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CAPITAL MARKET DEVELOPMENTS ABROAD

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FEDERAL RESERVE BANK
OF RICHMOND

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

I. Germany: Money and Capital Markets in December 1962

Despite an admonition from the Bundesbank that the traditional year-end practice of window-dressing was "undesirable," the commercial banks shifted substantial funds into Germany during December and then proceeded to rebuild money-market holdings abroad in early January. The banks reportedly also borrowed funds abroad both to improve their liquidity ratios and to raise their balance-sheet total assets and liabilities. Perhaps as much as \$100 million was repatriated from abroad in the first half of December alone.

The Frankfurt money market experienced continuing demand for funds as the year-end approached. Day-to-day loan rates climbed steadily from about 2 - 3-1/8 per cent in late November to 3 - 4 per cent in late December and year-end money was quoted at 5-1/2 - 6 per cent. Rates on 3-month inter-bank loans remained at between 4-1/4 and 4-1/2 per cent during November and December.

In early January, funds were shifted to the Euro-dollar market in London: on January 4, for example, the spread in favor of Euro-dollar deposits over inter-bank loans in Frankfurt was 0.85 per cent (see Table 5 and Chart 5) and forward cover was available in the market at only 0.40 per cent (see Table 5). Large reserve declines reported by the Bundesbank in early January indicated that the German banks were moving substantial funds back into the Euro-dollar market. On January 7 the Bundesbank increased its charge for forward cover to the banks from 0.50 to 0.75 per cent, but the market rate remained at 0.40 per cent. However, a sharp drop in Euro-dollar rates in the week of January 7-11 materially reduced the incentives to continue to shift funds to London.

The tone of the bond market improved during the latter part of December and yields on long-term fixed-interest securities eased below 6 per cent for the first time in six months. The 5-1/2 per cent Railway bond dropped from 6.14 per cent at the end of November to 5.97 per cent in the second week in January. By the end of December, some recent industrial issues were no longer being quoted at below-par prices.

The strengthening of the bond market in part reflected transfers of funds from the stock market where the stock price index declined from 174 on November 30 to 163 on December 19 and to 159 on January 15. In December, a DM 250 million Railways bond with a 6 per cent coupon was placed at par. In

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the first week in January, the authorities marketed a DM 400 million Federal loan at 6 per cent and took advantage of the improved conditions to lengthen the term to 15 years compared with a 10-year maturity on the preceding offering in early December.

In the light of the improved bond market, the Central Capital Market Committee has urged that new issues totalling \$1.2 billion be placed on the market in January and February to forestall a temporary drop in market yields below 6 per cent. At the beginning of 1961 and again in 1962, bond yields fell below 6 per cent and market volume was adversely affected.

It is estimated that perhaps 40 per cent of the Federal loan in January was taken up by foreign investors. The latest German balance-of-payments statistics show only a modest net inflow of funds into German securities during October and November. Net security transactions (in millions of D-marks) in 1962 were:

	Jan.- <u>Mar.</u>	Apr.- <u>June</u>	July <u>Sept.</u>	<u>Oct.</u>	<u>Nov.</u>
German securities purchased by foreigners(net)	523	198	358) 107	102
Foreign securities purchased(-) by Germans (net)	<u>-340</u>	<u>-168</u>	<u>- 23</u>)	---
Net inflow of capital to German securities market	183	30	335	<u>a/107</u>	<u>a/102</u>

a/ Includes also other net private capital.

The Federal Government has announced it will float a DM 250 million loan in 1963 to fulfill its obligations in the area of development aid. Secretary of State Vialon voiced the government's hope of placing part of this issue on foreign markets. In December, Germany announced a DM 470 million loan to India to be used to finance Indian industrial projects.

Money market. Money market conditions were easy in November but tightened continuously throughout December as the year-end approached. (See Tables 1 and 5). The monetary ease in November is ascribed to the reduced shift of funds by commercial banks to money markets abroad. In December, interest rates moved up as the commercial banks built up their liquidity positions in preparation for year-end window-dressing operations. Money was also tight because of an unusual public demand for cash in anticipation of the December 31 property tax assessment date. Under the law, bank deposits are included in personal property and the assessed values are effective for the next three years. (See: Frankfurter Allgemeine Zeitung, December 20, 1962, p. 11.) In December, the commercial banks were also making call loans to the Euro-dollar market at the same time as funds were being brought in from abroad because rates on U.S. dollar deposits in London were so attractive. (See Table 5.)

On December 7, the Bundesbank increased its buying price of commercial paper to the level of its selling price not only to discourage commercial banks from borrowing funds on foreign money markets but also to ease credit conditions at home.

Table 1. Money Market Rates in Frankfurt, November and December
(in per cent per annum)

	<u>Day-to-day money</u>	<u>Three month loans</u>
Nov. 1-7	2-3/4 - 3	4-1/4 - 4-1/2
8-15	2-1/4 - 2-3/4	4-3/8
16-23	2-1/8 - 3	4-1/4 - 4-3/8
24-30	2 - 3-1/8	4-1/4
Dec. 1-7	3 - 3-1/8	4-1/4 - 4-3/8
8-15	3 - 3-1/8	4-1/4 - 4-3/8
16-23	3-1/8 - 4	4-1/4
24-28	3 - 4	4-3/8 - 4-1/2
End of year money	5-1/2 - 6	---

Bond market. The German bond market strengthened during the last half of December and the first half of January. (See Chart 6.) The climate of the market definitely improved during the month of December. Until mid-December medium-term, non-bonded loans ("Schuldscheindarlehen") bearing 6-1/4 per cent interest per annum could not be placed above 98 per cent of par; after mid-December such loans were being placed at 99 per cent of par and yields were reported to be comfortably below the mid-November level of 6.5 per cent. (See Chart 6.) Banks are generally satisfied with the 1962 trade in these medium-term notes. The market was more orderly in 1962 than in 1961 because the very large industries who disrupted the market with bond issues in 1961 secured a greater part of their financing on the stock exchange, leaving the Schuldschein market to the traditional customers: municipalities, small and medium-sized firms, and certain branches of the Federal Government.

Yields on long-term fixed-interest bearing securities eased below 6 per cent for the first time in six months. The 5-1/2 per cent Railway Bond issue dropped 17 basis points from the end of November to the second week in January to 5.97 per cent. By the end of December some recent industrial issues were being quoted above par in contrast to the below-par quotations of recent months. (See Table 6.)

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	Oct.	Nov.
"Occasional" borrowers' bonds:									
Industrial	39	16	--	50	112	72	113	40	139
Public authority	441	78	84	79	314	136	358	309	1
Foreign issuers	--	--	4	--	32	--	--	--	--
Other bonds a/	101	117	53	84	89	132	154	48	79
Total	581	211	141	213	547	340	625	397	219
Mortgage and communal bonds	526	525	464	503	665	453	532	471	406
Total gross bond placements b/	1,107	736	605	716	1,212	793	1,157	868	625
Gross share placements	354	263	352	130	185	205	172	121	143
Total security placements at issue value	1,461	999	957	846	1,397	998	1,329	989	768
a/ Mostly bonds of specialized credit institutions, especially in 1961.									
b/ Includes medium-term notes (Kassenobligationen).									

During 1962, sales of fixed-interest bearing securities on the German capital market totaled more than DM 12 billion, an increase of 25 per cent or approximately DM 2.4 billion more than the 1961 total. The Bundesbank estimates that the issue of interest-bearing securities financed 22 or 23 per cent of total new investment in 1962.

The recent strengthening of the bond market has been due in part to the transfer of funds from the stock market. Considerable support has been lent by large-scale purchases of recent flotations by foreigners who have been attracted by the high returns on German securities; in Europe, Austrian securities alone offer a higher rate of return on investment.

The Central Capital Market Committee has decided to hold the interest rate at the 6 per cent level. In both 1961 and 1962 the rate fell below 6 per cent early in the year only to suffer a setback in the spring which adversely affected market volume for months. To support the 6 per cent interest rate, the Central Committee is urging new "occasional" borrowers' issues totaling DM 1.2 billion onto the market during January and February. This total includes flotations of DM 800 million by public authorities and DM 400 million of industrial issues.

In the first week in January, a 6 per cent DM 400 million Federal loan was immediately oversubscribed. The government took advantage of the improved market conditions to lengthen the time to maturity to 15 years.

In October and December the government had been forced to shorten to 10 years the time to maturity to insure full subscription of issues at par under the then existing market conditions. Redemption is scheduled to begin after the fifth year and the loan is non-recallable for ten years. Foreign investors subscribed 40 per cent of the issue.

Stock market. Prices on the German stock market rose steadily during November and by the beginning of December the Frankfurter Allgemeine general index stood 30 per cent above the October 12th low point of 132. (See Chart 7.) The rise in stock price index came to a halt on November 30 at 174, as end-of-year sales necessitated by tax payments and bank liquidity requirements depressed the market. The stock index slipped gradually to 163 on December 19; after recovering slightly during the remainder of the month, it continued to weaken to 159 on January 15, despite the strengthening of prices on Wall Street. Rumors of a tax increase, although officially denied, and an assertion by unions that they intend to pursue a more aggressive wage policy in 1963 are said to have caused investors to withdraw from the market. Trading has taken place on a thin market.

German foreign trade. Because of an unusual bulge in military imports, the seasonally-adjusted German trade surplus fell abruptly from \$115 million in October to \$27 million in November. The resulting trade surplus of \$27 million is the smallest on record this year. (See Table 3.)

Table 3. German Foreign Trade
(seasonally adjusted, monthly averages in millions of U.S. dollars)

	1961				1962					
	<u>I</u>	<u>II</u>	<u>III</u>	<u>IV</u>	<u>I</u>		<u>II</u>	<u>III</u>	<u>Oct.</u>	<u>Nov.</u> p/
					<u>Old Series</u>	<u>New Series</u>				
Exports	1037	1071	1085	1052	1083	1083	1105	1123	1109	1115
Imports	864	917	918	947	936	a/999	1024	1032	994	1088
Surplus	173	154	167	105	147	84	81	91	115	27

p/ Preliminary

a/ Change in import accounting procedure. As of April 1962 retroactive to January 1, goods entering and those already stored in bonded warehouses recorded as imports in contrast to old procedure of recording goods as imports upon their departure from bonded warehouses.

Had military imports been maintained at normal levels (an average of \$40 million in recent months), the November surplus would have been in line with those of September and October. Trade results for the first eleven months of 1962 show exports to be 4.2 per cent higher than in the comparable period of 1961; the increase in imports was approximately 11.3 per cent after adjustment for special statistical factors (see note to Table 3).

Foreign exchange reserves. Bundesbank gross gold and foreign exchange reserves rose \$82 million in October and the foreign exchange assets of the German commercial banks increased \$32 million during the month so that the combined reserve gain for October totaled \$114 million (See Table 4.) The flow of funds was reversed in November, when Bundesbank reserves fell \$80 million. This decline was partially offset by a gain of \$17 million in commercial bank foreign exchange reserves but combined reserves registered a loss of \$62 million for the month of November.

Table 4. German Foreign Exchange Reserves
(in millions of U.S. dollars)

	1961		1962						
	III	IV	I	II	III	Oct.	Nov.	Dec.	Jan. 15
Bundesbank	-570	+ 68	-163	+48	+240	+ 82	-80	7-12	7-144
Commercial banks a/	- 74	-427	+601	-89	-208	+ 32	+17	n.a.	n.a.
Total	-644	-359	+138	-40	+ 32	+114	-62	n.a.	n.a.

a/ Balances with foreign banks and money market investments abroad.

b/ Not completely comparable to data for earlier period due to differences of valuation.

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 Bond Yields
- 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 5. Germany: Selected Money Market Yields and Exchange Rates
(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. bank ^{a/}	Market	U.K.	Ger.	U.S.
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. 26	4.13	4.50	-0.37	+0.50	+0.75	3.78	2.63	2.73
Nov. 23	4.13	4.31	-0.18	+0.50	+0.10	3.66	2.63	2.84
Dec. 7	4.06	4.31	-0.25	+0.50	n.a.	3.56	2.63	2.84
14	4.31	4.31	0.00	+0.50	-0.20	3.53	2.63	2.85
21	4.13	4.25	-0.12	+0.50	-1.20	3.53	2.63	2.88
28	4.13	4.44	-0.31	+0.50	+0.50	3.66	2.63	2.93
1963-Jan. 4	3.97	3.12	+0.85	+0.50	+0.40	3.50	2.63	2.90
11	3.60	3.12	+0.57	+0.75	+0.40	3.41	2.63	2.89

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

Table 6. 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.	7.50	3.50	2.75	6.0	6.2	3.89	2.1
Nov.	7.50	3.50	2.75	6.1	6.2	3.34	2.8
Dec.	7.50	3.50	2.75	6.1	n.a.	n.a.	n.a.

a/ Approved credits on current account.

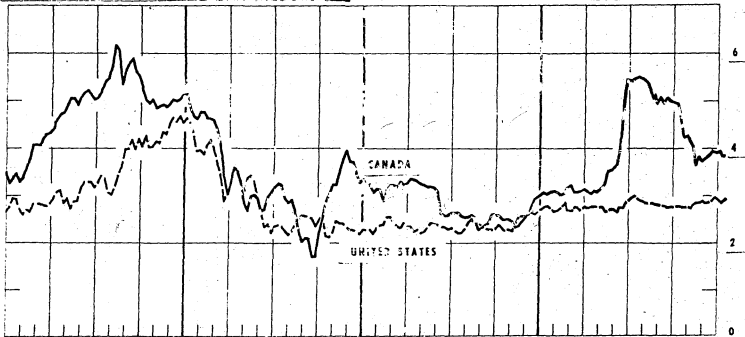
Chart 1

INTEREST ARBITRAGE, UNITED STATES / CANADA

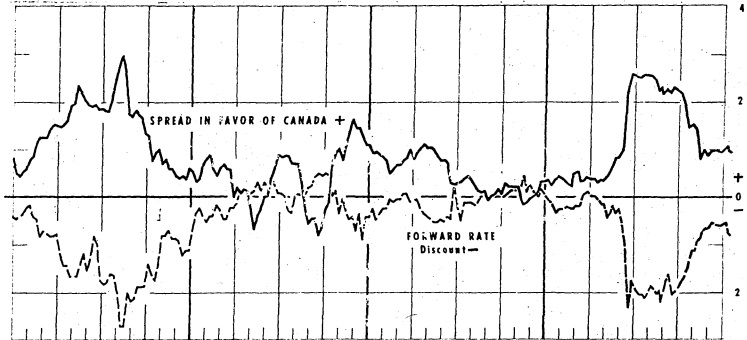
Thursday figures

THREE-MONTH TREASURY BILL RATES

Per cent per annum



RATE DIFFERENTIAL AND FORWARD CANADIAN DOLLAR



RATE DIFFERENTIAL WITH FORWARD EXCHANGE COVER

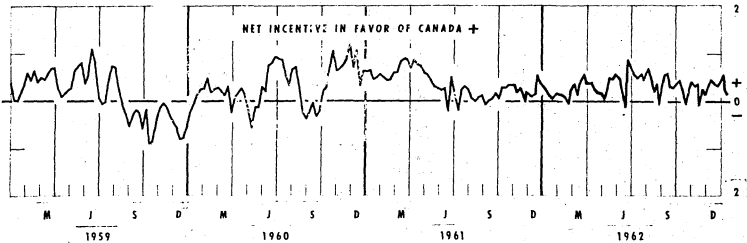


Chart 2

INTEREST ARBITRAGE, NEW YORK/LONDON

Friday figures

Per cent per annum

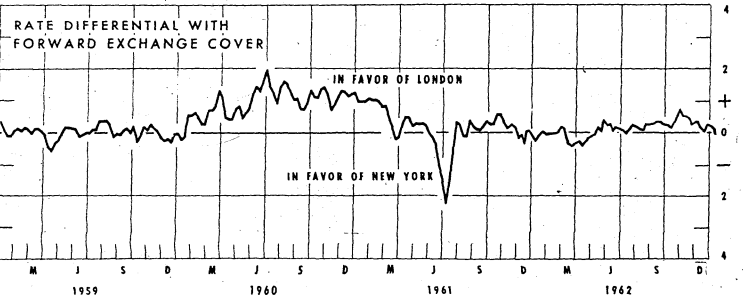
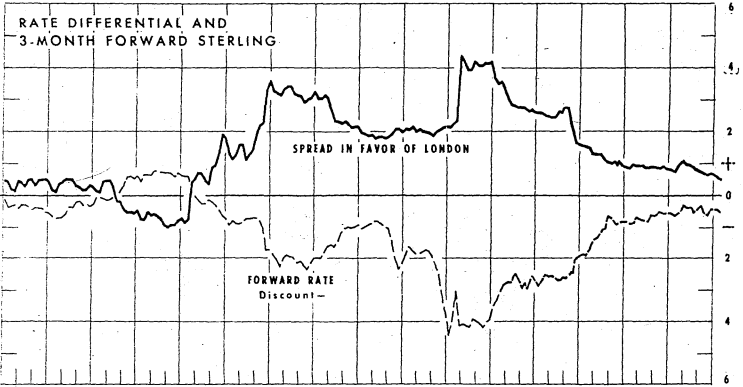
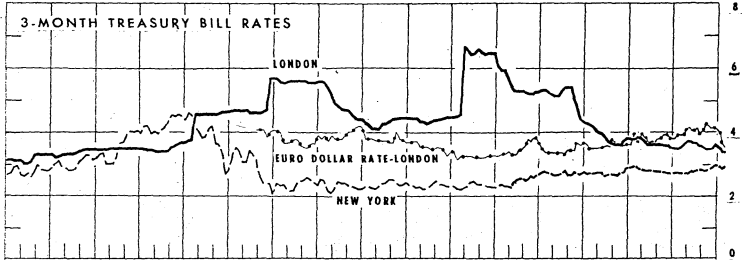
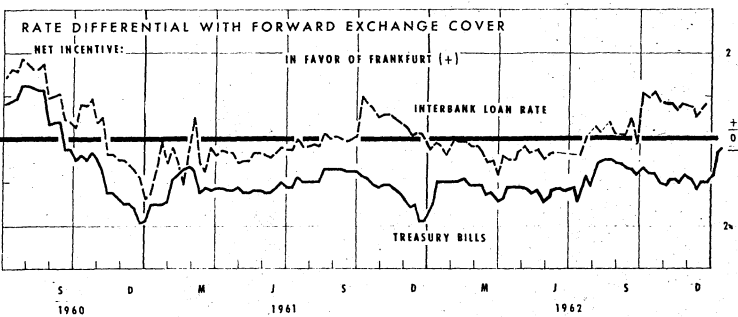
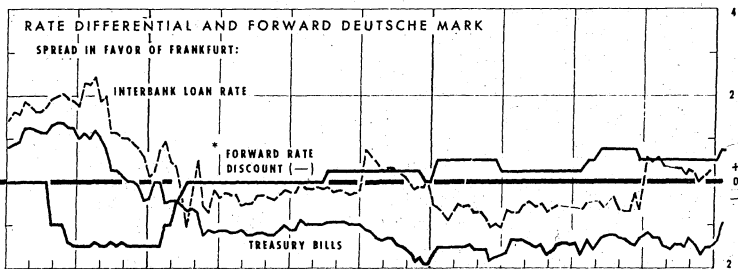
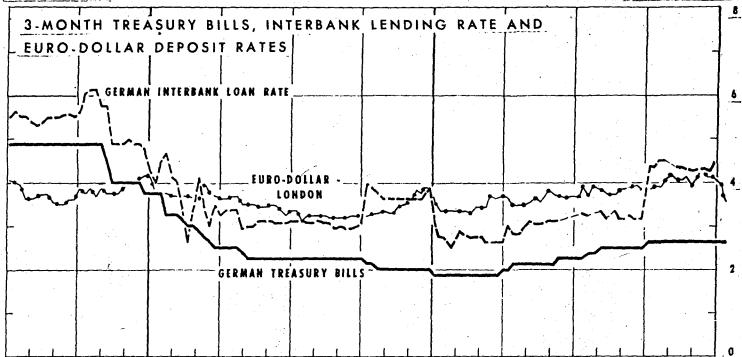


Chart 3

INTEREST ARBITRAGE FOR GERMAN COMMERCIAL BANKS

Friday figures

Per cent per annum



Notes: Special forward rate available to German commercial banks

INTEREST ARBITRAGE, FRANKFURT / LONDON

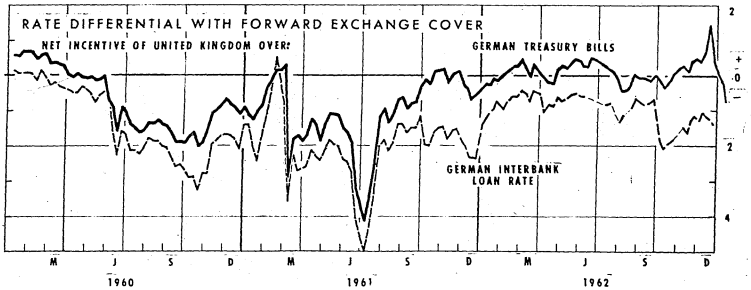
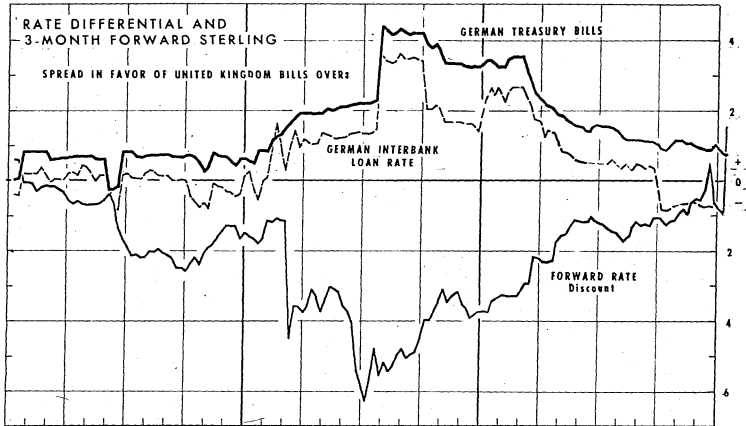
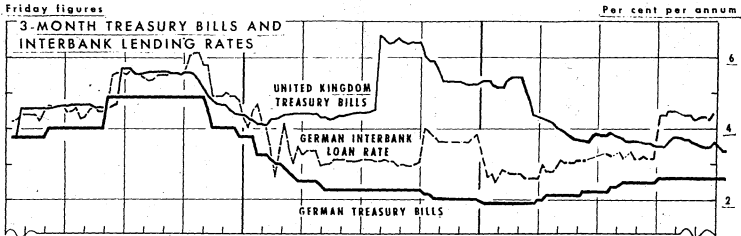
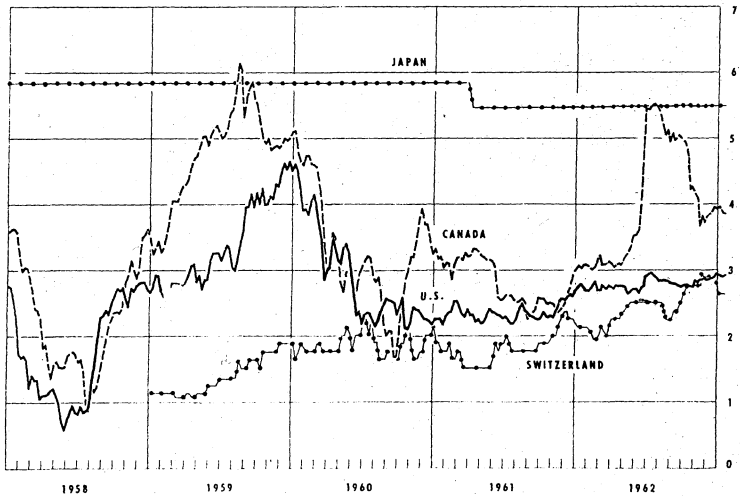
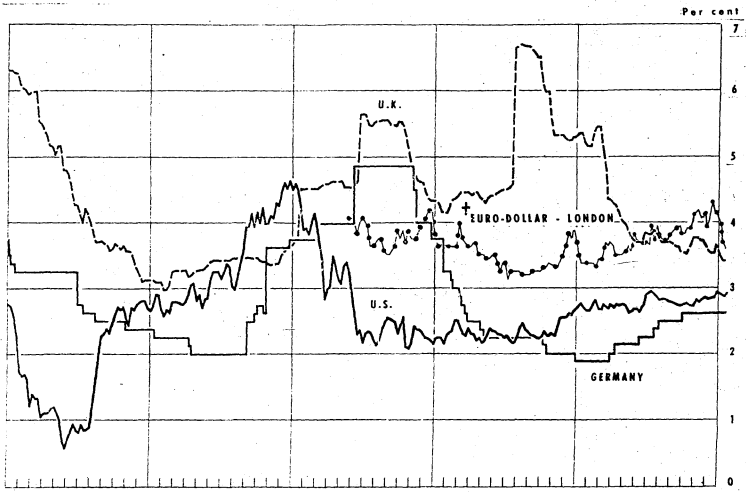


Chart 5
SHORT-TERM INTEREST RATES *



* 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

Chart 6

LONG-TERM BOND YIELDS

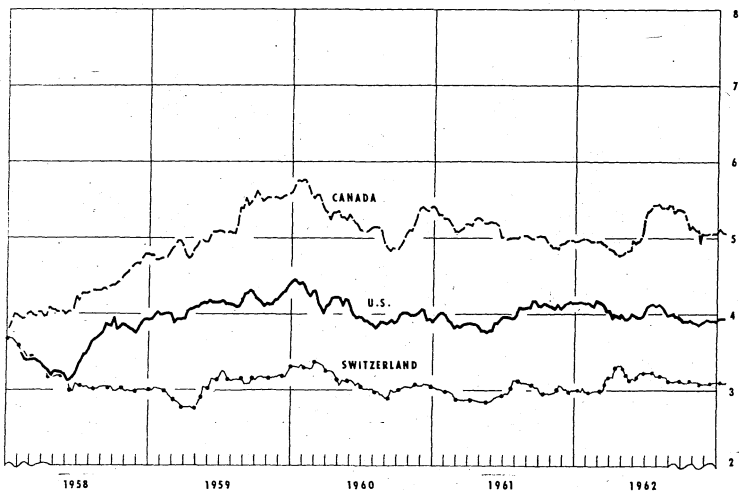
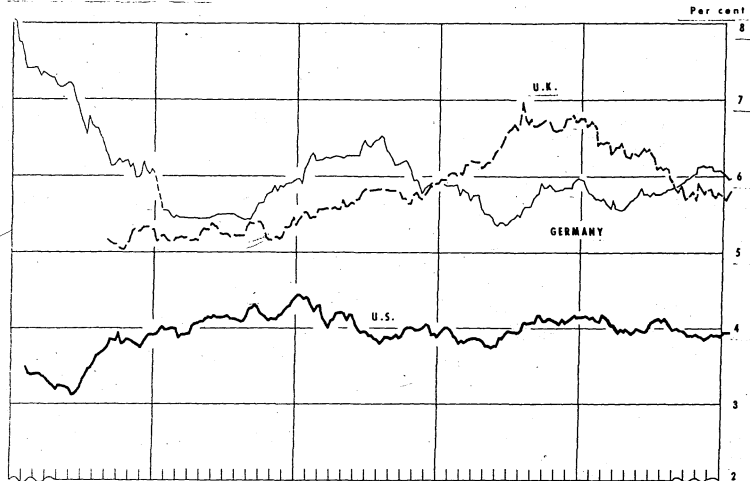
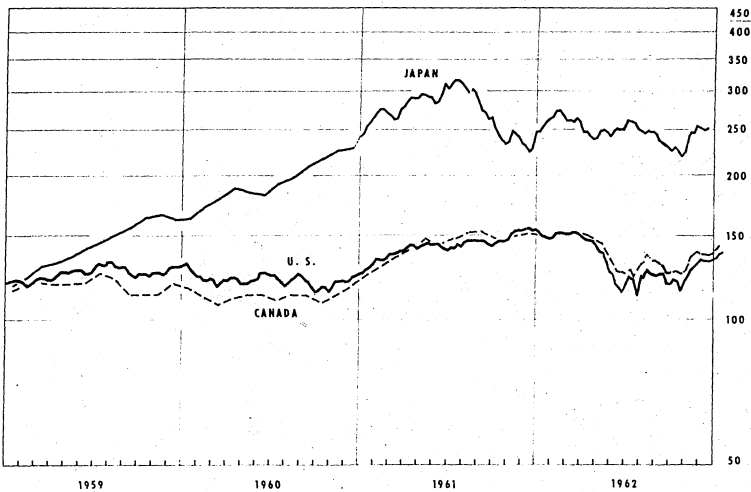
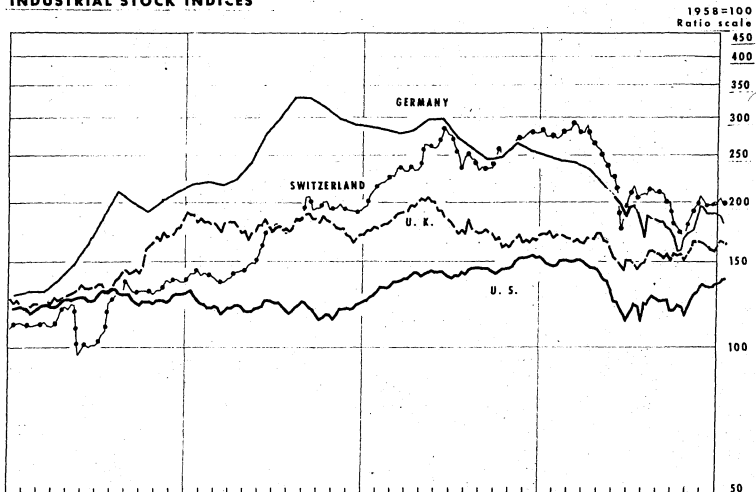


Chart 7

INDUSTRIAL STOCK INDICES*



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

Chart 8

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

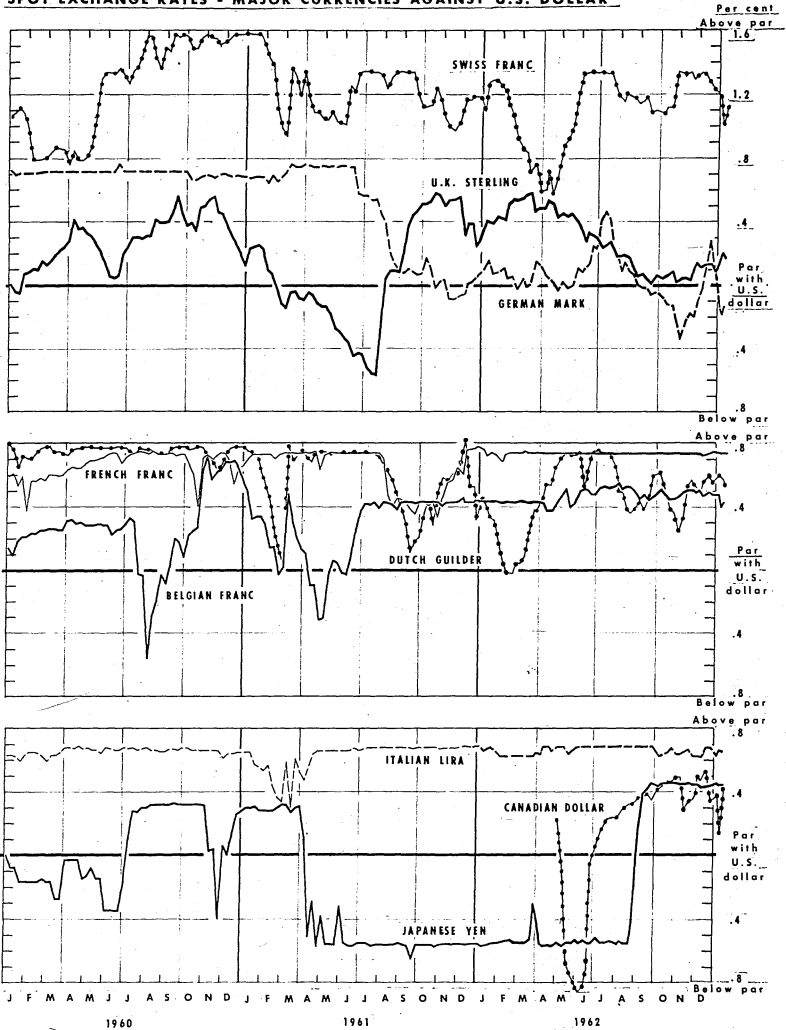


Chart 9

3-MONTH FORWARD EXCHANGE RATES

