BOARD OF GOVERNORS
OF THE
FEDERAL RESERVE SYSTEM

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H. 13
No. 89

CAPITAL MARKET DEVELOPMENTS ABROAD

I. Canada
II. Nine Charts on Financial Markets Abroad

I. Canada: Money and Capital Markets in November

The Bank of Canada, in reducing the discount rate to 4 per cent on November 13, served notice of a reorientation of Canadian monetary policy by observing that in view of the inflow of foreign capital and the increase in reserves "greater weight could be given to other factors."

Money rates reacted quickly to the Bank rate action, with the 91-day Treasury bill yield falling to 3.62 per cent on November 15 from 4.09 per cent the previous week. On December 5, the 3-month bill rate stood at 3.71 per cent. The yield on 6-month Treasury bills underwent similar movements, falling to 3.74 per cent on November 15 from 4.21 per cent on November 7, and partially recovering to 3.94 per cent on December 5.

Bond yields also fell following the Bank rate announcement, particularly at the short end of the yield curve. In the week ending November 14, declines in Government bond yields ranged from 53 basis points on short-term (1-1/2 year) issues to about 10 basis points on long-term (35 year) bonds. By December 5, bond yields had recovered most of the mid-month decline primarily because of heavy bond sales from the nonbank sector to finance purchases of Canada Savings Bonds (see Table 1).

Table 1. Canada: Net Purchases(+) or Sales(-) of Government Securities, October 24 - December 5, 1962

	Government of Canada Securities		
	Treasury Bills	Bonds	Canada Savings Bonds
Bank of Canada	+ 54	a/ +255	
Chartered Banks	+111	+216	
Government Accounts	+ 17	+ 2	
General Public	- 52	b/ -603	+820
Change in Total Outstanding	+130	-131	+820

a/ Increased by $270 million in consequence of the termination of portions of the Bank's reciprocal currency arrangement with the Federal Reserve System and the Bank of England amounting to $189 million (equivalent to U.S. $175 million) on October 31 and $81 million (equivalent to U.S. $75 million) on November 30.
b/ Decreased by the transactions described in a/, above.

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DECONTROLLED AFTER SIX MONTHS

In the exchange market, the Canadian dollar has remained strong following a temporary weakening immediately in the wake of the rate announcement. But the Bank of Canada acquired reserves at a rate substantially below that of recent months. As compared with accruals of U.S. $114 million in September and U.S. $189 million (adjusted) in October, the (adjusted) increase in official gold and U.S. dollar holdings during November was only U.S. $69 million.

On November 14, the Canadian Government announced the elimination (or, in a few cases, reduction) of the temporary surcharges on imports amounting to about $260 million annually. The surcharge removals, affecting principally food, fish, and agricultural products, were apparently motivated by a desire to moderate upward pressures on consumer prices, which have been rising in recent months. These surcharges, like those eliminated on October 17, covered about one-twelfth of the total import trade affected by the imposition of temporary surcharges in late June. Thus, about five-sixths of those imposed remained in effect.

Reduction in discount rate. On November 13, the Bank of Canada reduced its minimum rate on advances to chartered banks from 5 to 4 per cent. This action followed cuts in the discount rate of 1/4 of 1 per cent each on September 7 and October 12. In announcing the action, Governor Rasminsky cited the reappearance of an appreciable flow of long-term capital into Canada and the strengthening of exchange reserves and stated that, in view of these developments, "greater weight could in the present circumstances be given to other factors."

The extent of the cut in the discount rate and Governor Rasminsky's accompanying statement constitute clear evidence that, in this action, the Bank of Canada has shifted the focus of Canadian monetary policy. Earlier in 1962, before the June crisis, the rate "floated" at 0.25 per cent above the weekly auction yield on 91-day Treasury bills. In the two recent rate discount reductions, the rate was fixed at a range 1/4 to 1/2 of 1 per cent above the preceeding week's auction rate for Treasury bills (see Table 2). With the most recent cut in the discount rate, the Bank went further than would have been required in a technical adjustment to the fall in Canadian short-term money rates. Thus, the 4 per cent Bank rate on November 13 was slightly below the 4.09 per cent yield at the Treasury bill auction on November 8.

Table 2. Canada: Bank of Canada Discount Rate and Treasury Bill Yields, Selected Dates, 1962
(in per cent per annum)

Date	Bank rate	Treasury bill yield a/
1962:		
June 24	6.00	4.92
September 7	5.50	5.07
October 12	5.00	4.72
November 13	4.00	4.09

a/ 91-day Treasury bill yield at weekly auction on the Thursday preceeding Bank rate action on date shown.

Secondly, Governor Rasminsky's statement that the action could be taken as a move toward easier credit conditions was in sharp contrast to his statements accompanying the earlier discount rate acts, which cautioned that reductions were not to be understood as a move away from austerity.

Money market. After experiencing substantial declines during October, Canadian short-term interest rates dropped abruptly, following the announcement of the cut in the discount rate on November 13. The auction yield on the 91-day Treasury bill on November 15 was 3.62 per cent--47 basis points lower than the yield at the preceeding weeks's auction. The Treasury bill yield recovered to 3.82 per cent during the following week, and settled at 3.71 per cent on November 29, where it remained on December 6 (see Tables 10 and 11 and Chart 5).

The spread of the Canadian bill rate over the U.S. Treasury bill narrowed sharply with the decline in Canadian yields. The covered incentive in favor of the Canadian bill (after allowing for the cost of forward exchange cover) also declined with Canadian bill rates, but the decline was partially offset later in the month by a narrowed discount on the forward Canadian dollar (see Table 10 and Chart 1).

Canadian finance paper rates followed a pattern similar to that of the Canadian Treasury bill. Accordingly, the spread between U.S. and Canadian finance paper yields narrowed sharply in mid-November; the covered incentive in favor of Canadian finance paper fell from 0.49 per cent on November 9 to 0.19 per cent November 16, but had once again increased to 0.51 per cent by November 23 as Canadian rates underwent a partial recovery and the cost of forward exchange cover fell late in the month (see Table 3).

Table 3. U.S. and Canadian Finance Paper Rates and Arbitrage Calculation
(in per cent per annum)

		Canada	U. S.	Spread	90-day Forward Exchange	Net Incentive
August	24	5.00	2.88-3.13	2.00	-2.02	-0.02
September	7	5.00	2.75-3.00	2.12	-1.69	+0.43
October	5	5.00	2.50-3.00	2.25	-1.68	+0.57
	19	4.75	2.75-2.88	1.93	-1.28	+0.65
	26	4.25	2.63-2.88	1.49	-1.14	+0.35
November	2	4.25	2.25-2.88	1.69	-1.14	+0.55
	9	4.25	2.50-3.00	1.50	-1.01	+0.49
	16	3.75	2.50-3.00	1.00	-0.81	+0.19
	23	4.00	2.50-3.00	1.25	-0.74	+0.51

Bond market. Short- and intermediate-term Canadian Treasury bond yields shared in the decline in Canadian interest rates following the cut in the discount rate. A large part of this mid-month decline in bond yields was recovered in subsequent trading, and by December 5, yields on short- and intermediate-term Treasury securities had returned to within about 10 basis points of the levels they had occupied prior to the discount rate adjustment. Yields on long-term Treasury securities remained very nearly constant throughout November at or near the high level attained in July (see Table 4).

Table 4. Market Yields on Canadian Treasury Securities

		3 months Treasury bill (Thursday auction)	Bonds				
			1964	1965	1967-68	1975-78	1996-98
April	12	3.04	3.58	3.93	4.13	4.80	4.88
July	18	5.51	5.76	5.58	5.11	5.42	5.15
August	15	5.05	5.62	5.57	5.01	5.40	5.17
September	26	4.99	5.26	5.22	5.08	5.38	5.19
October	24	4.27	4.41	4.48	4.69	5.17	5.17
November	7	4.09	4.33	4.40	4.53	5.11	5.12
	14	3.62	3.80	3.98	4.27	4.94	5.03
	21	3.82	4.14	4.23	4.42	5.07	5.06
	28	3.71	3.98	4.14	4.38	5.06	5.07
December	5	3.71	4.20	4.30	4.43	5.06	5.09

An important factor in maintaining market yields on Treasury securities has been the large seasonal flow of funds within the nonbank sector from marketable issues into Canada Savings Bonds. Always large during the late fall, record sales of Savings Bonds were made during recent weeks in response to the favorable terms of issue of the present series. Non-marketable but always redeemable at par, Canada Savings Bonds presently offer an initial interest yield of 4.50 per cent and a yield of 5.11 per cent if held 14 years to maturity.

Debt management program. On November 30, the Minister of Finance outlined the Government's plans for refinancint three Treasury bond issues, totalling $615 million, maturing between December 1 and January 1. The maturing issues will be refinanced by $100 million in new Treasury bills and a new offering of $500 million in Government of Canada securities.

The new issue of $500 million will be offered in the two following maturities:

(1) 3-1/2 per cent non-callable bonds due February 1, 1965, priced to yield about 4.12 per cent to maturity.

(2) 4-1/4 per cent non-callable bonds due January 15, 1968, priced to yield about 4.42 per cent to maturity.

In exchange for 3-1/2 per cent Treasury bonds due December 15, the Bank of Canada has agreed to acquire $200 million of the new issue, open as to maturity; the remaining $300 million, also open as to maturity, will be offered for cash. Proceeds of the cash offering will be used to retire Treasury securities maturing December 15 and January 1.

Borrowings in the United States. Canadian long-term bond yields have remained sufficiently high to provide continued active interest in the U.S. as a source of lower-cost financing. According to A. E. Ames & Co., sales of new Canadian securities in the United States totaled Can. $677 million through November 26, as compared with Can. $238 million and Can. $148 million in comparable periods of 1960 and 1961 (see Table 5).

Statistics on trade in outstanding securities between Canadians and foreigners reveal net sales by Canadians of $15 million in August (including $12 million of Canadian securities); this was the first instance of net sales since January of this year, and contrasted with net purchases of $19 million in July. In September, net sales of outstanding securities to foreigners amounted to $9 million. For the third quarter, transactions in new as well as in outstanding securities between Canada and other countries gave rise to a net capital inflow of $38 million. Outflows were recorded for each of the previous quarters of 1962.

Table 5. Sales of New Canadian Securities Payable in U.S. Funds
(Can. $ millions)

	Total	Government	Provincial, Direct and Guaranteed	Municipal	Corporation
1960					
Total to Nov. 28	238.2	--	77.0	110.9	50.3
I	144.1	--	37.0	82.1	25.0
II	93.9	--	40	28.6	25.3
III	.2	--	--	.2	--
1961					
Total to Nov. 27	148.4	--	--	26.4	122.0
I	11.0	--	--	--	11.0
II	106.4	--	--	26.4	80.0
III	24.0	--	--	--	24.0
1962					
Total to Nov. 26	677.2	250.0	102.0	28.7	296.5
I	3.0	--	--	--	3.0
II	101.5	--	--	1.5	100.0
III	307.3	250.0	8.0	24.6	24.8
Monthly:					
April	1.5	--	--	1.5	--
May	100.0	--	--	--	100.0
June	--	--	--	--	--
July	37.6	--	--	13.8	23.8
August	9.8	--	--	8.9	1.0
September	259.9	250.0	8.0	1.9	--
October	52.5	--	15.0	1.8	35.7
November (to 26th)	212.9	--	79.0	.8	133.0

Source: A. E. Ames & Co., Weekly Bond Sales Summary.

Bank loans and bank liquidity. General loans of the chartered banks continued a seasonal decline during November. As loans declined, the chartered banks added to their holdings of Treasury bills and Canadian Government bonds. Cash reserves were reduced to just under the 8 per cent legal minimum in the week ending December 5, but as a result of continued Treasury bill purchases the liquid asset ratio of the banks, at 18.25 per cent, remained well above the 15 per cent agreed minimum (see Table 6).

Table 6. Canadian Chartered Banks: Cash Reserves & Other Assets
(In millions of dollars or per cent)

	Cash Reserves	Cash Ratio	Liquid Assets	Liquid Asset Ratio	General Loans a/	Treasury Bills a/	Canadian Government Bonds a/ (par value)
Average of Wednesdays:							
April	1,113	8.1	2,351	17.12	6,033	1,075	2,679
May	1,114	8.1	2,358	17.13	6,261	1,048	2,719
June	1,165	8.18	2,286	16.05	6,519	1,009	2,457
July	1,159	8.20	2,195	15.53	6,649	908	2,212
August	1,151	8.12	2,204	15.56	6,709	987	1,932
September	1,113	8.14	2,205	16.12	6,718	989	1,892
October	1,106	8.18	2,370	17.53	6,649	1,119	1,893
Average for week ending:							
October 10	1,100	8.14	2,309	17.07	6,704	1,066	1,887
November 7	1,144	8.37	2,513	18.38	6,606	1,163	1,945
14	1,104	8.07	2,465	18.03	6,571	1,159	1,997
21	1,102	8.06	2,483	18.16	6,544	1,179	2,044
28	1,105	8.08	2,502	18.30	6,528	1,184	2,064
December 5	1,106	7.99	2,522	18.25	n.a.	1,214	2,094

a/ Monthly data are for the last Wednesday of the month. Weekly figures are holdings as of date indicated.

Source: Bank of Canada, Weekly Financial Statistics and Statistical Summary, June 1962.

Foreign exchange. Official reserve figures for the end of November, down U.S. $6 million from the end of October, confirmed a slowdown in official Canadian reserve accruals. During November, the remaining reciprocal currency arrangements with the Federal Reserve System and the Bank of England were reduced by U.S. $50 million and U.S. $25 million, respectively. If these special transactions had not taken place, official reserve accruals during November would have been U.S. $69 million, as compared with accruals of U.S. $114 million in September and U.S. $189 million (adjusted) in October (see Table 7).

The earlier rapid pace of reserve accruals by the Bank of Canada slowed in early November; on November 9, the market rate on the Canadian dollar dropped slightly and induced the Bank of Canada to sell U.S. dollars to the market. A turning point apparently came with the Bank of Canada discount rate announcement. Immediately following that announcement, on November 14, the market rate on the Canadian dollar dropped sharply enough to induce substantial support sales by the Bank of Canada for the first time since the end of June. This weakness in the Canadian dollar was short lived, however, and since mid-November the rate has edged higher, but with the Bank of Canada generally out of the market.

Table 7. Canada: Official Holdings of Gold and U.S. Dollars

	Gold	U.S. dollars	Total	Change during period
1962: March	963.7	745.7	1,709.4	- 37.3
May	913.0	579.8	1,492.8	-102.0
June 24	n.a.	n.a.	1,100.0	-392.8
June	669.0	1,139.7	1,808.7	+708.7
July	673.8	1,440.6	2,114.4	+305.7
August	683.0	1,647.6	2,330.6	+216.2
September	688.6	1,756.0	2,444.6	+114.0
October	n.a.	n.a.	2,613.9	+169.3
November	n.a.	n.a.	2,607.5	- 6.4

Canadian banks operations in U.S. dollars. Non-Canadian currency deposits in Canadian banks increased Can. $223 million in October, following increases of Can. $8 million in September and Can. $126 million in August. A large part of the October increase was probably due to "window dressing" operations of Canadian banks.

Table 8. Call Loans in the New York Market, end of Month
($ millions)

Date	U.S. Banks a/	Foreign Agencies Total a/	Canadian b/	Other c/
1960-December	1,496	849	829	20
1961-December	1,963	859	809	50
1962: April	1,828	959	848	111
May	1,430	752	727	25
June	1,361	610	541	69
July	1,042	487	473	14
August	1,141	778	734	44
September	2,020 r/	750 r/	708	42 r/
October	2,086	846	782	64

a/ Estimates by New York State Banking Department.
b/ Call Loans, as reported by Canadian banks, converted into U.S. dollars at end-of-month exchange rates.
c/ Residual.
r/ Revised.

Stock market. The Canadian D.B.S. industrials index recovered quickly following a late-October drop in reaction to the Cuban crisis. With stock purchasing spurred somewhat by the prospect of easier credit following the Bank rate cut in mid-November, the index advanced strongly throughout the month (see Table 9 and Chart 7).

Table 9. Canadian and U.S. Industrial Stock Prices

Average for week ending		DBS Industrials a/	N.Y. Standard and Poor Industrials
1962:			
July	19	112.3	59.41
August	16	123.2	61.23
September	6	120.3	61.03
	27	113.9	58.87
October	18	114.1	59.10
November	1	115.5	59.36
	8	118.6	61.31
	15	122.3	62.93
	22	124.0	63.55
	29	125.5	64.97

a/ This series is the recently-published DBS index of 76 industrials (1956=100), and replaces the older DBS index of 66 industrials (1935-1939=100) previously reported in Capital Markets Developments Abroad series for Canada.

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 10. Canada: Treasury Bill Yields and Exchange Rates

	3-mo. Treas. bill arbitrage calculation					Spot Can.$ (U.S. cents	Finance paper	
	Canada a/	U.S. a/	Difference	3-mo. Can.$ b/	In favor Can. bill c/		30-89 days	90-179 days
1962-High	5.51	2.98	2.59	0.13	0.84	95.75	--	--
Low	3.01	2.64	0.22	-2.13	-0.11	91.73	--	--
1962-June 7	3.62	2.64	0.98	-0.55	0.43	91.73	3-3/8--1/2	3-5/8--3/4
July 19	5.51	2.93	2.58	-2.02	+0.56	92.72	--	--
Sept. 27	4.99	2.76	2.23	-1.95	+0.28	92.84	5	5-1/4--1/2
Oct. 18	4.22	2.74	1.48	-1.82	-0.34	92.88	4-1/4--1/2	4-3/8--3/4
Nov. 1	4.16	2.72	1.44	-1.14	+0.30	92.97	4-1/4--4-1/2	4-1/2--5-1/4
8	4.09	2.80	1.29	-0.94	+0.35	92.97	4-1/4	4-1/2--3/4
15	3.62	2.84	0.78	-0.88	-0.10	92.77	3-3/4	4
22	3.82	2.84	0.98	-0.74	+0.24	92.83	--	--
29	3.71	2.86	0.85	-0.68	+0.17	92.89	--	--
Dec. 6	3.71	2.84	0.87	-0.67	+0.20	93.00	--	--

a/ Thursday quotations. b/ Spread between spot and 3-month forward rate in per cent per annum. Discount equals (-). c/ Net of difference in bill yield less discount on 3-month Canadian dollar.

Table 11. Selected Government of Canada Security Yields

	6-mo. Treas. bills		Intermediate bonds (8 yr.)		Long-term bonds (20 year)		Long-term bonds (35 year)	
	Canada a/	Spread over U.S. b/	Canada c/	Spread over U.S. d/	Canada e/	Spread over U.S. f/	Canada g/	Spread over U.S. h/
1962-High	5.74	2.84	5.20	1.29	5.48	1.45	5.19	1.10
Low	3.18	0.19	4.04	0.03	4.73	0.73	4.81	0.82
1962-June 6	3.83	1.10	4.31	0.64	4.95	1.10	4.94	0.98
July 19	5.74	2.59	5.11	1.16	5.48	1.44	5.15	1.03
Sept. 26	5.20	2.29	5.08	1.33	5.36	1.44	5.19	1.24
Oct. 17	4.36	1.52	4.56	0.89	5.00	1.13	5.10	1.18
31	4.30	1.50	4.56	0.96	5.04	1.19	5.12	1.23
Nov. 7	4.21	1.33	4.53	1.00	5.03	1.19	5.12	1.25
14	3.74	0.89	4.27	0.73	4.88	1.02	5.03	1.15
21	3.96	1.05	4.42	0.84	5.01	1.14	5.06	1.17
28	3.83	0.88	4.38	0.80	5.04	1.17	5.07	1.17
Dec. 5	3.94	1.03	4.43	0.83	5.06	1.16	5.09	1.17

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.

Chart 1

INTEREST ARBITRAGE, UNITED STATES / CANADA

Thursday figures

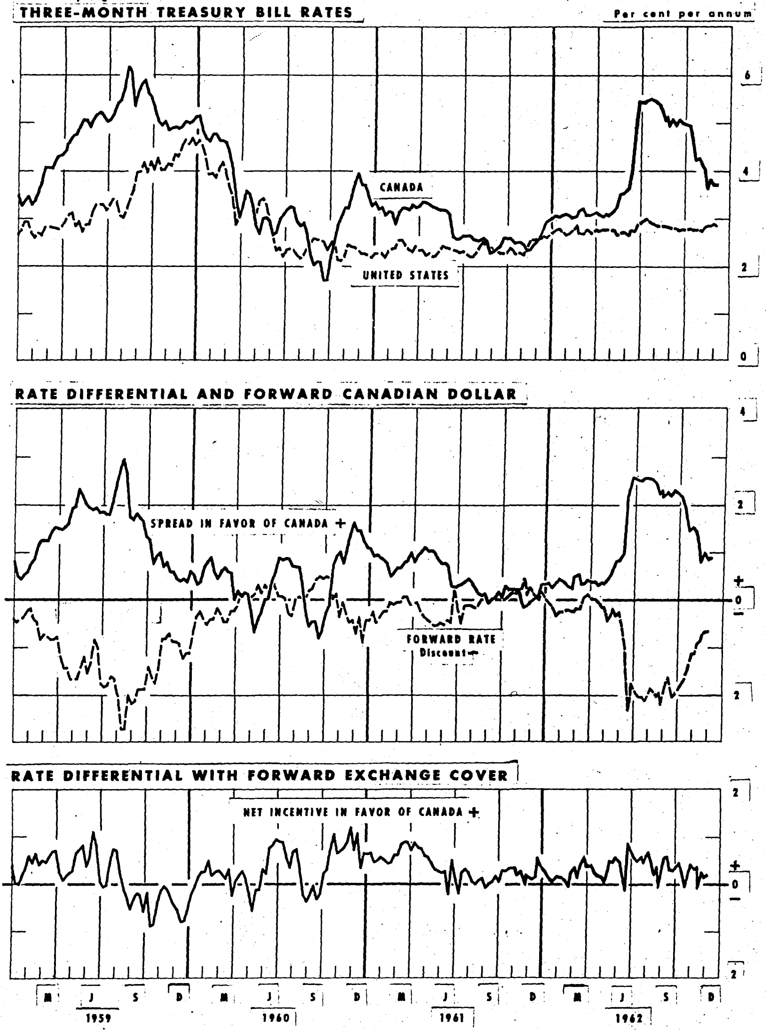


Chart 2
INTEREST ARBITRAGE, NEW YORK/LONDON

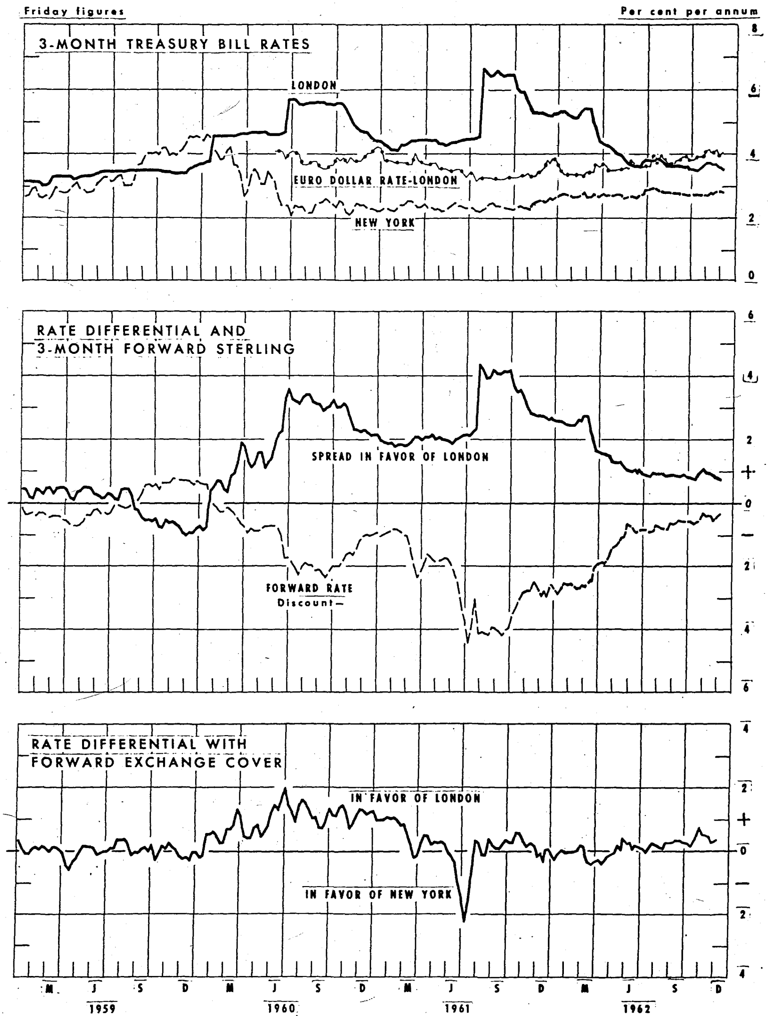
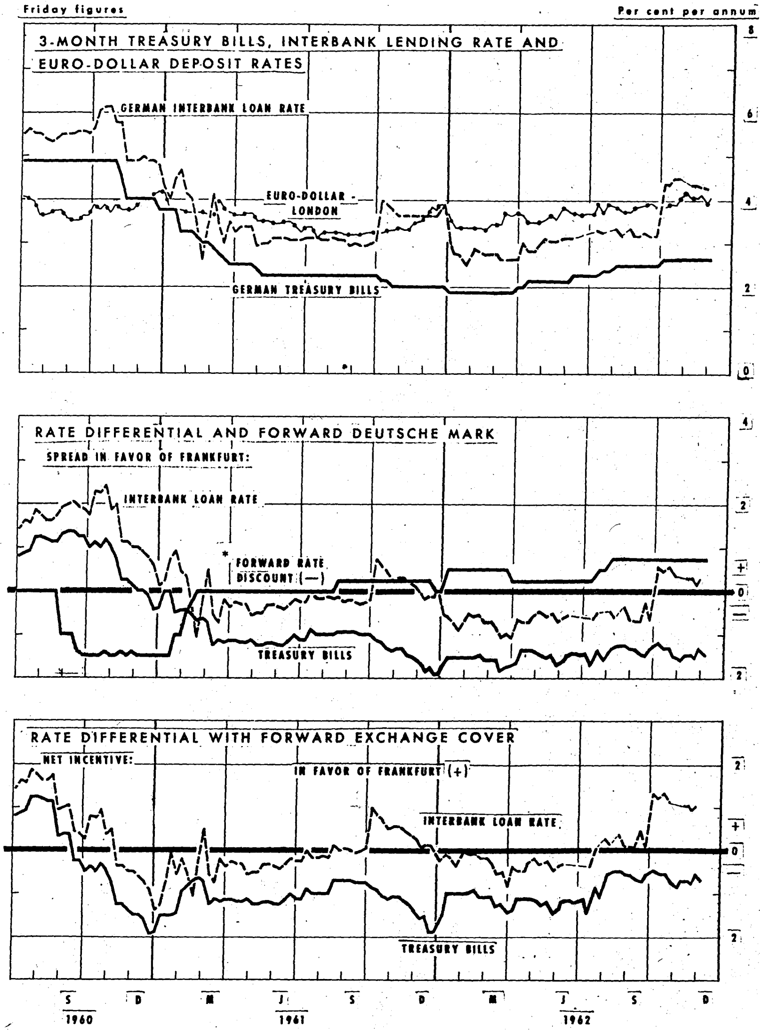


Chart 3

INTEREST ARBITRAGE FOR GERMAN COMMERCIAL BANKS



Note: Special forward rate available to German commercial banks.

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Chart 4

INTEREST ARBITRAGE, FRANKFURT / LONDON

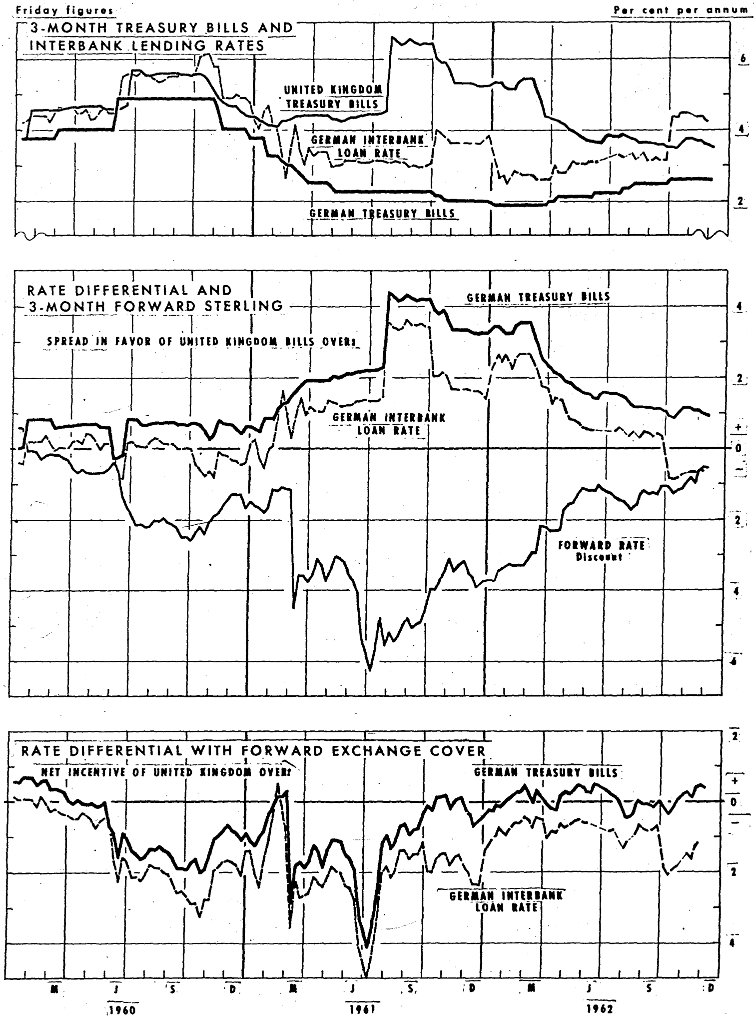
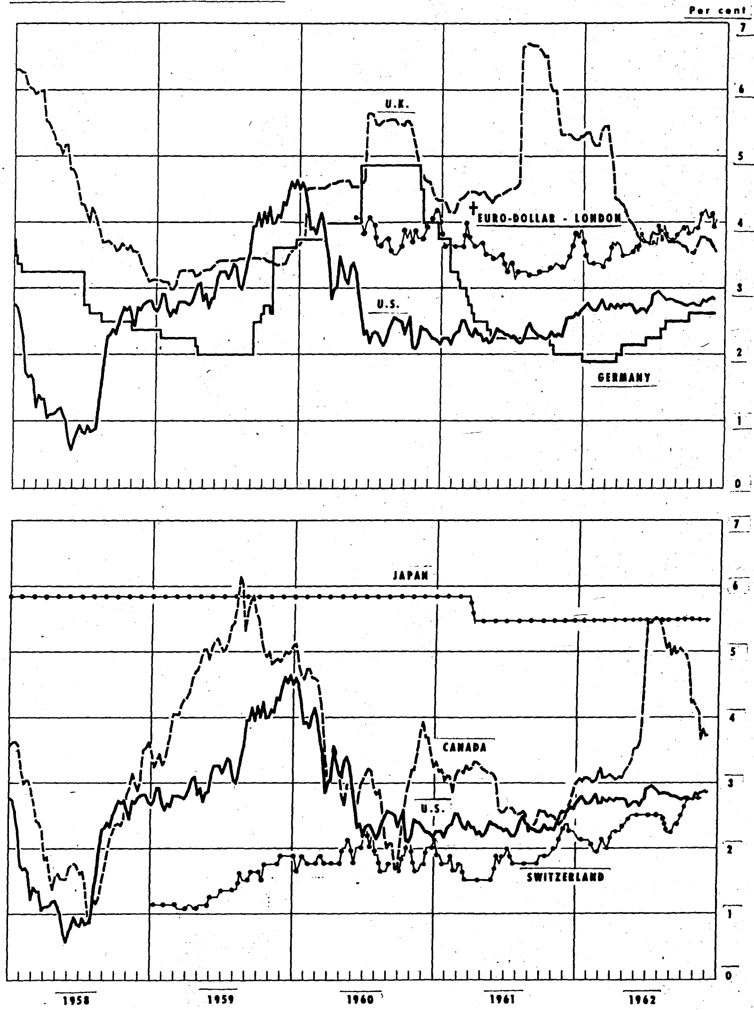


Chart 5

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

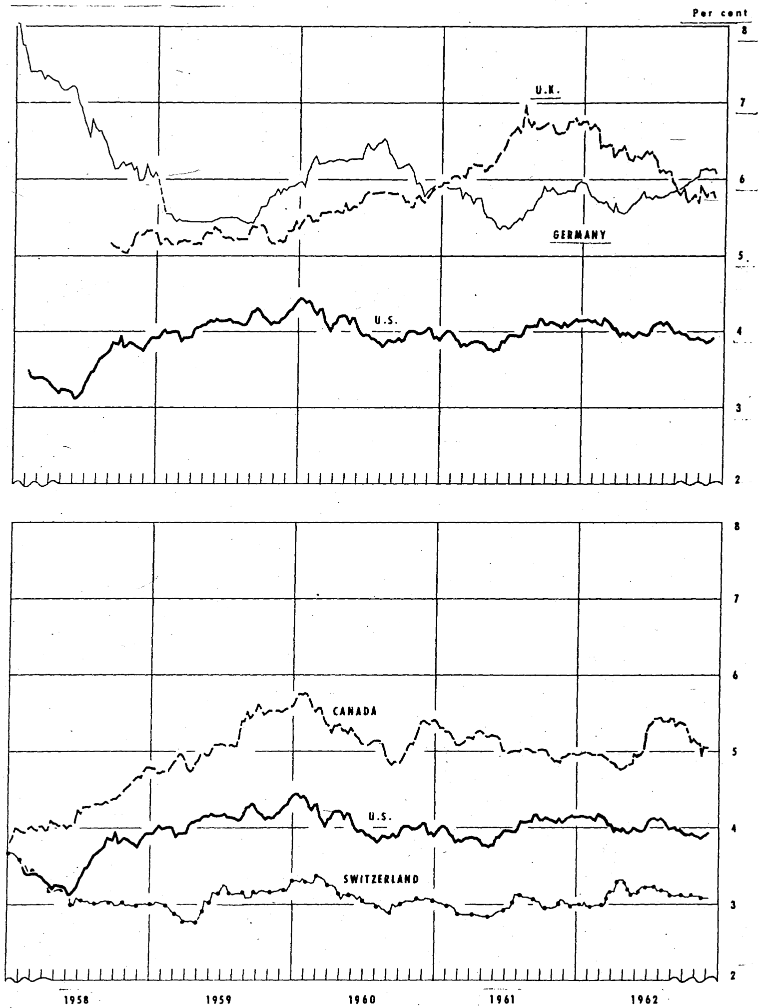
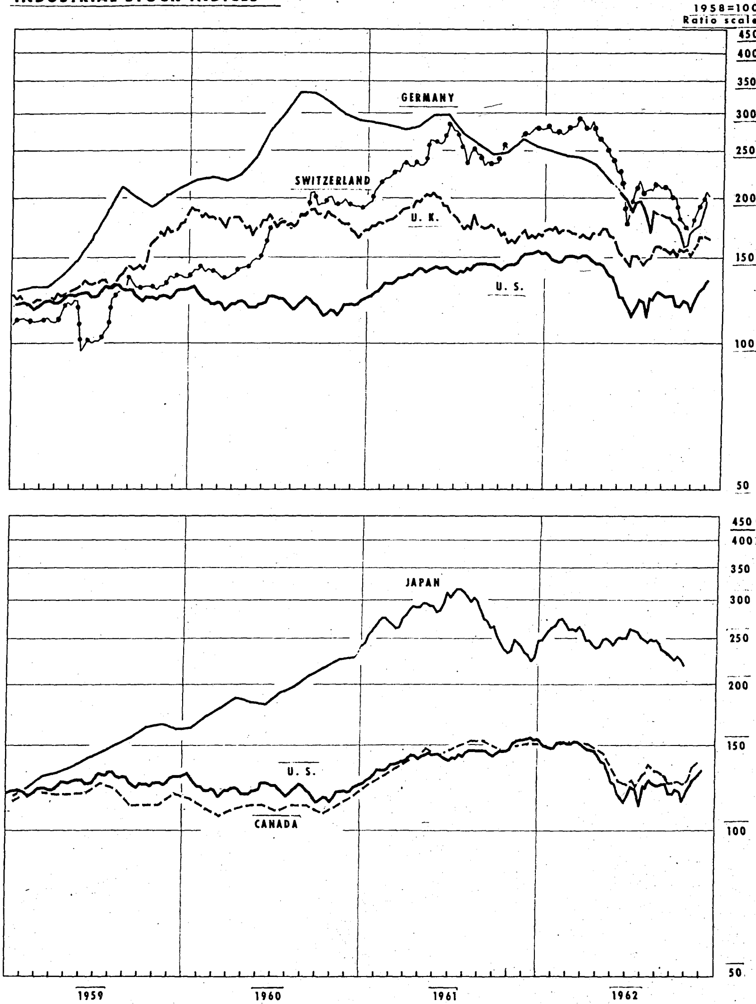


Chart 7

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

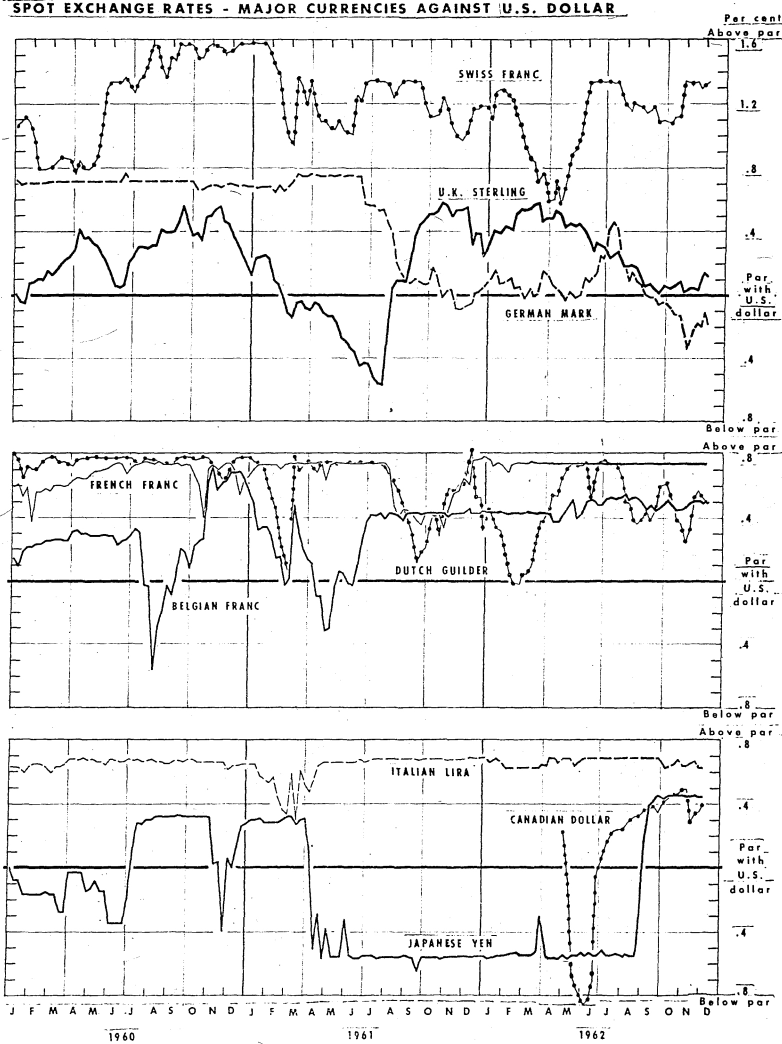

Chart 9

3-MONTH FORWARD EXCHANGE RATES