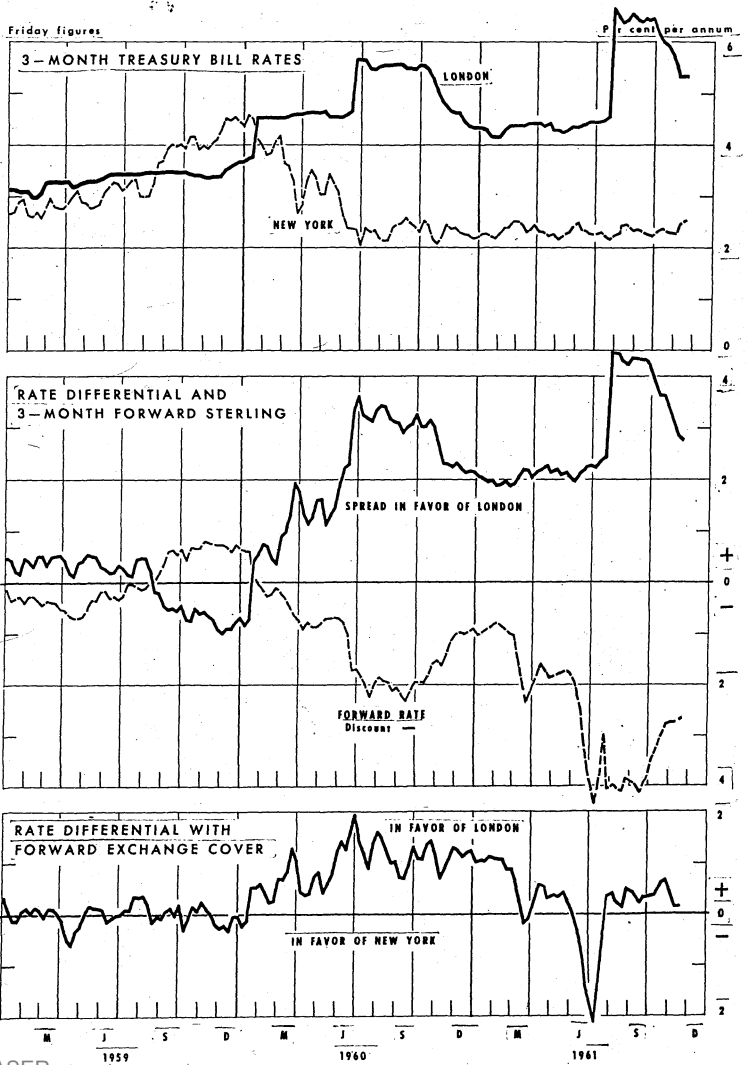


RATE DIFFERENTIAL WITH FORWARD EXCHANGE COVER



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Chart 2
INTEREST ARBITRAGE, NEW YORK / LONDON

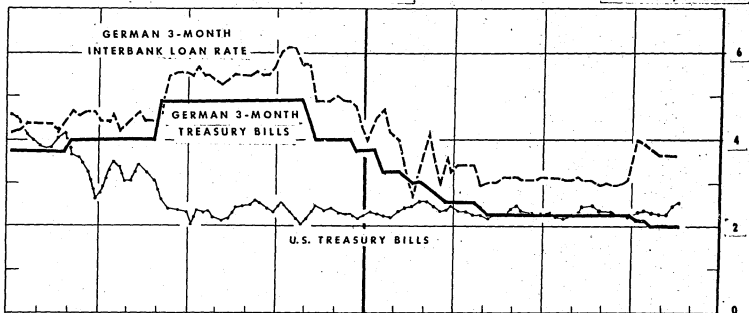


INTEREST ARBITRAGE FOR GERMAN COMMERCIAL BANKS

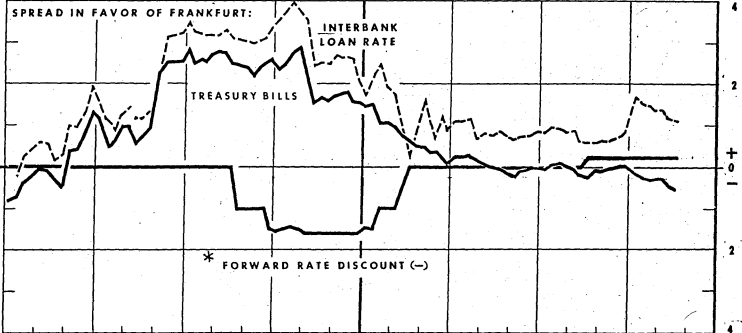
Friday figures

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

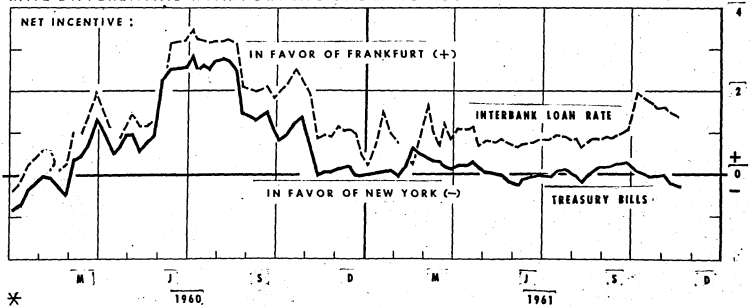
Per cent per annum



RATE DIFFERENTIAL AND FORWARD DEUTSCHE MARK

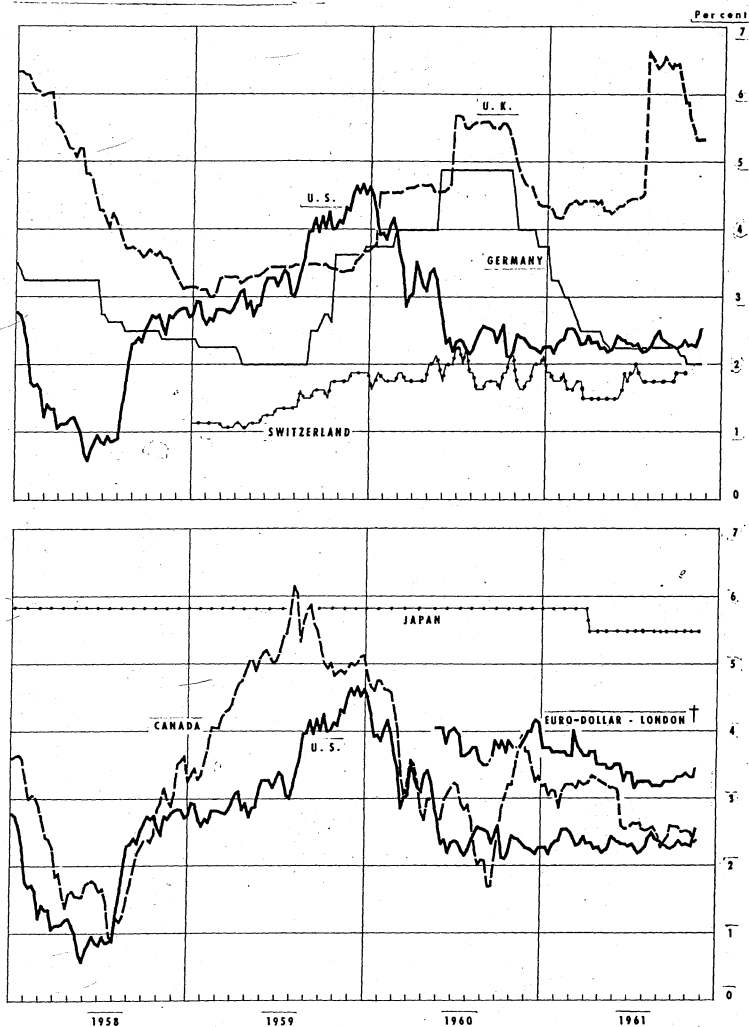


RATE DIFFERENTIAL WITH FORWARD EXCHANGE COVER



* Special forward dollar rate available to German commercial banks.

SHORT-TERM INTEREST RATES *

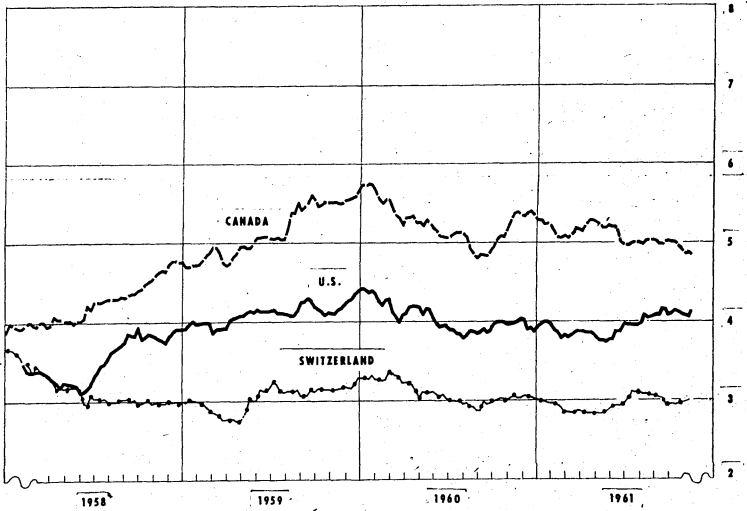
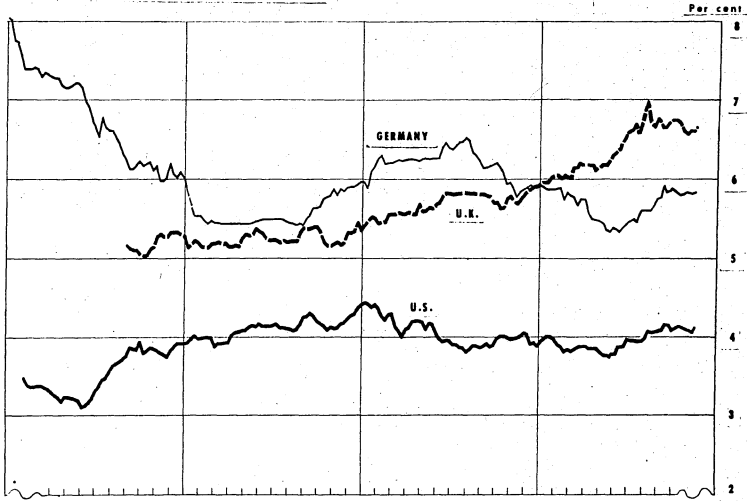


* 3-month treasury bill rates for all countries except Japan (3-month interbank deposit rate) and Switzerland (3-month deposit rate).

† 3-month rate for U. S. dollar deposits in London.

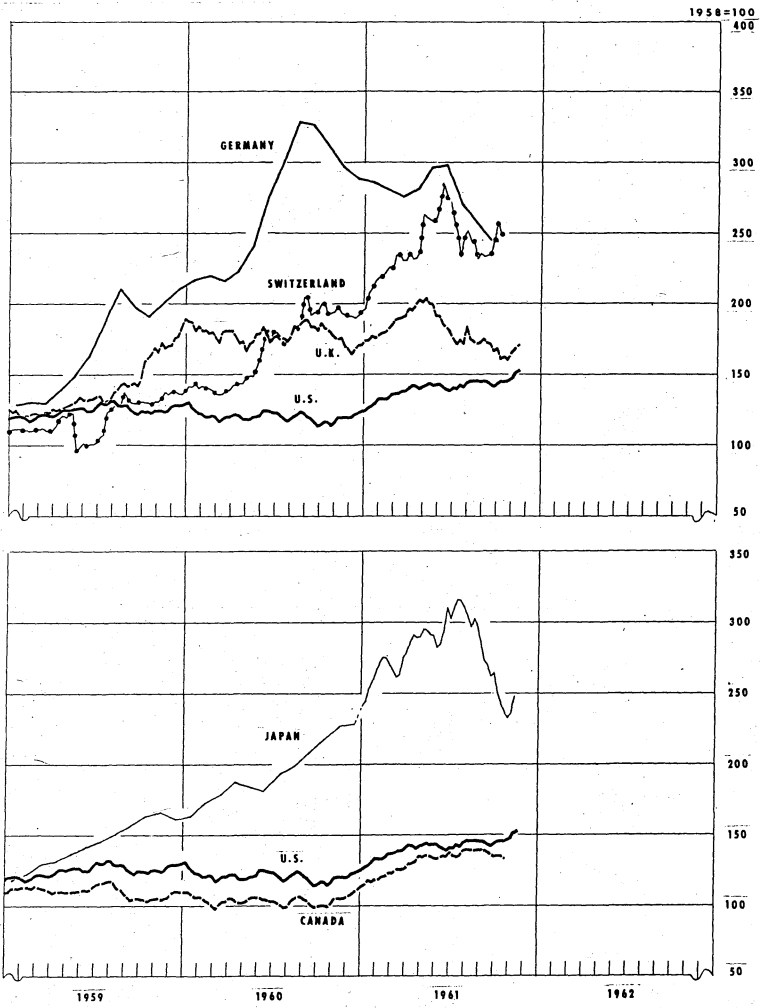
Chart 5

LONG-TERM BOND YIELDS



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Chart 6
INDUSTRIAL STOCK INDICES*



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

Chart 7
MAJOR CURRENCIES IN TERMS OF THE SPOT U. S. DOLLAR

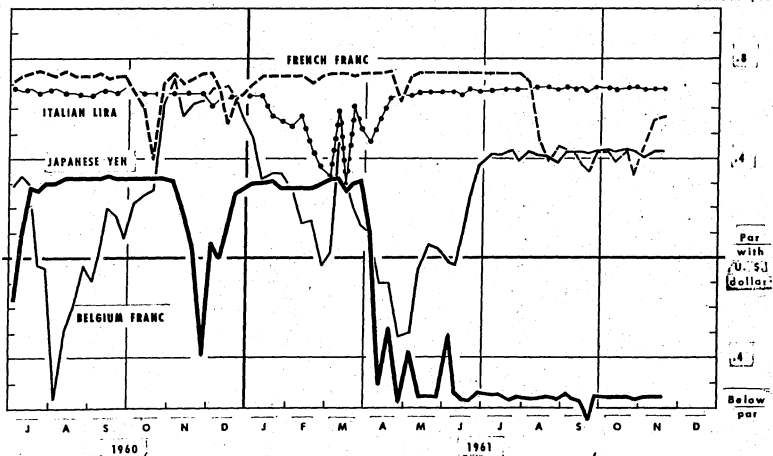
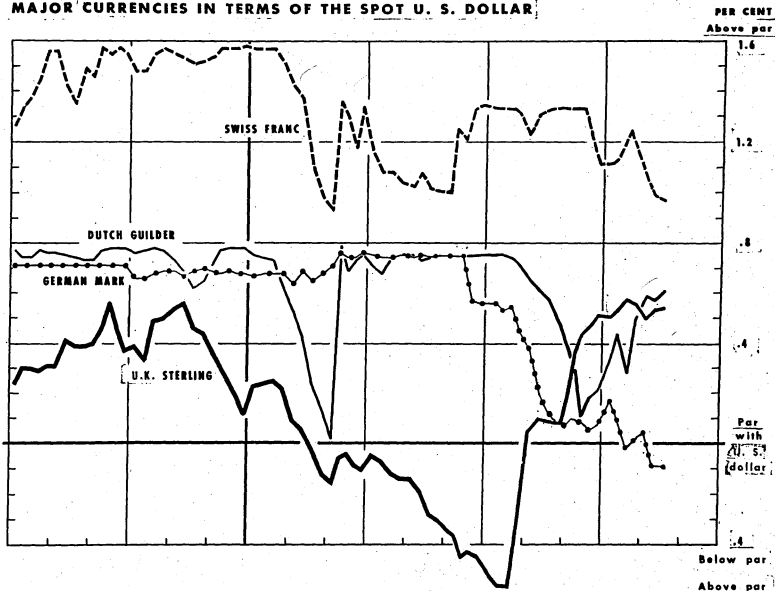


Chart 8

3-MONTH FORWARD RATES - LONDON QUOTATIONS

