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CAPITAL MARKET DEVELOPMENTS ABROAD

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I. Switzerland: Money and Capital Markets in February

The Swiss franc weakened continuously throughout February and early March. In mid-March the Swiss National Bank intervened momentarily with support purchases to slow down the decline. The spot dollar in Switzerland rose from SF 4.317 at the end of January to SF 4.343 on March 15, its highest level since November 1959. It was quoted at SF 4.342 on March 20, and fell to SF 4.337 on March 21. The premium on the forward Swiss franc (discount on the forward dollar) was generally higher in February and March, when the spot rate was declining, than it had been in January. (See Table.)

Two factors were responsible for the unexpected selling pressures on the franc. First, heavy imports in January and February widened the Swiss trade gap. The import surplus exceeded $100 million a month in January and may have reached this figure in February (according to a press estimate) compared with an average monthly trade deficit of $55 million in 1961. Rising imports, a widened trade deficit, and rising prices in Switzerland have induced the Government and the National Bank to discuss with the banks, industry, commerce, and trade unions a program to place restraints on investment expenditures and credit expansion. According to press reports, those proposals have not yet been worked out because of technical problems and some objections from business circles.

Second, a heavier outflow of short-term funds (and a reduced inflow) have contributed to the exchange-rate movements. The premium on the 3-month forward Swiss franc widened from 0.53 per cent per annum on January 5 to 0.99 per cent on February 2, declined to 0.69 per cent on February 16, and then increased in late February to 1.09 per cent on March 2. (See Table.) The widened premium in late January and again in late February may have reflected shifts of Swiss funds to the Euro-dollar market in London with the exchange risk covered. Such a shift would have required spot sales of Swiss francs and forward sales of dollars against francs; the effects of these two operations would have been to widen the premium on the forward franc.

In addition to the widened trade deficit, the recent deterioration in the Swiss balance of payments also reflects sizeable lending abroad by Switzerland. Short-term funds have been moving to London, and long-term foreign borrowing on the Swiss capital market in January and February was heavier than in most periods of 1961. In addition, the Swiss Confederation Treasury appears to have acquired as much as $100 million in short-term foreign assets since the middle of last October.

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DECONTROLLED AFTER SIX MONTHS

Official reserves of the Swiss National Bank decreased $35 million in February and $23 million in the first half of March. These declines occurred mostly as a result of increases in the short-term foreign assets of the Swiss Federal Government, and to no extent reflected Swiss National Bank sales of foreign exchange to the market.

The short-term money market eased in early February, but subsequently tightened in late February and early March in response to greater demand for internal purposes as well as to the large volume of payments for imports and short-term international capital flows.

Long-term bond yields were virtually unchanged during the period under review. On the stock market, industrial stock prices moved up in February and March to a record high level. New issue activity continued in large volume in February. It appears that for the time being the Swiss authorities have decided to continue the policy of allowing foreign borrowers to enjoy access to the Swiss capital market on a large scale. Foreign public security issues in Switzerland in January and February totaled $51 million.

In its annual report for 1961, the Swiss National Bank reported that a heavy inflow of foreign funds resulted in easy credit conditions in Swiss financial markets and, despite a record trade deficit and record long-term capital outflow, large accruals of official reserves. The Swiss authorities took a number of steps to neutralize the inflows:

a. Most of the addition to commercial bank reserves was blocked;
b. Other direct measures taken in late 1960 to sop up bank liquidity were continued;
c. Fiscal policy was contractionary;
d. Both long-term and short-term capital outflows were encouraged.

In addition, to discourage capital inflows there was a renewal of the "Gentlemen's Agreement" with the banks which places unattractive terms on "hot money" investments in Switzerland. Despite these efforts, the Swiss authorities were not entirely successful in preventing foreign exchange accruals from feeding a very strong internal demand for funds, and, in the words of the Bank, the internal economy was characterized by "cyclical overheating."

The year was also marked by Swiss participation in several cooperative arrangements in the international finance field. The German and Dutch revaluations of March 1961 gave rise to an extremely heavy foreign exchange inflow into Switzerland, and weakened the position of sterling. Under the "Basle agreements," Switzerland extended large-scale, short-term assistance to the United Kingdom. One form taken by this assistance was a $200 million advance from the Swiss National Bank to the Bank of England. All of the advance was repaid by the end of 1961 except for the last installment of $50 million, which toward the end of December was converted into a 3-year loan of SF 215 million to the British Government. Another form of this assistance was about $40 million of swaps of gold for sterling, to be reversed in two or three months. The Bank adds that, to help the U.S. dollar at the same time, Switzerland abstained from converting this foreign exchange into gold "at a time when the United States had just overcome a crisis of confidence."

Later in the year the Swiss National Bank cooperated with the U.S. Treasury in reducing the discount on the forward dollar in Switzerland in order to remove an obstacle to flows of short-term funds out of Switzerland. The report reveals that in 1961 the Swiss National Bank bought about $150 million of forward dollars for the account of the Federal Reserve Bank of New York acting as agent for the U.S. Treasury. The Bank observes that "To this extent the National Bank was relieved of the dollars it would otherwise have had to take over. On the other hand, the United States was spared the corresponding gold losses which would have arisen from the conversion of dollars into gold."

Money market. The short-term money market continued to ease in early February. Freely-utilizable balances with the National Bank increased from $505 million at the end of January to $555 million on February 15, and rates paid on 3-month bank deposits dropped from 2-1/8 per cent on January 31 to 1-7/8 to 2 per cent on February 16. (See Table and Chart 5.) Late in February and in early March, however, the money market tightened. Funds were in demand for commercial needs, for payments for imports, and for making short-term investments abroad. With a slowing-up of capital inflows from abroad, by March 7 freely-utilizable balances with the National Bank had declined to $490 million and 3-month deposit rates reportedly stiffened to around 2 per cent.

Bond market. Long-term bond yields rose very slightly in early February and then remained virtually unchanged in the rest of the month and in early March. The yield to maturity on the Swiss Confederation 3 per cent bond of 1967-74, which had fluctuated between 2.97 and 3.02 per cent since the start of the year, was stable at 2.99 per cent in the four weeks ending March 9. (See Table and Chart 6.) Yields on medium-term deposit certificates were unchanged between mid-January and mid-February.

Stock market. In the first sharp advance of 1961, industrial stock prices moved up 3.7 per cent in the first two weeks of February, with all large industrial groups participating in the rise. Following a period when prices changed little, the industrial index rose a further 3.5 per cent in the week ending March 9, and reached a new all-time high. (See Chart 7.) The volume of trading was heavy. In commenting on the sharpness of the price advances in that week, analysts stated that "the extreme thinness in the supply of Swiss issues" makes for sharp price rises when demand for stocks increases.

New issues. New public issues of Swiss securities and foreign bonds on the Swiss market in January totaled $39.3 million, equal to the average monthly level in the second, third and fourth quarters of 1961. (See Table.) In February the volume of new issues was reported to be very heavy but demand was maintained and all flotations were successful. The Bowater Paper Corporation, Ltd. of London floated $13.95 million of 4.5 per cent, 15-year bonds at par in early February, and this issue was oversubscribed 13 times according to the financial press. It was being traded at about 110 on March 12. A $13.95 million offering at par of 4-1/2 per cent, 15-year Kingdom on Denmark bonds at the end of February was also oversubscribed.

Foreign Borrowings in January-February

	Amount (mil. $)	Term	Coupon rate	Issue price	Yield to maturity
January					
IBRD	23.2	1970-73	4.0	100	4.0
February					
Bowater Paper Corp. Ltd. (London)	13.95	1970-77	4.5	100	4.5
Kingdom of Denmark	13.95	1977	4.5	100	4.5

Apparently the Swiss authorities have decided to continue, at least for the time being, the policy of allowing a heavy volume of foreign loan issues on the Swiss market. Press reports last December indicated that the Swiss Finance Ministry desired a reduction in foreign borrowing in Switzerland because it feared continued heavy borrowing would drive up interest rates. However, foreign loans in January and February came to $51 million, an amount well in excess of the average monthly level in 1961 ($19 million) and equal to the exceptionally high average monthly level of the first quarter of last year.

For the month of March, loans by Cinzano, Ltd. of Montreal for $2 million and by Rheinkraftwerk Saeckinger of West Germany for $7 million were expected. Recent British press reports state that Anglo-American Corporation of South Africa may float a loan soon, and that other loans, probably for $14 million each, are being prepared by the Mannesman and Thyssen firms in Germany, I.C.I. of Great Britain, and International Standard Electric of the United States.

Balance of payments. The Neue Zuercher Zeitung, a leading Swiss newspaper, estimates that in 1961 Switzerland incurred a current-account balance-of-payments deficit of between $140 and $163 million, in contrast to a current-account surplus of $95 million in 1960. The change was caused by a rise in the trade deficit (imports on a c.i.f. basis) from $353 million to $656 million which was only partly offset by an increase (from $448 million to approximately $500 million) in the surplus on current invisibles. In 1961, imports were up 21 per cent and exports up 8.5 per cent over 1960. Other Swiss payments to foreigners in 1961 included $223 million of foreign long-term public loans on the Swiss capital market, and loans by the Swiss Federal Government of $50 million to the United Kingdom and $11.6 million to the IBRD. Despite these payments, the Swiss National Bank's gold and foreign exchange reserves rose $436 million in 1961. Thus, all other transactions produced a net capital inflow of $861-884 million.

Foreign trade. The trade deficit became much wider in January. Seasonally-adjusted imports of $273 million in January were nearly 18 per cent above the average for the fourth quarter of 1961. Exports were up only slightly. The seasonally adjusted deficit was $94 million for the month compared with averages of $58 million in the last quarter of 1961 and $55 million in 1961 as a whole. On an unadjusted basis the January deficit was $104 million. A press report indicates that the unadjusted deficit may have been as large in February as in January.

Seasonally-adjusted Foreign Trade
($ millions, monthly average or month)

	1960	1961 by quarters				1962
	Year	I	II	III	IV	Jan.
Imports c.i.f.	187	221	217	229	232	273
Exports f.o.b.	158	166	168	171	174	179
Balance	-29	-55	-49	-58	-58	-94

Foreign exchange reserves. The $41 million decline in the Swiss National Bank's gold and foreign exchange reserves in the first week of February was caused by an increase in the short-term foreign investments of the Swiss Federal Government, and not as a result of exchange-market transactions. Reserves rose $6 million during the remainder of February, but decreased $11.5 million in the first week of March as a result of a further addition to the Confederation's short-term investments abroad, and by about $12 million in the second week. These declines in official reserves did not reflect any sales of foreign exchange to the market.

Swiss National Bank Reserves
($ millions)

	Gold	Foreign exchange	Total
1960 - Dec. 31	2,185	137	2,322
1961 - Feb. 28	2,162	138	2,300
Mar. 31	2,165	372	2,538
Sept. 23	2,453	327	2,780
Dec. 30	2,560	198	2,758
1962 - Jan. 31	2,505	181	2,686
Feb. 7	2,482	163	2,645
Feb. 28	2,482	169	2,651
Mar. 7	2,465	174	2,639
Mar. 15	2,457	171	2,628

In the autumn of 1961, declines in National Bank reserves in late October and early November totaling $58 million were attributed primarily to short-term foreign investments by the Swiss Confederation. Assuming that those investments are still outstanding or have been renewed, it would appear that since mid-October of 1961 the Swiss Federal Government has increased its short-term investments abroad by something like $100 million. If that is in fact the case, it accounts for most of the $128 million decline in National Bank reserves between October 14, 1961, and March 7, 1962.

Foreign exchange rates. The Swiss franc weakened continuously throughout February and the first half of March. The spot dollar rate in Switzerland rose from SF 4.317 on January 27 to SF 4.343 on March 15, the highest since November 1959, while the spot pound rose from SF 12.137 on January 27 to SF 12.21 on March 10. (See Table and Chart 8.)

Commercial demand, growing out of the trade deficit, was one reason for the weakening of the Swiss franc. Imports had increased markedly in January, resulting in a trade deficit of $104 million for the month, about double the 1961 average, and are reported to have continued to run at very high levels in February and early March.

In addition, pressures on the spot rate developed in late February because of increased outflows of short-term funds. Swiss funds apparently moved to London where Euro-dollar deposits yielded a return in Swiss francs of between 2.47 and 2.75 per cent compared with the equivalent return of between 1.60 and 1.86 per cent on U.S. Treasury bills. (See Table.) The appreciable rise in the premium on the Swiss franc after mid-February may have reflected purchases of spot dollars covered by sales of forward dollars on Euro-dollar and similar foreign investments. The Swiss may also have put funds directly into the local-authority market and into deposits with hire-purchase houses in London where the covered yield slightly exceeded the Euro-dollar deposit rate in late February and where the uncovered yield (with an open exchange risk) was appreciably higher.

The high forward premium also attracted dollar and sterling funds into Switzerland. Even though foreign residents are limited to only a few types of short-term assets in Switzerland, market reports state that foreigners brought funds in to obtain the small running yield current in Swiss markets together with the 1 per cent premium on the 3-month forward Swiss franc.

The price of the Swiss "Vreneli" gold coin, which had moved up in December and January, dropped from SF 37.25 on January 26 to SF 36.25 on February 16 simultaneously with declines in gold prices in London and Paris. The "Vreneli" was reportedly traded at SF 36 to 36.20 on March 10.

Europe and British Commonwealth Section.

II. Nine Charts on Financial Markets Abroad

Switzerland: Money Rates, Exchange Rates, and Gold Price

	Forward Swiss franc (3-mo.)	US Tr. bill: Bill yield	US Tr. bill: Net return in SF	Euro-dollar deposit: London rate	Euro-dollar deposit: Net return in SF	Swiss bank deposit (3-mo.)	Exchange rates: Spot $ in SF	Exchange rates: Spot £ in SF	Gold coin a/ in SF
1961-Dec. 1	+0.60	2.55	1.95	3.63	3.03	2.38	4.317	12.139	36.50
8	+0.59	2.58	1.99	3.81	3.22	2.38	4.316	12.131	36.75
15	+0.46	2.61	2.15	3.75	3.29	2.25	4.315	12.125	36.75
22	+0.38	2.60	2.22	3.88	3.50	2.25	4.315	12.110	36.75
29	+0.51	2.66	2.15	3.88	3.37	2.25	4.316	12.118	37.00
1962-Jan. 5	+0.53	2.72	2.19	3.63	3.10	2.13	4.319	12.136	37.25
12	+0.76	2.78	2.02	3.56	2.80	2.13	4.318	12.135	37.25
19	+0.85	2.71	1.86	3.56	2.71	2.13	4.317	12.137	37.25
26	+0.88	2.67	1.79	3.56	2.68	2.13	4.317	12.137	37.25
Feb. 2	+0.99	2.67	1.68	3.50	2.51	2.13	4.318	12.143	36.75
9	+0.76	2.72	1.96	3.56	2.80	2.06	4.323	12.164	36.25
16	+0.69	2.83	2.14	3.44	2.75	1.94	4.327	12.181	36.25
23	+0.83	2.69	1.86	3.56	2.73		4.333	n.a.	
Mar. 2	+1.09	2.69	1.60	3.56	2.47		4.336	12.208	
9	+0.94	2.76	1.82	3.69	2.75		4.337	12.210	
16	+1.00	2.72	1.72	3.69	2.69		4.342		

a/ "Vreneli" 20-franc piece (0.1867 troy ounces; $6.53 at $35 per ounce).

Switzerland: Selected Capital Market Statistics

Capital market yields

	Long-term govt. bonds	Deposit cert's: 12 cantonal banks	Deposit cert's: 5 large banks
1961			
High	3.12	3.34	3.34
Low	2.83	3.29	3.25
Dec. 8	3.01	3.34	3.27
15	2.98	3.34	3.27
22	3.00	3.34	3.27
29	3.00	3.34	3.27
1962			
Jan. 5	3.00	3.34	3.27
12	2.99	3.35	3.29
19	3.02	3.35	3.29
26	2.98	3.35	3.29
Feb. 2	2.97	3.35	3.29
9	2.98	3.35	3.29
16	2.99	3.35	3.29
23	2.99		
Mar. 2	2.99		
9	2.99		

New issues (millions $'s, monthly ave. or month)

	Swiss bonds	Swiss stocks	Fgn. bonds	Total
1960	17.3	3.8	10.8	31.8
1961	19.8	7.2	18.6	45.7
Qtr. I	24.0	14.3	25.9	64.2
II	17.6	6.8	15.5	39.9
III	19.6	1.2	18.6	39.5
IV	18.2	6.6	14.3	39.1
May	13.0	12.6	17.0	42.6
June	23.3	2.7	18.0	44.0
July	17.7	2.2	42.0	61.9
Aug.	7.4	0.9	7.0	15.3
Sept.	33.7	0.6	7.0	41.3
Oct.	38.3	1.2	20.9	60.2
Nov.	14.1	2.1	10.5	26.6
Dec.	2.1	16.3	11.6	30.0
1962				
Jan.	13.9	2.1	23.3	39.3

Chart 1

INTEREST ARBITRAGE, UNITED STATES / CANADA

Thursday figures

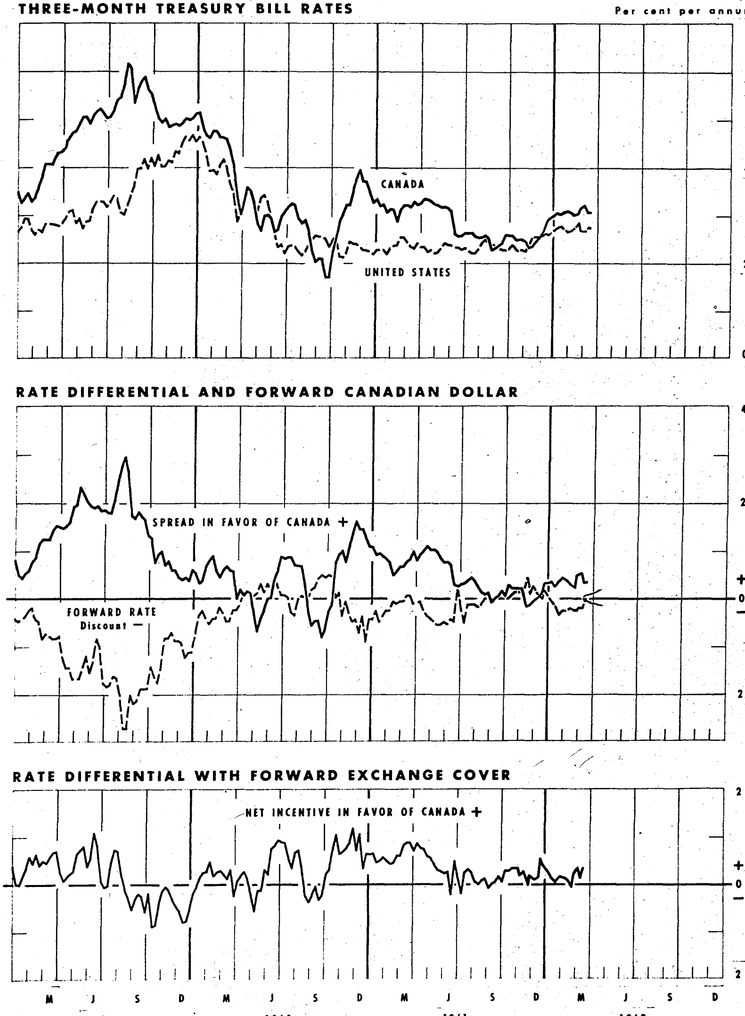


Chart 2

INTEREST ARBITRAGE, NEW YORK/LONDON

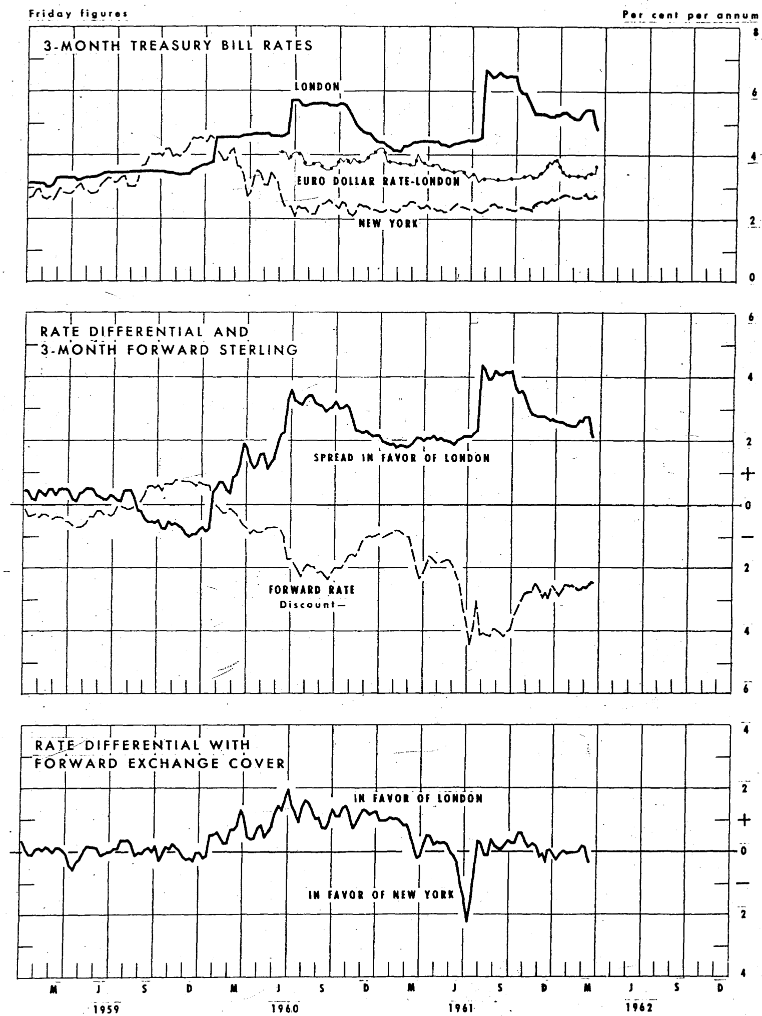
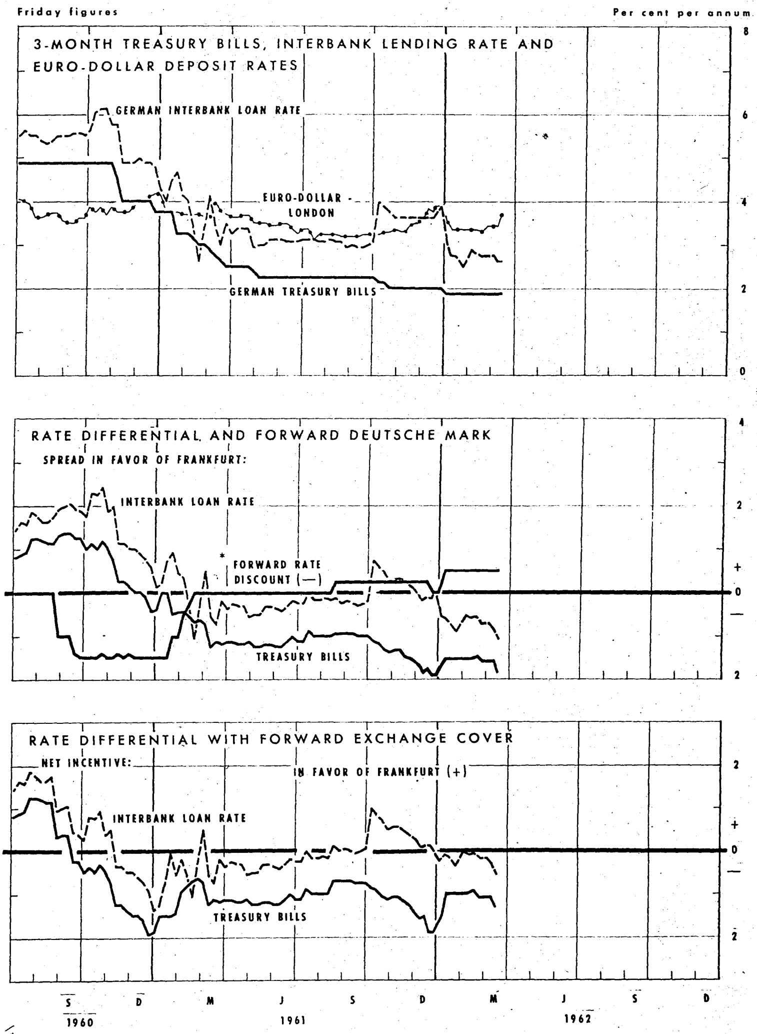


Chart 3

INTEREST ARBITRAGE FOR GERMAN COMMERCIAL BANKS



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

Chart 4

INTEREST ARBITRAGE, FRANKFURT / LONDON

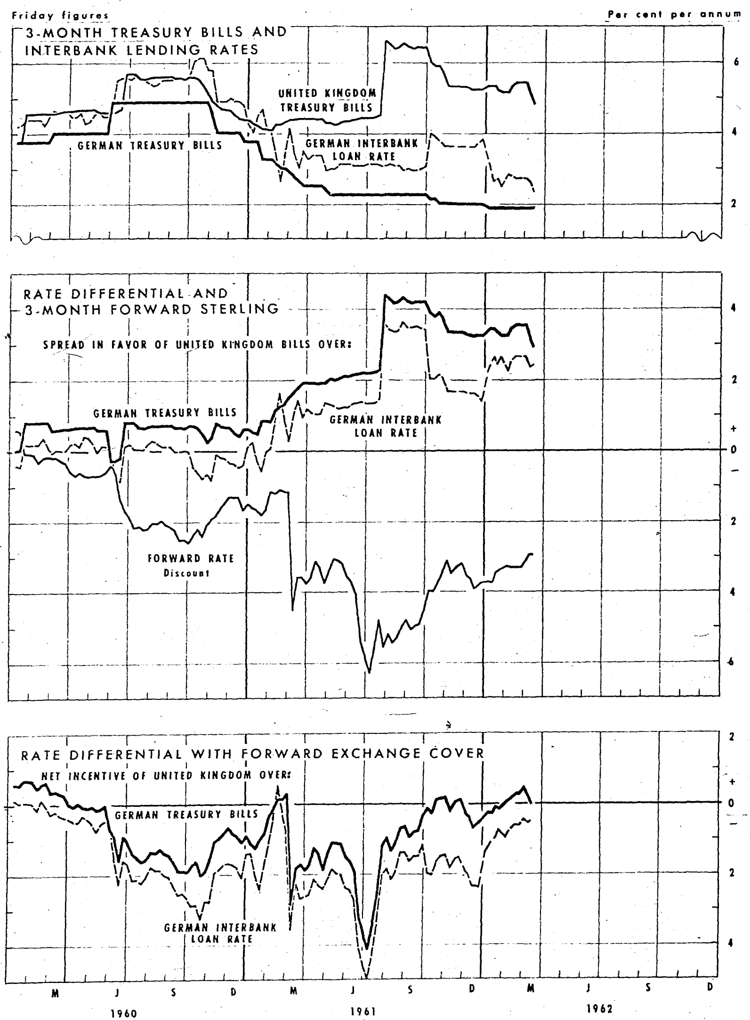
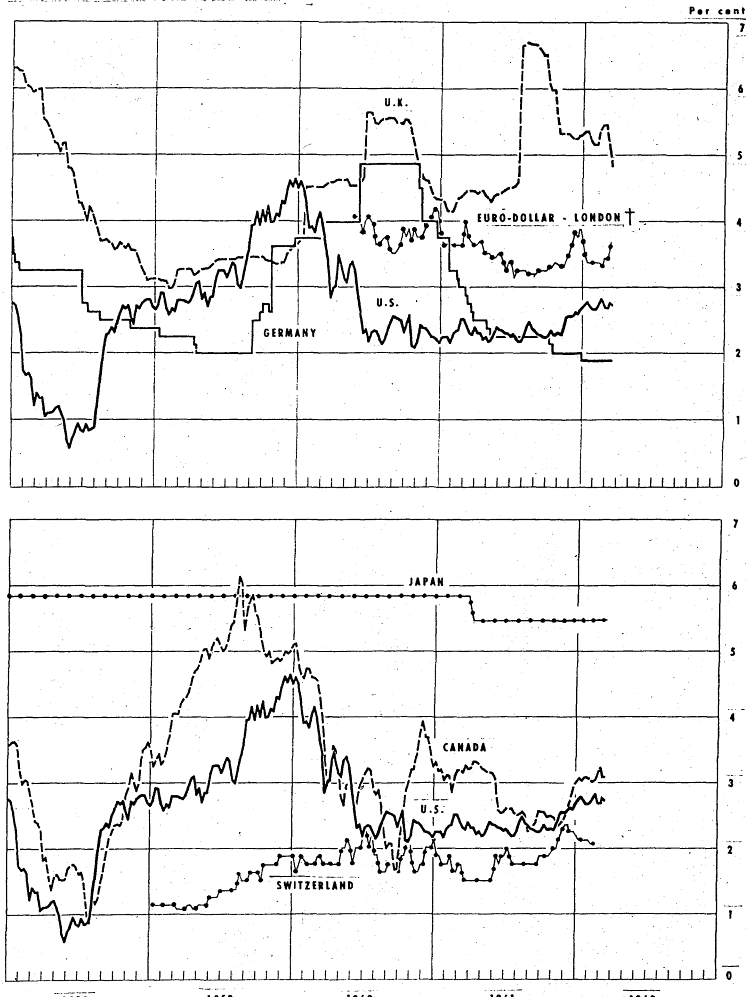


Chart 5

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

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Chart 6

LONG-TERM BOND YIELDS

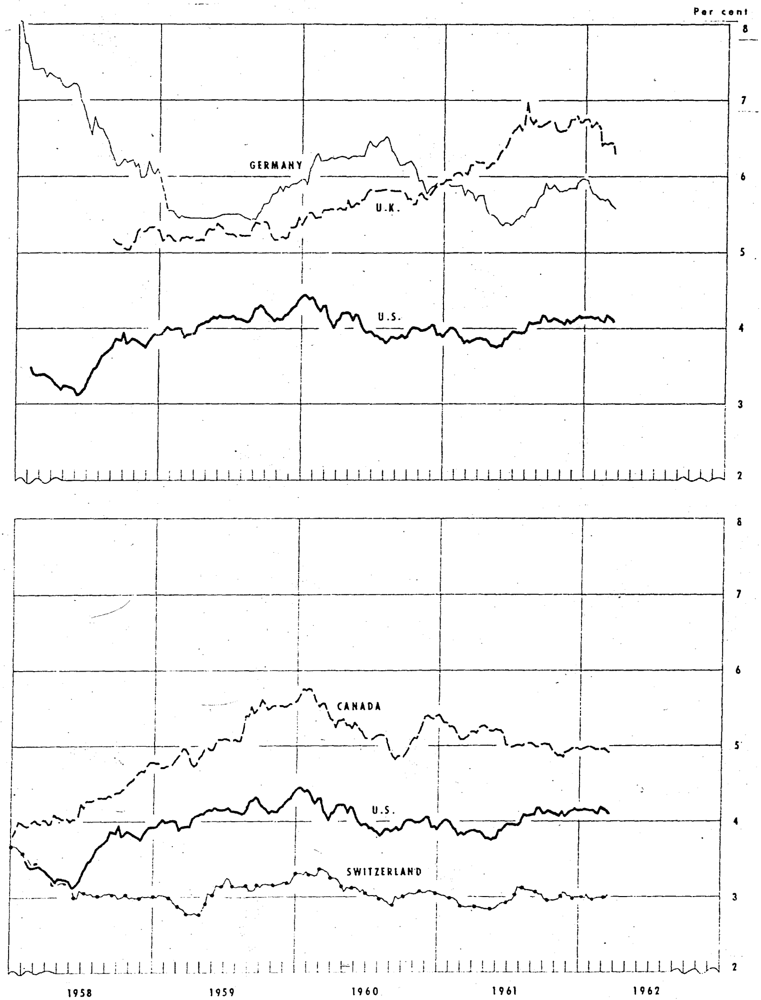
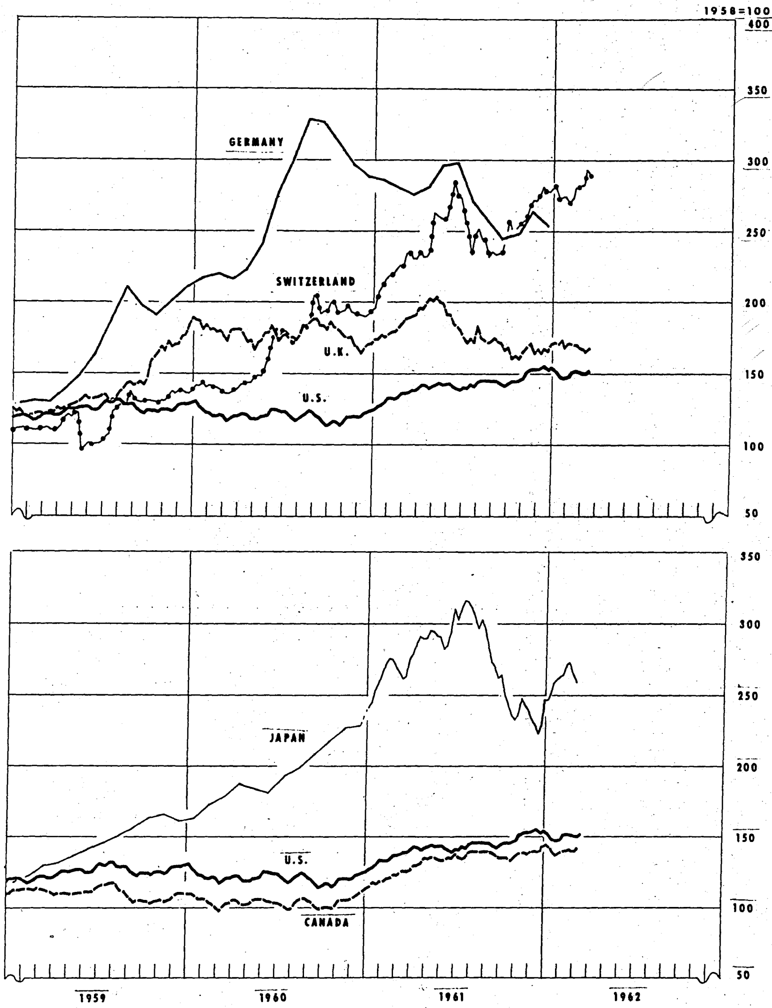


Chart 7
INDUSTRIAL STOCK INDICES*



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

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Chart 8

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

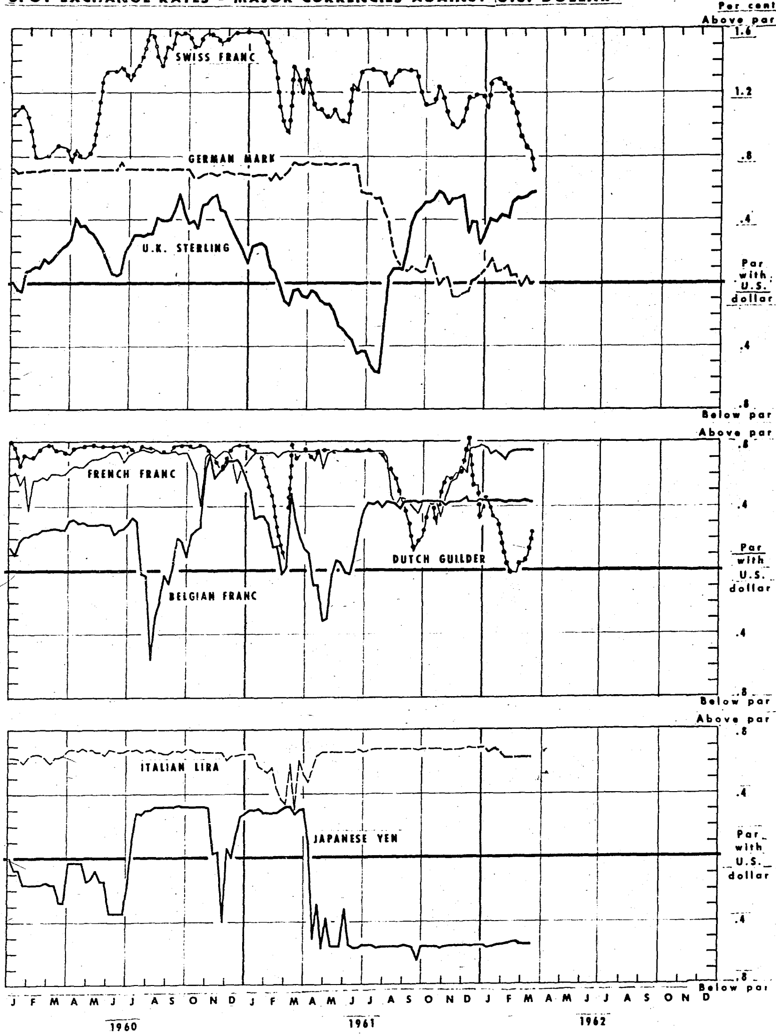

Chart 9

3-MONTH FORWARD EXCHANGE RATES