

H. 13
No. 87

November 30, 1962

CAPITAL MARKET DEVELOPMENTS ABROAD

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FEDERAL RESERVE BANK
OF BOSTON

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

Germany: Money and Capital Markets in October

A 16 per cent rise in German stocks between October 12 and November 20 brought to an end, at least for the moment, a downward trend which began in mid-1960 and has been particularly steep during 1962 (See Chart 7). This vigorous advance, which coincided with a sharp rise in prices in New York and in European financial centers, appears to reflect a market opinion that German share prices have now passed the low point. However, the bond market showed no improvement during this period and market yields advanced further beyond the 6 per cent level.

Over the past several months, the German banks and business community have been experiencing a general contraction in liquidity. As a result, the banks have recently begun to show greater restraint in their lending and security market transactions.

On the bond market, the reduced liquidity of the banks and a substantial slate of new issues brought average bond yields to about 6.1 to 6.2 per cent in recent weeks. The inability of the market to hold the 6 per cent level in October was attributed to "some DM 200 million of recent industrial issues. . . in the hands of the underwriting banks. . . clogging the market." The new issue slate has included a DM 250 million issue of the German Railways and two industrial issues totalling DM 125 million. The Federal Railways issue to be offered in early December is expected to be at the same terms as a DM 250 million offering by the Federal Government which was fully subscribed on October 22: a 6 per cent coupon at par for 10 years with no call provision. Because the time of large Federal budget surpluses has passed, it is expected that the Federal authorities will henceforth have to have regular recourse to the capital market to finance the deficits.

Tightening domestic liquidity and the inadequacy of the German capital market seem to be causing an increasing number of businesses to turn to foreign markets for financing. A large German firm floated a SFr 50 million (DM 50 million) loan in Switzerland during October for the second time this year. Part of the larger net inflow of private capital in the payments data for the third quarter reflects heavier borrowings abroad by German firms as well as by German banks.

Declining security prices, together with reduced profit margins, have created liquidity pressures on both industry and the banks. In addition, money-market factors have been reducing the free liquidity resources of the banks. Despite the Federal cash deficit, the public authorities are continuing to drain

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reserves from the banks for two reasons: (a) Federal spending abroad, a significant part of total spending, does not provide reserves to the banks; and (b) the Treasury deficit has been covered by market borrowing. In addition, notes in circulation have continued to expand. The inflows of foreign funds to the banks in recent months, despite repatriation of money-market assets and the resumption of German borrowing abroad,

"were no longer sufficient, as they were in early years, to offset--still less to outweigh--the seasonal influences depressing bank liquidity."

(Bundesbank, Monthly Report, October 1962, p. 5.)

On the external side, the German balance of payments showed a deficit of DM 242 million in the third quarter compared with a DM 146 million deficit in the preceding three months. During the third quarter, large net tourist payments virtually eliminated the surplus on other "goods and services" transactions; the long-term private capital inflow was limited. Despite rising imports, the seasonally-adjusted trade surplus averaged \$91 million in the third quarter (compared with an average of about \$82 million in the first half of 1962) and was about \$115 million in October. (See Table 4.)

Money market. As a result of technical factors, money-market rates eased in October from high late September levels. Rates on day-to-day money declined from 2-3/4 - 3-1/4 at the beginning of October to an end of the month range of 1-3/4 - 2-1/8 (see Table 1). Rates on three-month loans continued high, perhaps in part because of rising rates on deposits in the Euro-dollar market and in the United States. At the end of October, the rate on call money stood below the Treasury bill rate for the first time in months. The ready availability of short-term money was due in major part to the measures taken in early October by the Bundesbank to induce the banks to hold money in Germany until the end of the year.

Table 1. Money Market Rates in Frankfurt, September and October
(in per cent per annum)

	<u>Day-to-day money</u>	<u>Three-month loans</u>
Sept. 3-7	2-7/8 - 3	3-1/8 - 3-1/4
10-14	2-7/8 - 3-1/8	3-1/4
17-21	3 - 3-1/4	3-1/8 - 3-1/4
24-28	3 - 3-1/4	3-1/8 - 3-1/4
Oct. 1-5	2-3/4 - 3-1/4	4-1/4 - 4-1/2
8-11	2-1/8 - 2-3/4	4-1/4 - 4-1/2
15-19	2-1/8 - 2-1/4	4-3/8 - 4-5/8
22-26	1-3/4 - 2-1/8	4-3/8 - 4-5/8

The money market tightened appreciably in the first week of November as commercial banks replenished their required reserves with the Bundesbank. Call rates rose to 2-7/8 - 3 per cent but eased during the following week. By

the third week of November the market for day-to-day money was extremely liquid with rates at 2-1/8 per cent - almost a full per cent under the central bank discount rate. The liquidity on the money market was the result of the fact that commercial banks were highly liquid in anticipation of year-end credit stringencies.

Bond market. The general weakening of the bond market which began some time ago continued during the period under review. Whereas six per cent issues were placed easily in July at par despite a record volume of new issues, certain 6 per cent loans opened for subscriptions in October at 99-3/4 were still not fully taken up by the middle of November. The October Report of the Bundesbank attributes the weakness of the market to the large volume of new issues and the especially large financing demands of the Federal Government during the past few months. (See Table 2.)

Table 2. Gross Placements in German Security Markets
(in millions of DM, monthly or monthly average)

	1961				1962				
	I	II	III	IV	I	II	III	Aug.	Sept.
"Occasional" borrowers' bonds:									
Industrial	39	16	--	50	112	72	113	25	56
Public authority	441	78	84	79	314	136	358	360	76
Foreign issuers	--	--	4	--	32	--	--	--	--
Other bonds a/	101	117	53	84	89	132	154	56	254
Total occasional borrowers' bonds	581	211	141	213	547	340	625	441	386
Mortgage and communal bonds	526	525	464	503	665	453	532	530	425
Total gross bond placements b/	1,107	736	605	716	1,212	793	1,157	971	811
Gross share placements	354	263	352	130	185	205	172	148	55
Total security placements at issue value	1,461	999	957	846	1,397	998	1,329	1,119	866

a/ Mostly bonds of specialized credit institutions, especially in 1961.

b/ Includes medium-term notes (Kassenobligationen).

Bond prices dropped during October and the average yield on bonds rose to 6.1 - 6.2 per cent. (See Chart 6.) The yield on medium-term, non-bonded loans (Schuldscheindarlehen) had risen above 6.5 per cent by mid-November. Preliminary calculations indicate that the total nominal value of bonds traded in October amounted to DM 875 million; stocks totaled DM 108 million.

Some bankers find grounds for hope that the rise in interest rates is coming to an end in the fact that the volume of new mortgage bank issues has decreased. These issues exert considerable influence on the market and a further increase in mortgage rates by the mortgage banks seems scarcely possible because

of ever increasing competition from the savings banks and insurance firms. Moreover the suspension of the Government subsidy on housing should lead to a decrease in the number of new mortgages, thus easing the over-all demand on the bond market..

A relatively heavy slate of new issues was announced for December including two 6 per cent industrial issues totaling DM 125 million which will probably be offered at 99-1/2 of par and a DM 250 million Federal Railways loan. The Railways issue will carry a coupon of 6 per cent and will be non-callable until maturity in January 1973. Market sources question whether the rate of the Railways issue can be held at par. Because of market conditions, the tranche of a Federal Government loan scheduled for December has been postponed till January.

Stock market. The bear mood which dominated the stock market throughout the third quarter seems finally to have worn itself out. After the mid-October shake-out when the Frankfurter Allgemeine general index fell to 132, the market regained its losses and during the last half of the month consolidated its position. The FAZ index rose 9 per cent from the 12th to 31st of October and another 7 per cent from the 1st to 20th of November when the index reached 156 on an increasingly high rate of turnover.

The performance of the market in the past few weeks has shown an underlying strength in holding steady throughout the Cuba crisis, the Spiegel affair and the German Cabinet crisis. Careful buying is evident but unfavorable public sentiment seems to have been dissipated, at least for the moment. In the third quarter of 1962, foreigners purchased DM 313 million worth of German stocks; foreign sales totaled only DM 175 million. These figures suggest that sales of stocks by foreigners could not have been responsible for market weakness over the past few months as was thought in some circles.

Recent price trends. Prices have remained relatively stable in Germany over the past few months. Between June and September, consumer prices declined by one point because of lower food prices. (See Table 3.) Export prices also declined by one point. The wage index does not go beyond June.

Table 3. Selected Price Indices for Germany
1953 = 100

	End - of - Period									
	1960	1961				1962				
		I	II	III	IV	I	II	III	Aug.	Sep.
Industrial production	186	191	190	188	192	195	199	197		
Hourly wages in manufacturing	151	152	153	161	163	169	172			
Consumer prices	112.0	113.0	114.1	114.9	115.3	117.0	118.9	118.6	118.2	117.8
Wholesale prices	104.2	104.8	104.7	104.9	105.3	105.7	106.1	106.2	106.2	106.3
Export prices	101	100	101	101	102	102	102	101	101	101

Source: OECD

German foreign trade. The seasonally-adjusted German trade surplus rose in the third quarter about 10 per cent above the uncommonly low first and second quarter levels but is currently only about half the 1961 surpluses. (See Table 4.) The steep increase in imports, the chief reason for the diminishing trade surplus, has slowed down very considerably. Imports increased 2 per cent from the first to second quarter but only 1 per cent from the second to third. Exports increased 2 per cent in both periods. Imports of foods declined by a large amount; however imports of finished goods and consumer products -- most notably textiles, leather and paper goods, shoes, and electric products -- increased. Preliminary estimates show the trade surplus in October advanced further. Although both imports and exports declined, the greater decline in imports produced a trade surplus of \$115 million in the month.

Table 4. German Foreign Trade
(seasonally adjusted, monthly or calendar month in millions of U.S. dollars)

	Calendar Year		1961				1962				
	1960	1961	I	II	III	IV	I	II	III	Sep.	Oct. p/
Exports	947	1061	1037	1071	1085	1052	1083	1105	1123	1140	1109
Imports	843	911	864	917	918	947	999	1024	1032	1038	994
Surplus	104	150	173	154	167	105	84	81	91	102	115

p/ Preliminary

In September Germany and Japan signed a treaty providing for a liberalization of the German protective quotas set on Japanese imports, the most important of which are textiles and ceramics. Under the terms of the treaty, the quotas on certain types of goods may remain in effect for another year; in some instances a 10 per cent increase in quota has been agreed upon. New quotas for cotton textiles were set; they remain in effect for the next five years but may be discussed at the end of three years if desired. Seventy-five per cent of Japanese shipments to Germany are now free of restrictions.

Balance of payments and reserves. Despite the improved trade balance, the German balance of payments showed a deficit of DM 242 million compared with a DM 146 million deficit in the second quarter. (See Table 5.) A very large increase in net tourist spending virtually offset the surplus on all other "goods and services" transactions. Reduced official payments abroad and some increase in private capital inflow helped to limit the size of the payments deficit. In part, the capital inflow represented heavier purchases of German securities by foreigners. There was also an increase in short-term trade credits received by the German commercial banks. Partly offsetting these favorable developments were an increase in official outpayments on long-term capital account, consisting mainly of increased credits to India and Turkey, and a net outflow of unrecorded private capital (comprising the bulk of errors and omissions).

Table 5. German Balance of Payments, Oct. 1961 - Sept. 1962
(in millions of DM)

	1961	1962			July	Aug.	Sept.
	Oct. Dec.	Jan.- Mar.	Apr.- June	July- Sept.			
Balance of Payments							
1. GOODS AND SERVICES							
Trade balance	1268	617	938	968	280	217	471
Services purchased by foreign troops	963	1021	1066)		(378	322)	
Tourism (net)	- 217	- 291	- 562)	-869	(-404)	-514)	-250
Other	- 908	- 567	- 615)		(-436	35)	
Total	<u>1106</u>	<u>780</u>	<u>827</u>	<u>99</u>	<u>-182</u>	<u>60</u>	<u>221</u>
2. OFFICIAL PAYMENTS							
Donations a/	-1012	- 944	-1012	-709	-256	-242	-211
Long-term capital	-1208	- 483	- 68	-104	-489	78	7
Short-term capital	277	- 141	- 225	218	288	-109	39
Total	<u>-1943</u>	<u>-1568</u>	<u>-1305</u>	<u>-895</u>	<u>-457</u>	<u>-273</u>	<u>-165</u>
3. PRIVATE CAPITAL							
Securities transactions:							
German securities ^{b/}	238	523	198	358	158	130	70
Foreign securities ^{c/}	- 37	- 340	- 168	- 23	1	- 11	- 13
Other long-term	- 181	101	40	20	- 20	36	4
Short-term ^{b/}	185	- 582	- 69	461	376	137	- 52
Errors and omissions	- 599	1129	331	-262	- 7	- 96	-159
Total	<u>- 394</u>	<u>831</u>	<u>332</u>	<u>554</u>	<u>508</u>	<u>196</u>	<u>-150</u>
SURPLUS OR DEFICIT (-)	<u>-1231</u>	<u>43</u>	<u>- 146</u>	<u>-242</u>	<u>-131</u>	<u>- 17</u>	<u>- 94</u>
Financed by:							
1. COMMERCIAL BANK FOREIGN ASSETS (increase-)	1711	-2384	1068	832	-174	236	770
2. RESERVE MOVEMENTS							
IMF position	292	301	- 140	247	260	--	- 13
Bundesbank liabilities	- 352	228	- 204	122	- 51	- 27	200
Gold and foreign exchange (increase-)	- 420	1812	- 578	-959	96	-192	-863
Total	<u>- 480</u>	<u>2341</u>	<u>- 922</u>	<u>-590</u>	<u>305</u>	<u>-219</u>	<u>-676</u>
TOTAL FINANCING	<u>1231</u>	<u>- 43</u>	<u>146</u>	<u>242</u>	<u>131</u>	<u>17</u>	<u>94</u>

a/ Includes private donations, which averaged only DM 119 million a quarter in 1961.

b/ Excluding commercial bank foreign assets.

c/ Net purchases of German securities by foreigners.

d/ Net purchases (-) of foreign securities by Germans.

In spite of the overall balance of payments deficit of DM 94 million in September, the Bundesbank's gold and foreign exchange assets increased by DM 863 million in that month due largely to the increase of DM 200 million in Bundesbank liabilities, presumably to foreign central banks, and to a DM 770 million repatriation of foreign exchange by the commercial banks. Hence, the net gold and foreign exchange assets of the Bundesbank and the commercial banks increased by DM 93 million in September, or, adjusting for DM drawings of DM 13 million from the IMF by Egypt, by DM 106 million (\$26.5 million).

Europe and British Commonwealth Section.

II. Nine Charts on Financial Markets Abroad

- Chart 1 - Interest Arbitrage, United States/Canada
- Chart 2 - Interest Arbitrage, New York/London
- Chart 3 - Interest Arbitrage for German Commercial Banks
- 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 - Spot Exchange Rates - Major Currencies
Against U.S. Dollar
- Chart 9 - 3-month Forward Exchange Rates

Table 6. Germany: Selected Money Market Yields and Exchange Rates

- 8 -

(per cent per annum)

	3-mo. Euro-dollar deposits London	3-mo. inter-bank loans Frankfurt	Spread in favor London	3-mo. U.S. \$ into Marks		3-mo. Treas. bills		
				Comm. banka/	Market	U.K.	Ger.	U.S.
1961-Oct. 6	3.25	4.00	-0.75	+0.25	+0.60	6.00	2.13	2.31
Nov. 10	3.31	3.63	-0.32	+0.25	+0.73	5.31	2.00	2.47
Dec. 22	3.88	3.75	+0.13	--	+1.30	5.28	2.00	2.60
1962-Jan. 5	3.63	3.00	+0.50	+0.25	+0.95	4.34	1.88	2.74
Feb. 16	3.44	2.75	+0.56	+0.50	+0.62	5.44	1.88	2.83
Mar. 30	3.69	2.63	+1.06	+0.25	+0.35	4.34	2.00	2.75
Apr. 27	3.50	2.94	+0.56	+0.25	+0.32	4.03	2.13	2.74
May 25	3.81	3.13	+0.68	+0.25	+0.35	3.69	2.13	2.69
June	3.66	n.a.	n.a.	+0.25	+0.21	3.78	2.25	2.74
July 27	3.94	3.31	+0.63	+0.50	+0.82	3.81	2.38	2.88
Aug. 24	3.72	3.38	+0.34	+0.75	+0.63	3.69	2.50	2.82
Sep. 21	3.94	3.19	+0.75	+0.75	+0.65	3.63	2.50	2.76
Oct. 5	3.81	4.38	-0.57	+0.75	+0.47	3.55	2.63	2.76
11	3.91	4.38	-0.47	+0.75	+0.60	3.53	2.63	2.77
19	3.91	4.50	-0.59	+0.75	+0.56	3.69	2.63	2.74
26	4.13	4.50	-0.37	+0.75	+0.75	3.78	2.63	2.73
Nov. 2	4.19	n.a.	n.a.	+0.75	+0.50	3.78	2.63	2.83
9	4.06	n.a.	n.a.	+0.75	+0.64	3.72	2.63	2.80

a/ Bundesbank special rate for 2 to 6 month deposits.

Germany: Selected Loan, Deposit and Security Rates
(per cent per annum)

	Comm. bank loans ^{a/}	6-12 mo. deposits		Bond yields		Share yields	Yield gap
		Savings	Time	5-1/2% Railway 1958-83	Public author- ities		
1960-March	8.50	3.75	3.25	6.3	6.4	2.27	4.1
Dec.	8.50	4.50	3.50	5.9	6.2	1.96	4.2
1961-March	8.00	4.25	3.25	5.8	5.9	2.11	3.7
Dec.	7.50	3.50	2.75	6.0	6.0	2.49	3.5
1962-Jan.	7.50	3.50	2.75	5.8	5.9	2.57	3.3
Feb.	7.50	3.50	2.75	5.7	5.7	2.61	3.1
Mar.	7.50	3.50	2.75	5.6	5.6	2.65	3.0
Apr.	7.50	3.50	2.75	6.6	5.6	2.77	2.8
May	7.50	3.50	2.75	5.7	5.8	3.23	2.6
June	7.50	3.50	2.75	5.8	5.9	3.49	2.3
July	7.50	3.50	2.75	5.8	5.9	3.71	2.1
Aug.	7.50	3.50	2.75	5.8	6.0	3.58	2.2
Sept.	7.50	3.50	2.75	5.9	6.0	3.79	2.1
Oct.				6.0			

a/ Approved credits on current account.

INTEREST ARBITRAGE, UNITED STATES / CANADA

Thursday figures

THREE-MONTH TREASURY BILL RATES

Per cent per annum

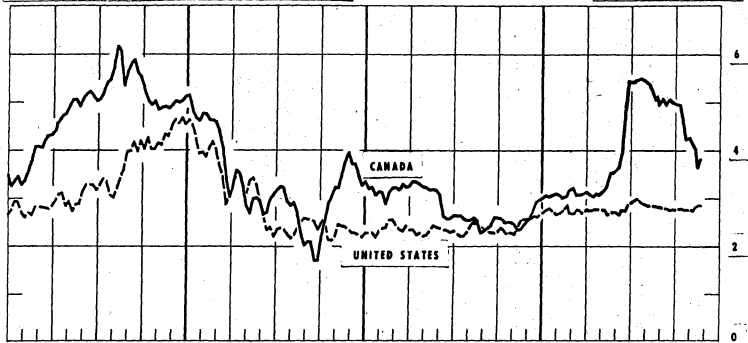
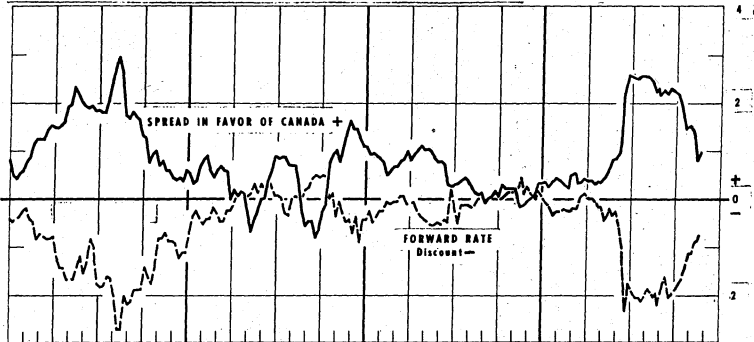
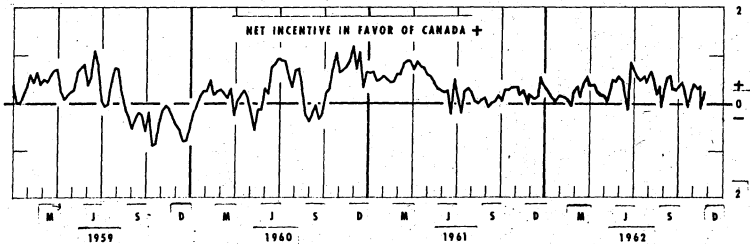
**RATE DIFFERENTIAL AND FORWARD CANADIAN DOLLAR****RATE DIFFERENTIAL WITH FORWARD EXCHANGE COVER**

Chart 2

INTEREST ARBITRAGE, NEW YORK/LONDON

Friday figures

Per cent per annum

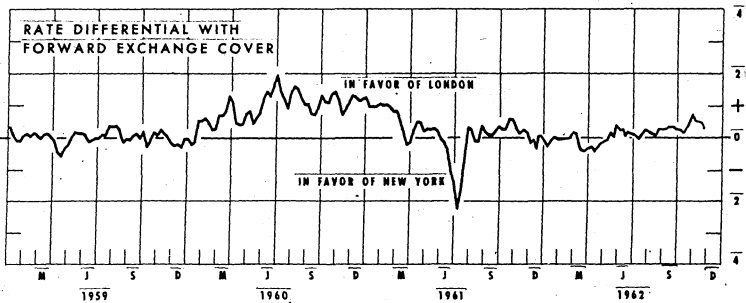
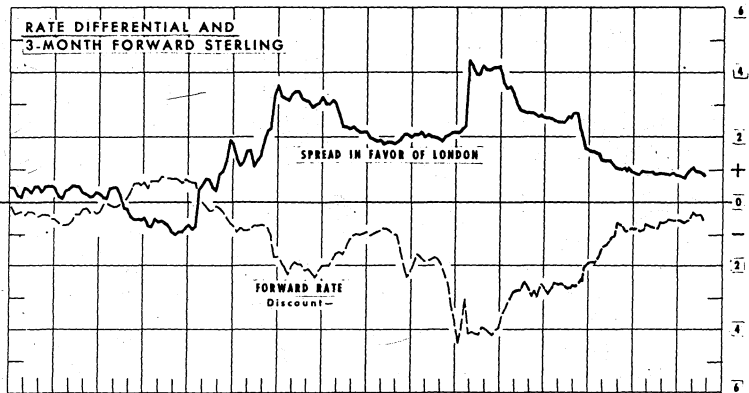
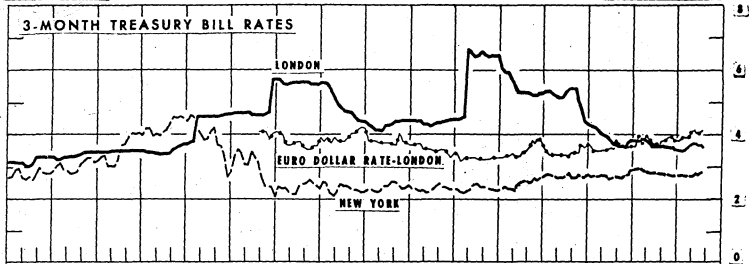
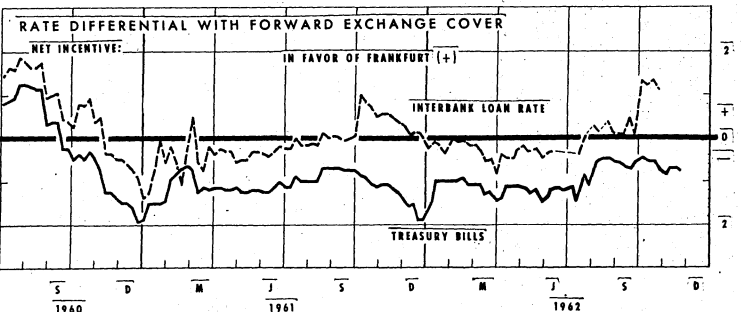
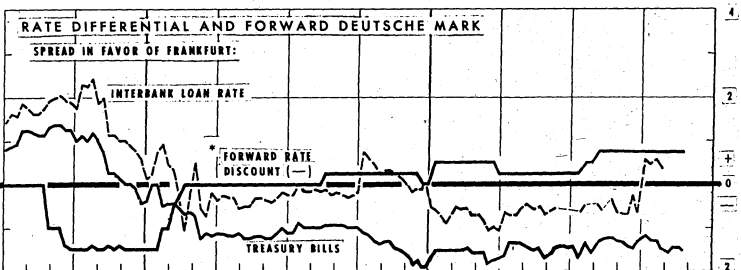
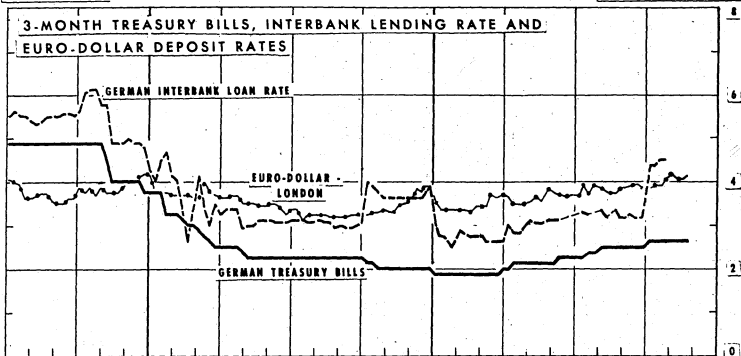


Chart 3

INTEREST ARBITRAGE FOR GERMAN COMMERCIAL BANKS

Friday figures

Per cent per annum



Note: Special forward rate available to German commercial banks.

Chart 4

INTEREST ARBITRAGE, FRANKFURT / LONDON

Friday figures Per cent per annum

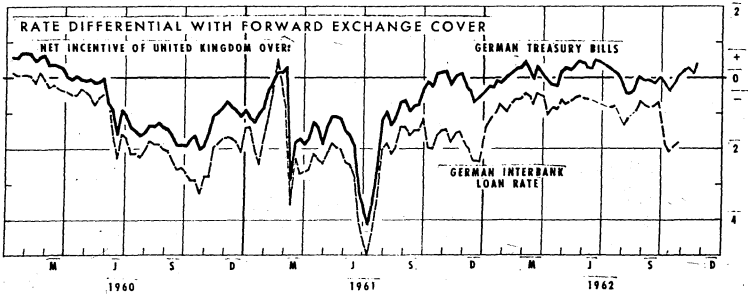
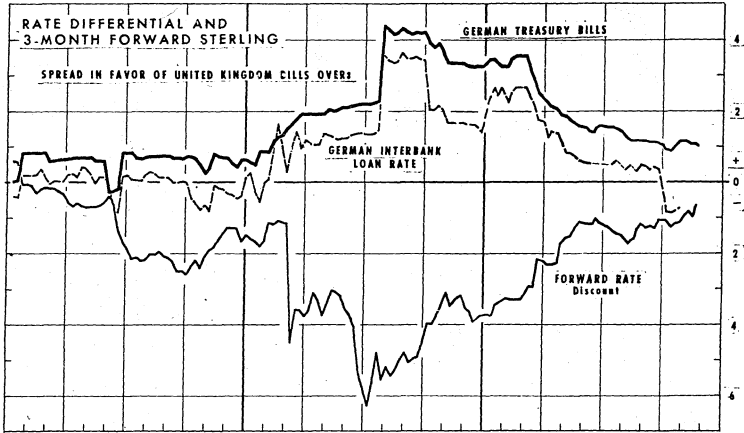
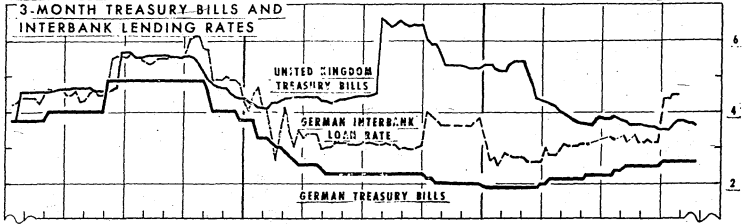
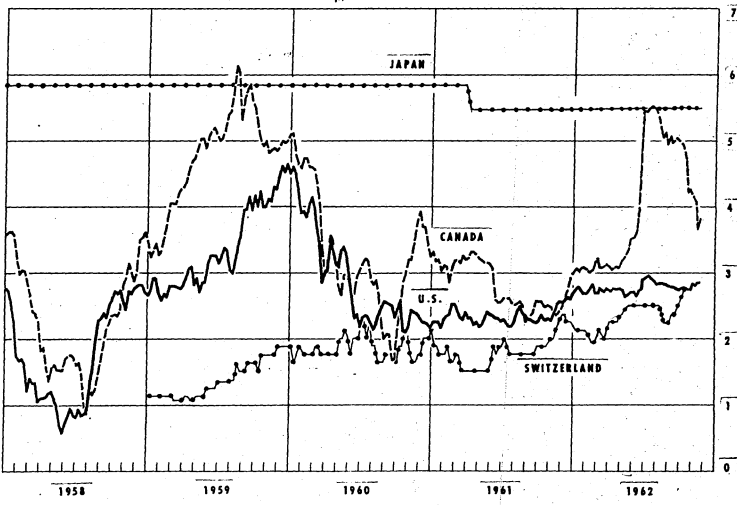
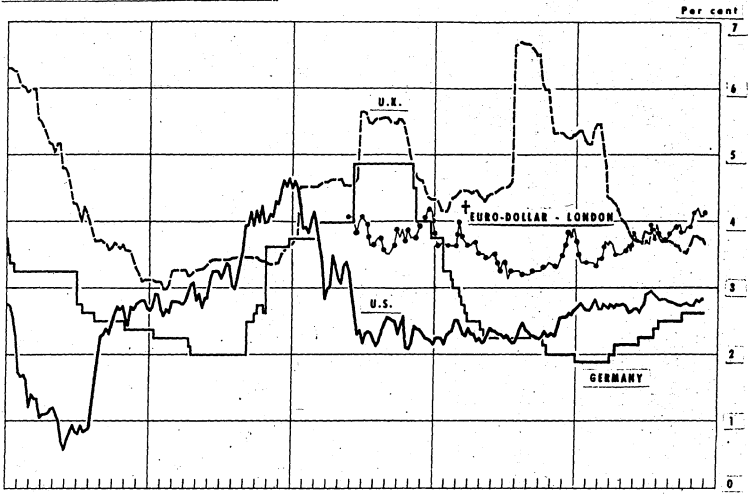


Chart 5
SHORT-TERM INTEREST RATES *



* 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.

Chart 6

LONG-TERM BOND YIELDS

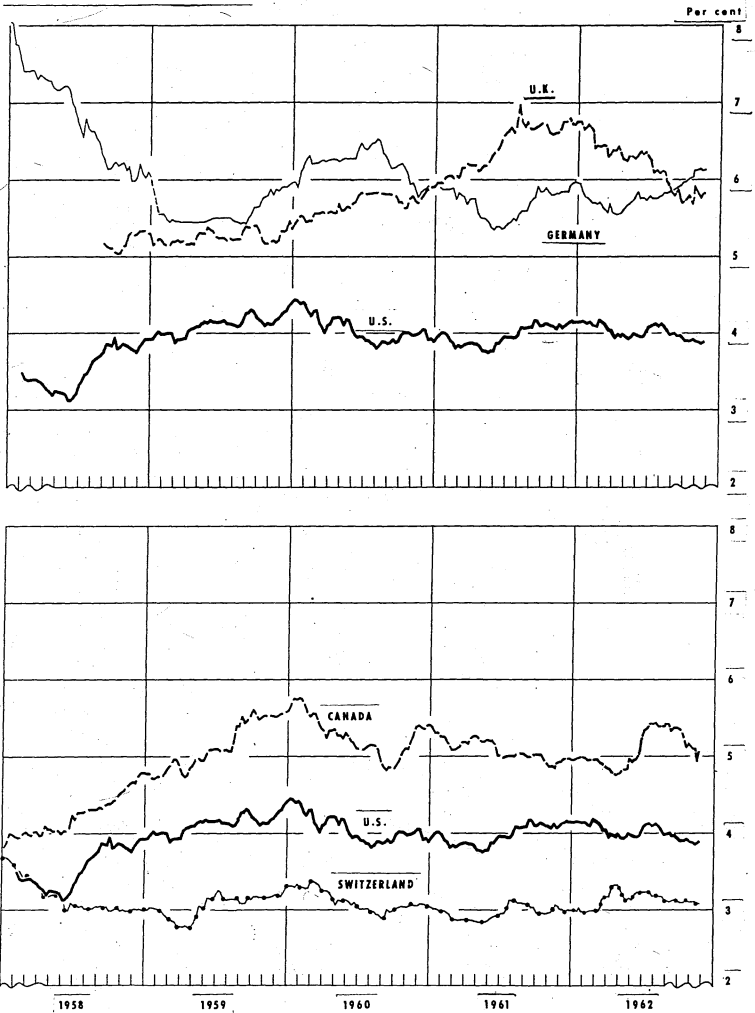
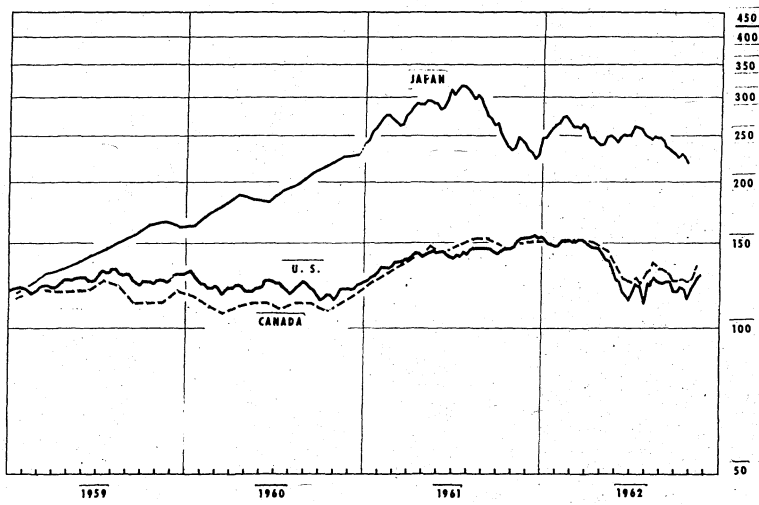
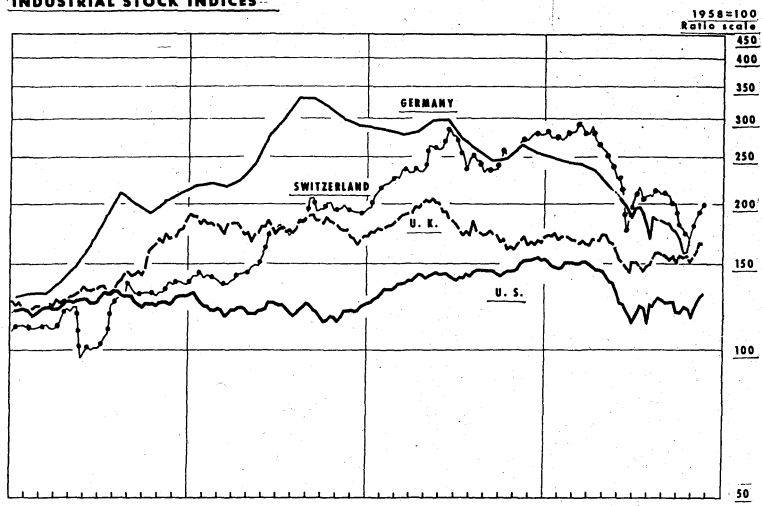


Chart 7
INDUSTRIAL STOCK INDICES*



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

Chart B

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

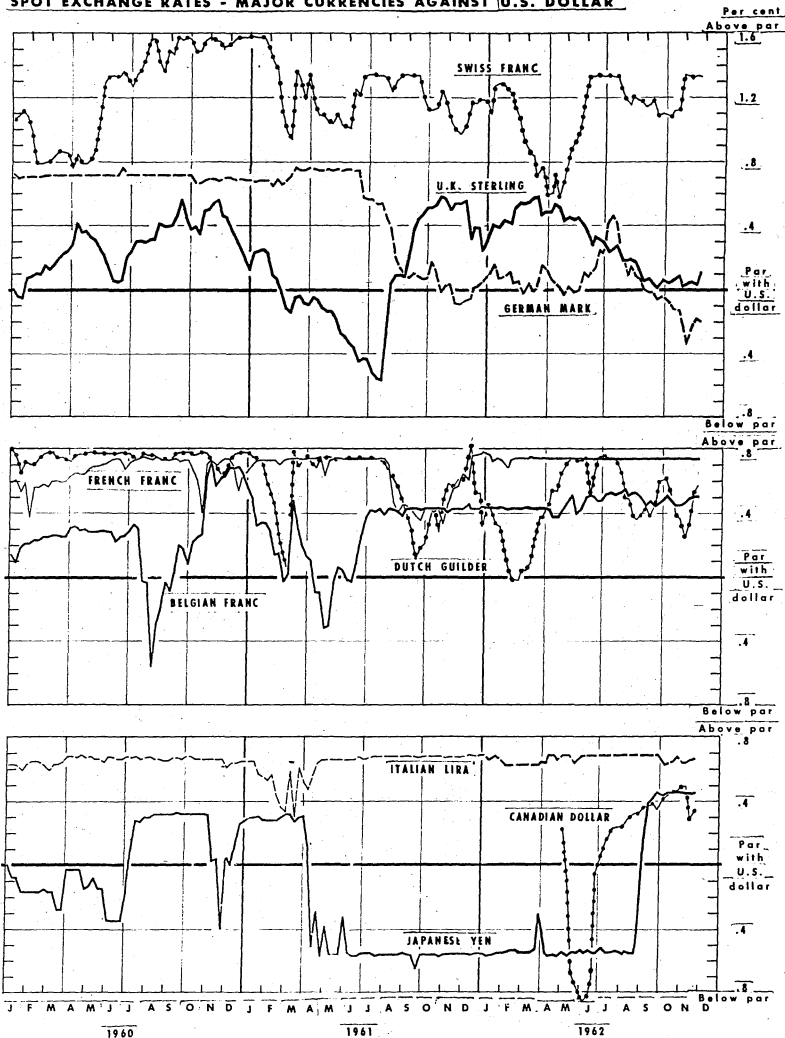


Chart 9
3-MONTH FORWARD EXCHANGE RATES

