

H. 13

No. 138

February 19, 1964.

CAPITAL MARKET DEVELOPMENTS ABROAD

- I. United Kingdom
 II. Nine Charts on Financial Markets Abroad

I. United Kingdom: Money and Capital Markets in January

Electoral uncertainties and concern about external payments strains had progressively unsettling effects on British financial markets during the period under review. During January, primarily in response to domestic political considerations, stock prices broke sharply and the discount on forward sterling widened. (See Table 1.) During February, unsettled conditions developed in several other financial markets as a result of growing concern about Britain's international payments position.

Table 1. United Kingdom: Selected Financial Statistics,
November 1963-February 1964
 (in per cent per annum unless otherwise indicated)

	<u>November:</u>		<u>January:</u>		<u>February:</u>	
	<u>8</u>	<u>14</u>	<u>3</u>	<u>24</u>	<u>7</u>	<u>14</u>
<u>Security Yields</u>						
Treasury bills	3.61	3.61	3.61	3.61	3.64	3.64
Bonds: 1964	3.76	3.73	3.78	3.74	3.87	3.82
1965-75	4.98	5.14	5.28	5.22	5.13	5.29
2008-12	5.58	5.74	5.88	5.90	5.92	5.95
War Loan	5.66	5.83	5.95	5.99	6.03	6.05
Consols	5.53	5.71	5.77	5.85	5.88	5.91
<u>Stock Price Index</u>						
Industrials	344.6	342.6	351.0	331.8	329.3	335.9
<u>Exchange Rates:</u>						
Spot (U.S. cents)	279.77	279.80	279.73	279.79	279.78	a/ 279.64
Forward (3-month discount in per cent per annum)	-0.21	-0.22	-0.24	-0.35	-0.44	-0.45
<u>Fully-hedged U.K. money-market assets:</u>						
Treasury bill differential in favor of U.K.:	-0.13	-0.13	-0.14	-0.23	-0.29	-0.31
purchase deposits (actual yield)	3.98	4.00	4.00	3.85	3.90	3.85

Note: Bond yields are for Thursday, other quotations for Friday.

a/ Quotation for Tuesday, February 18.

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(Decontrolled after six months)

Early in February, the forward discount widened further and both short- and long-term market rates moved up. Stock prices recovered some lost ground. Expectations of rising imports and evidence of price and wage advances in Britain, which would require higher interest rates in Britain, electoral uncertainties, and talk about a possible revaluation of the D-mark provided the background against which conditions in financial markets tended to deteriorate. By mid-month, press comment about possible payments strains contributed to a fall in spot pounds from 279.75 on February 14 to 279.64 on February 18. The announcement of unfavorable foreign trade returns for January on February 18 added to pressures on the pound in foreign-exchange markets.

The gradual widening of the discount on forward pounds during the period under review (see Table 1) threatened to push up short-term rates in London. In early February, the Treasury bill rate rose by 3 basis points. The incentive in favor of U.S. Treasury bills over British bills increased from 14 to 23 basis points during January and to 31 basis points on February 14. This development created in financial markets the expectation that the Bank of England might soon find it necessary to raise Bank rate in order to prevent too substantial a shift of funds from London.

Bond yields were consolidated during January after sharp rises in November and December, but they began to rise further in early February. (See Table 1.) Between early November and mid-February, in fact, the rises in bond yields were (in percent per annum):

1965 - 15½	0.11	War Loans	+0.39
1968 - 16½	0.12	Consols	+0.38

Euro-dollar deposit rates in London declined from the mid-December peak of 4.62 per cent to 4.09 per cent in early February. (See Table 9.) Flotation of U.S. dollar bonds in London continued on a large scale: \$40 million in December, \$35 million in January and a further \$27 million in the first half of February. Some jobbers, who had planned to finance their purchases of the loan with funds acquired from the investment dollar market, were allowed to acquire the funds at the official spot rate in order to relieve the pressure on the investment dollar rate which had reached a peak premium of 17.73 per cent on January 28.

Credit has continued to expand in the past few months in order to finance the general expansion of business activity. The continued increase in personal consumption expenditures has resulted in both an increase in installment credit and an increase in bank advances to individuals. The available figures appear to confirm reports that the commercial banks in Britain are expanding loans to finance consumption expenditures (mostly secured by liens on consumer durables) at a more rapid rate than stores and finance companies.

Money market. In January the money market tightened as the Exchequer began to develop a net cash surplus on account of seasonal tax revenues. The Bank of England attempted to provide relief by purchasing Treasury bills in the market, and so the discount houses had to borrow a small amount only on one day (January 15) between January 2 through February 7. In spite of the Bank's efforts, however, in the latter part of January and in the first half of February the discount houses had to pay as much as 3-3/4 per cent for day-to-day loans from the clearing banks, whereas earlier in January even marginal funds could be obtained for less than 3 per cent.

Therefore, in the Treasury bill tender of January 31, the discount houses lowered their bid, forcing the tender rate up to 3.76 per cent. The tender rate remained at this level in the auctions of February 7 and 14; this was subsequently reflected in the market rates. (See Table 9 and Charts 3 and 5.) On February 8, the discount houses received only 9 per cent of the allotment, believed to be the smallest allocation since 1939. Aside from the seasonal high cost of borrowing from the banks, the main reason why the discount houses lowered their bid was that they did not anticipate much demand for bills from the London clearing banks, owing to the tightness of credit. Preceding the January 31 tender, the market's bid had been held constant in six successive auctions.

In the local authorities funds market, short-term rates fell sharply early in January as the strong demand for funds manifest in December eased. (See Table 9.) Towards the end of the end of January, rates were slightly up and remained firm in the first two weeks of February, perhaps in response to the rise in the Treasury bill rate. (See Table 9.) Local authorities' short-term rates were further strengthened as funds were shifted from London into the Paris Euro-sterling market.

Little money was available for local authority mortgages in January, owing to the high yields available in the gilt-edged market. However, in the first week of February, money was available for 5 to 15-year mortgages at 5-7/8 per cent (1/8 higher than the PWLB mortgage rates).

Interest rates offered by building societies will not be reduced in the next three months, according to the chairman of the Building Societies Association in a press conference on January 23.

Interest differentials between New York and London short-term money market assets widened sufficiently to cause some concern in London. (See Table 2.) The covered Treasury bill differential widened to 25-30 basis points in favor of New York in the latter part of January and early February because of the wider forward discount on sterling. However, the differential between Euro-dollar deposits in London and negotiable certificates of time deposit in New York declined in January after Euro-dollar rates fell from seasonal end-year levels. (See Table 9 and Chart 1.) The differential between London Euro-dollar deposits and covered local authorities deposits remained insignificant.

Table 2. U.S./U.K. Short-Term Money Market Yields and Yield Spreads
(In per cent per annum)

	1 9 6 3		1 9 6 4					Feb. 7
	Nov. 29	Dec. 27	January					
			3	10	17	24	31	
<u>TIME DEPOSITS (3-month)</u>								
U.S. dollar: <u>a/b/</u>								
N.Y. - Certf. deposit	3.82	3.86	3.86	3.92	3.92	3.92	3.88	3.84
London - Euro-\$	4.12	4.25	4.12	4.00	3.88	3.88	3.94	4.00
Sterling (covered)								
Local authorities	4.12	4.40	4.20	3.96	4.00	3.96	3.97	3.94
Finance Houses	4.10	4.08	4.00	3.75	3.75	3.85	3.85	3.90
<u>YIELD SPREADS (Favor U.K.)</u>								
Treasury bills (3-month) <u>c/</u>								
Uncovered	.14	.11	.10	.09	.09	.12	.13	.15
Covered	-.05	-.05	-.14	-.26	-.22	-.23	-.18	-.29
Euro-\$ - N.Y. C/D <u>a/</u>	.30	.76	.33	.09	.09	.09	.24	.16
Euro-\$ - Local Authority (covered)	--	.15	.08	-.04	.12	.08	.13	-.06

a/ Previous Wednesdays.

b/ Secondary market offering rates for negotiable time certificates of deposits.

c/ U.S. and U.K. bill rates are shown in Table 9. See also Chart 3.

Gilt-edged market. Yields on most Government securities rose by a few basis points in January as the market was generally weak. (See Table 10 and Chart 6.) The announcement on January 9 of a 10-year £15 million New Zealand Government loan weakened the gilt-edged market. At the end of the month the market was weakened further when the London County Council floated a £30 million loan during the same week that £10 million of new industrial bonds were issued: the underwriters had to retain 75 per cent of the L.C.C. issue.

On February 19, the Treasury offered a 16-year (1978-80) £400 million 5-1/4 per cent funding loan, mainly to replace the existing medium-term tap stock (a 5 per cent Exchequer stock 1976-78). In order to make this issue attractive to foreign investors, income tax will not be withheld from bonds owned by nonresidents. Also, bearer bonds will be made available after April 20 in denominations as small as £100.

\$60 million of dollar denominated loans were floated in London between January 1 and February 14, as compared \$50 million in December, alone. (See Table 3.) The underwriters of these loans have shown some concern about attracting short-term Euro-dollar funds. A large portion of the Norges Kommunalbank loan, for example, was placed directly with institutional investors in Britain and on the Continent who already possessed dollar balances obtained from previous sales of dollar securities.

However, the issue of these loans apparently has been partially responsible for the steady increase in the investment dollar premium from 8 per

cent in mid-October to 13-7/8 per cent on January 28. The Bank of England reportedly permitted jobbers to finance \$0.75 million of their purchases of the City of Oslo loan at the current spot rate in order to take some strain off the investment dollar market.

Table 3. U.S. Dollar Loans Floated in London

	Month	Borrower	Coupon	Maturity	Value (\$ mns.)
<u>1963</u>	December	Government of Belgium	5-1/4%	1966	20.0
	December	Canon Camera Co. (Japan)	6-1/4%	1988	5.0
	December	Takeda Chemical (Japan)	6%	1984	15.0
<u>1964</u>	January	Norges Kommunalbank	5-3/4%	1974-84	10.0
	January	Government of Austria	6%	1979-84	18.0
	January	Wolfson Clore Mayer Corp. (Israel)	6-1/2%	1983-88	5.0
	February	City of Oslo	5-3/4%	1979	15.0
	February	Copenhagen Telephone Co.	5-3/4%	1984	12.0

Stock market. The 18 month rise in stock prices broke in January. The Financial Times Industrial common stock price index fell from 352.4 on January 3 to 329.2 on January 24. (See Table 10 and Chart 7.) The market had discounted expected profits in the near future and, therefore, was vulnerable to the political and economic shocks received in January. The first bearish day in January followed the failure of employers and the T.U.C. to reach an agreement at the N.E.D.C. meeting on an interim declaration on incomes policy. Labor unrest in the steel industry and the political controversy over the ending of resale price maintenance led to further weakness in the market. The market also reached to a speech by Mr. Wilson that a new Labour Government would impose a more effective capital gains tax and would tax distributed profits at a higher rate than undistributed profits. In the first week of February, the market steadied.

London clearing banks. Credit extended to the public sector expanded in January in an amount roughly equal to that extended to the private sector in January, but the total expansion of credit was considerably less than in January 1963. (See Table 4.) Advances, other than to nationalized industries, fell below the level sustained in the fourth quarter of 1962 as far as can be determined from a provisional seasonally adjusted figure.

The banks' liquidity position is roughly the same as it was a year ago, four percentage points above the customary minimum, which was reduced officially last October from 30 per cent to 28 per cent.

Table 4. United Kingdom: London Clearing Banks' Net Deposits
and Selected Assets
(in millions of pounds)

	Changes: a/						Outstanding Jan. 15, 1964
	1962 Jan.	Sept.	1963 Oct. Nov. Dec.			1964 Jan.	
NET DEPOSITS	+127	+33	+91	+54	+54	+114	7,097
SELECTED ASSETS							
Claims on the Public Sector							
Government bonds	+ 28	+19	+21	+25	+ 4	+11	1,174
Treasury bills and loans to the Discount Market	+ 91	+78	+37	+28	+30	+30	1,582
Loans to nationalized industries	- 4	-13	+19	- 7	- 5	+ 8	73
Total	+115	+84	+77	+46	+29	+49	2,836
Claims on the Private Sector							
Advances (net)	+ 46	-44	- 1	+14	+ 5	+38	3,935
Other b/	- 13	+12	- 8	--	+ 2	+12	643
Total	+ 33	-32	- 7	+14	+ 7	+50	4,578
SEASONALLY ADJUSTED							
Advances (net)	+ 20	+22	+23	+39	+30	+13	--
Deposits (net)	+ 2	+31	+72	+84	+ 5	n.a.	--
LIQUIDITY RATIO	34.6	32.1	32.3	32.2	32.7	32.7	

a/ To the third Wednesday of the month, except in December when the change is to the second Wednesday.

b/ Includes commercial bills, call loans other than to the discount market, and other investments. c/ Estimate.

Source: Financial Statistics.

Installment credit. New credit extended in December changed no more than seasonally, according to The Board of Trade, sharply upwards for household goods shops and sharply downwards for finance houses. However, there was a net increase in credit outstanding of £7 million. (See Table 5.)

Table 5. United Kingdom: Installment Credit
(end of period)

	1961	1962	Year	1963			Outstanding Dec. 31, 1963
				Oct.	Nov.	Dec.	
New Credit Extended, Index of value (1957=100)							
Household goods shops	124	139	145	131	140	145	
Finance houses	96	94	129	175	157	129	
Credit Outstanding (£ mns.)							
Household goods shops	-16	+ 9	+22	+ 1	+ 5	+11	340
Finance houses	+ 8	-49	+45	+ 4	+ 3	- 4	614
Total	- 8	+10	+67	+ 5	+ 8	+ 7	954

Foreign exchange markets. The spot rate fluctuated within a narrow range from the first of the year through February 14, remaining between \$2.797 and \$2.788. (See Table 9 and Chart 8.) The discount on three-months forward sterling, however, widened steadily from 0.24 per cent per annum on January 3 to 0.45 per cent per annum on February 14. (See Table 9 and Chart 9.)

In recent weeks, attention has been focused on the investment dollar premium, which has risen from 8 per cent in mid-October to as high as 13 per cent at the end of January. As was mentioned earlier, part of the reason for this rise was the attempt of British residents to purchase some of the dollar securities currently being floated in London. However, this is just one of the several pressures being exerted on the rate. Of greatest significance is the drying up of the supply by making these funds available for direct investment abroad. These funds are never repaid to the pool, whereas funds acquired for the purchase of foreign securities eventually are returned when the securities mature or are liquidated.

Foreign trade. Exports in 1963 experienced one of the largest year-to-year increases since World War II. (See Table 6.) The expansion in value was 8 per cent; the growth in volume 5 per cent. The rate of growth slowed down in the last half of the year, although there was a sharp rise in December exports.

The main feature of imports in 1963 was the rapid increase of industrial materials imports after the second quarter. Consequently the trade deficit increased steadily during the year, rising by 35 per cent from the fourth quarter of 1962 to the fourth quarter of 1963.

In January, however, customs data show a sharp fall in exports. Imports also rose substantially, owing to the continued increase in industrial materials imports and to imports of sheet steel as a consequence of the strike in The Steel Company of Wales, Ltd. An average of the December 1963 and the January 1964 figures shows a very substantial deterioration in the "visible balance".

Gold and foreign exchange reserves. Reserves rose by \$17 million in January. (See Table 7.) This is considered to be very small in view of the fact that the current account of the balance of payments is seasonally strong in the first quarter of the year and that the net earnings of overseas sterling area countries from non-sterling countries are reported to be continuing.

Bullion market. The London gold market was quiet from January 2 through mid-February with the exception of the week of January 13-17, when demand varied from moderate to heavy. Following that week, when the fixing price rose to \$35.091 per fine ounce on January 16, the fixing price fell gradually to \$35.076 by February 14. (See Table 8.)

Table 6. United Kingdom: Foreign Trade
(millions of pounds; seasonally adjusted; monthly averages)

	1962		1963					1964	
	Year	Year	1st Qtr.	2nd Qtr.	3rd Qtr.	4th Qtr.	Dec. ^{a/} Jan.	Dec.	Jan.
Imports, c.i.f.	374	402	375	395	412	422	449	442	457
Exports, f.o.b.	316	340	327	335	346	348	344	361	326
Re-exports, f.o.b.	13	13	12	13	13	13	12	12	11
Trade Balance	-45	-49	-36	-47	-53	-61	-97	-69	-120
Visible balance ^{b/}	- 6	- 4	+ 7	- 2	- 9	-11	-42	-13	- 72

a/ An average of the December 1963 and the January 1964 export figures are shown, owing to the wide fluctuations in exports data in these two months.

b/ The customs returns are adjusted for valuation and coverage (for example, the revaluation of imports from a c.i.f. to an f.o.b. basis) to make them more closely comparable with the balance of payments estimates.

Table 7. United Kingdom: Reserve Position
(In millions of U.S. dollars)

	Changes:					1964 Jan.	Outstanding Jan. 31, 1964
	1963						
	1st Qtr.	2nd Qtr.	3rd Qtr.	4th Qtr.	Dec.		
A. Gold and convertible currencies	+ 8	-101	+22	-78	-115	+17	2,674
Less: Central bank loans	+250	-250	--	--	--	--	--
Less: U.S. opns. in sterling ^{a/}	+ 33	+ 18	-18	n.a.	n.a.	n.a.	--
Adjusted Reserves	-275	+131	+38	-78	-115	+17	--
B. Drawing rights on IMF	--	- 8	- 5	--	--	n.a.	^{b/} 2,439
Total	-275	+123	+33	-78	-115	+17	5,113

a/ As published in the Federal Reserve Bulletin, September 1963, pp. 1219-20.

b/ As of December 31, 1963.

Table 8. London Fixing Price for Gold, November 1963-February 1964
(In U.S. dollars per fine ounce)

November 29	35.078	December 27	35.077	January 24	35.084
December 6	35.085	January 3	35.072	31	35.078
13	35.081	10	35.069	February 7	35.078
20	35.084	17	35.087	14	35.076

European and British Commonwealth Section.

II. Nine Charts on Financial Markets Abroad

- Chart 1 - International Money Market Yields for U.S.
Dollar Investors
- Chart 2 - Interest Arbitrage, United States/Canada
- Chart 3 - Interest Arbitrage, New York/London
- Chart 4 - Interest Arbitrage for German Commercial Banks
- 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 9. United Kingdom: Treasury Bill Yields and Exchange Rates

	3-mo. Treasury bill arbitrage calculation					Spot pound (U.S. cents) ^{a/}	London deposit rates	
	U.K.	U.S.	Difference	3-mo. pound	In favor U.K. bill		U.S. dollar (3-mo.)	Local authority
1963								
High	3.58	3.32	.26	-.03	+.23	280.59	4.62	4.88
Low	3.31	2.85	.46	-1.08	-.62	279.59	3.56	4.06
1963								
Nov. 15	3.61	3.52	.09	-.22	-.13	279.80	4.12	4.25
22	3.61	3.48	.13	-.21	-.08	279.79	4.12	4.25
29	3.61	3.47	.14	-.19	-.05	279.70	4.12	4.31
Dec. 6	3.64	3.49	.15	-.19	-.04	279.65	4.44	4.31
13	3.61	3.49	.12	-.14	-.02	279.67	4.62	4.38
20	3.61	3.51	.10	-.16	-.06	279.65	4.62	4.88
27	3.61	3.50	.11	-.16	-.05	279.64	4.25	4.56
1964								
Jan. 3	3.61	3.51	.10	-.24	-.14	279.73	4.12	4.44
10	3.61	3.52	.09	-.35	-.26	279.87	4.00	4.31
17	3.61	3.52	.09	-.31	-.22	279.87	4.00	4.31
24	3.61	3.49	.12	-.35	-.23	279.79	4.00	4.31
31	3.61	3.48	.13	-.31	-.18	279.77	4.12	4.38
Feb. 7	3.64	3.49	.15	-.44	-.29	279.78	4.00	4.38
14	3.64	3.50	.14	-.45	-.31	279.74	4.00	4.38

a/ Certified N. Y. noon buying rate.

Table 10. United Kingdom: Selected Capital Market Yields

	U.K. Government bond yields					Share yield a/	Yield gap b/	Share prices a/
	4-1/2% 1964	3% 1965-75	5-1/2% 2008-12	3-1/2% War Loan	2-1/2% Consols			
1963								
High	4.05	5.44	6.00	6.12	5.98	5.42	--	347.7
Low	3.56	4.76	5.45	5.68	5.39	4.58	--	283.3
1963								
Nov. 14	3.73	5.14	5.74	5.83	5.71	4.61	1.10	342.6
21	3.76	5.26	5.75	5.84	5.68	4.66	1.02	339.5
28	3.66	5.16	5.81	5.85	5.70	4.61	1.09	343.5
Dec. 5	3.69	5.27	5.91	5.95	5.79	4.63	1.16	341.9
12	3.80	5.31	5.95	5.95	5.76	4.59	1.17	345.6
19	3.77	5.33	5.93	5.99	5.84	4.60	1.24	344.2
24	3.81	5.33	5.93	5.98	5.83	4.56	1.27	347.7
1964								
Jan. 2	3.78	5.28	5.88	5.95	5.77	4.52	1.25	351.0
9	3.73	5.30	5.88	6.00	5.86	4.63	1.23	343.8
16	3.79	5.22	5.93	5.96	5.81	4.77	1.04	333.9
23	3.74	5.22	5.90	5.99	5.85	4.81	1.04	331.8
30	3.80	5.26	5.93	6.00	5.86	4.87	1.01	329.4
Feb. 6	3.87	5.13	5.92	6.03	5.88	4.87	1.01	329.3
13	3.82	5.29	5.95	6.05	5.91	4.79	1.12	335.9

a/ Financial Times.

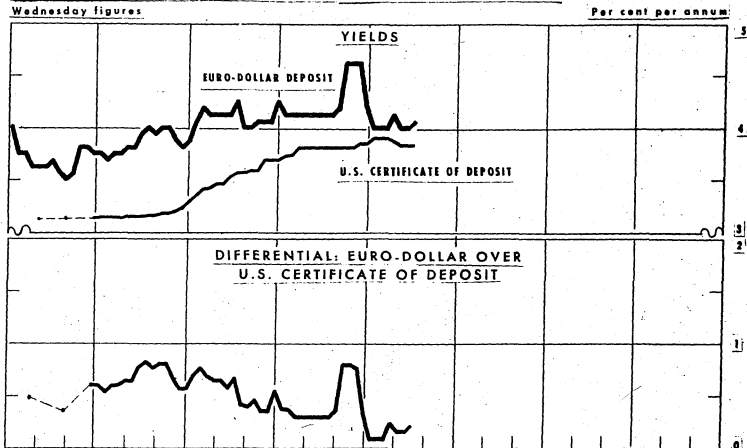
b/ Difference between yield on 2-1/2 per cent Consols and share yield.

Chart 1

INTERNATIONAL MONEY MARKET YIELDS FOR U.S. DOLLAR INVESTORS

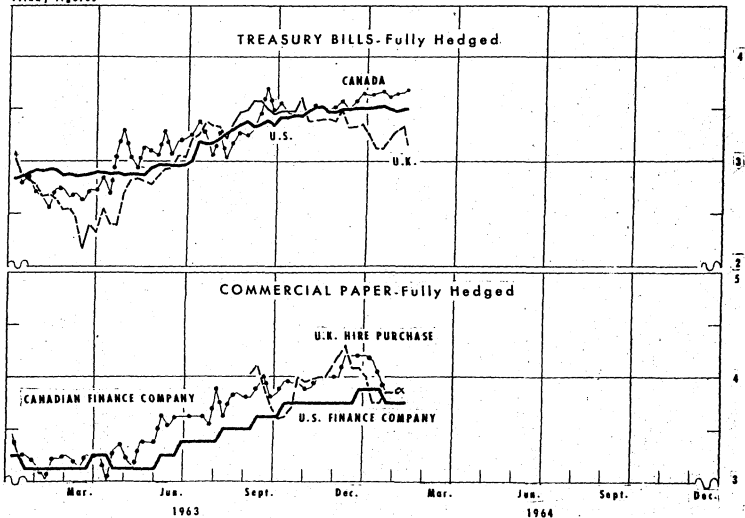
3-MONTH EURO-DOLLAR DEPOSIT VS. CERTIFICATE OF DEPOSIT

Wednesday figures



NEW YORK OFFER RATES ON SELECTED 3-MONTH INVESTMENTS

Friday figures



12

Chart 2

INTEREST ARBITRAGE, UNITED STATES / CANADA

Thursday figures

Per cent per annum

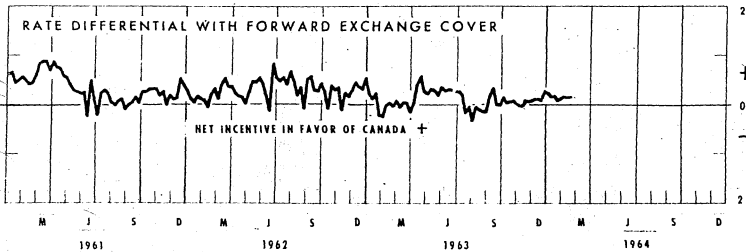
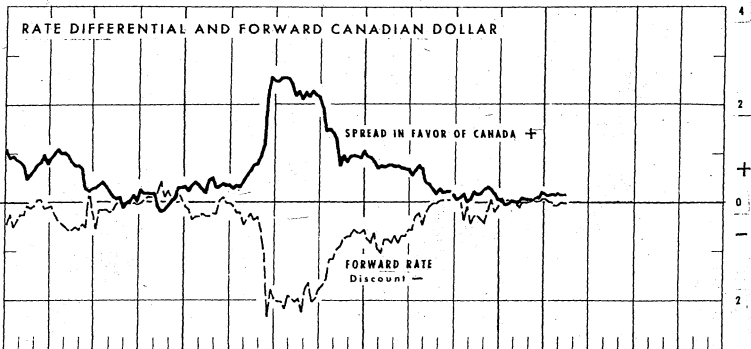
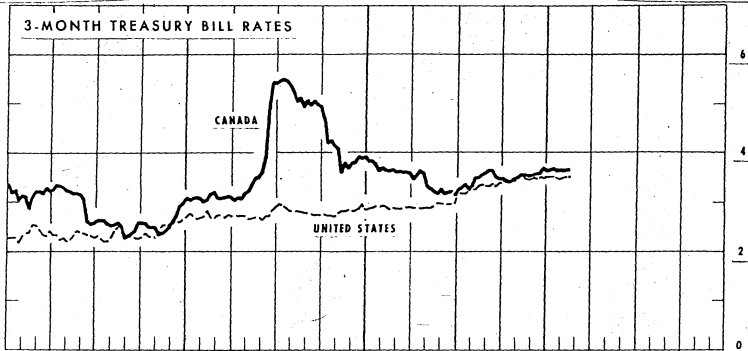


Chart 3
INTEREST ARBITRAGE, NEW YORK/LONDON
Friday figures

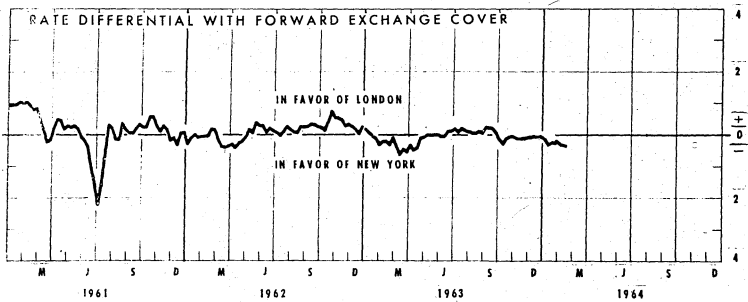
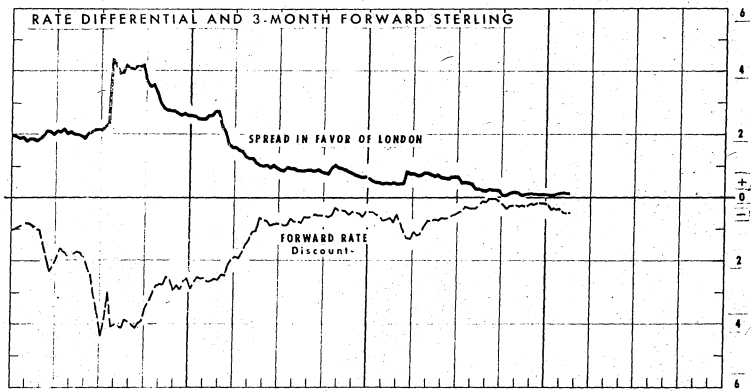
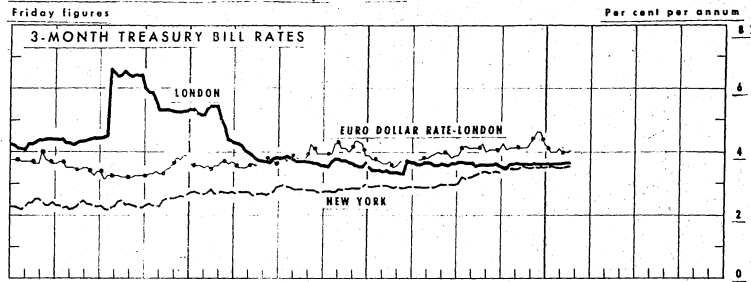


Chart 4
INTEREST ARBITRAGE FOR GERMAN COMMERCIAL BANKS

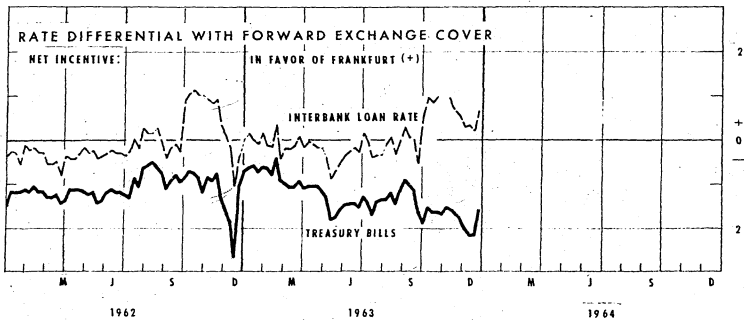
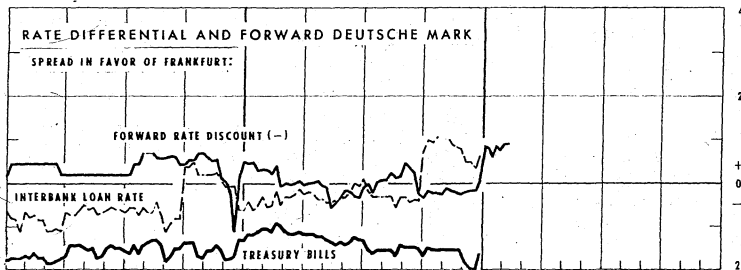
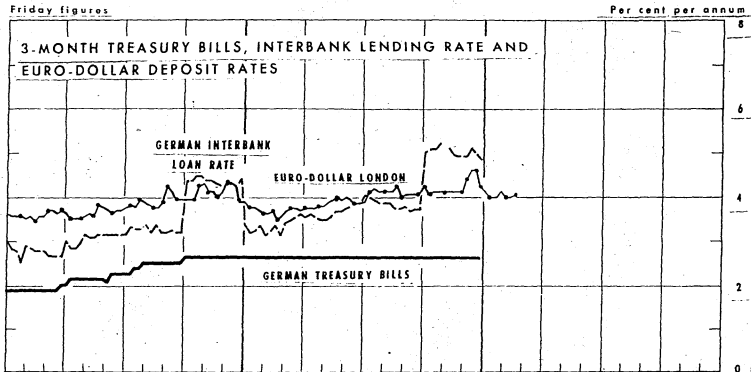
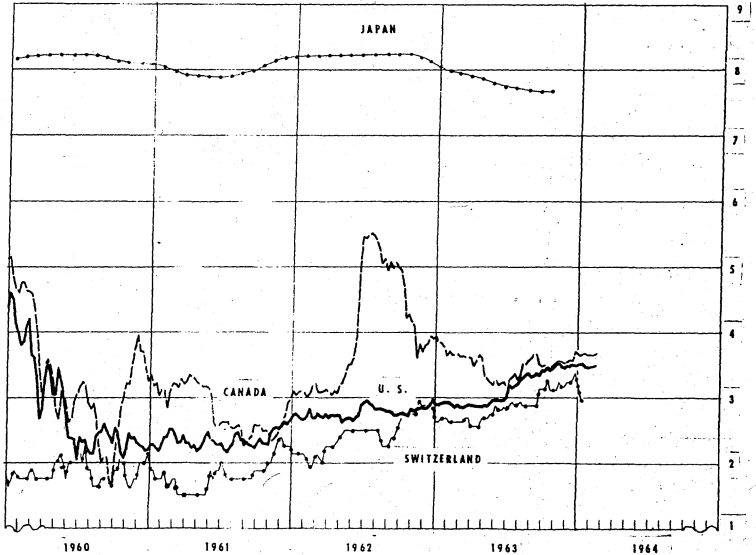
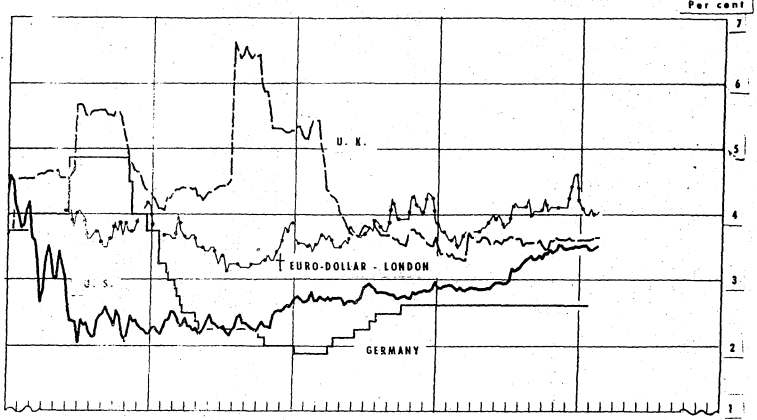


Chart 5
SHORT-TERM INTEREST RATES *



* 3-month Treasury bill rates for all countries except Japan. (Average rate on bank loans and discounts)
 † 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

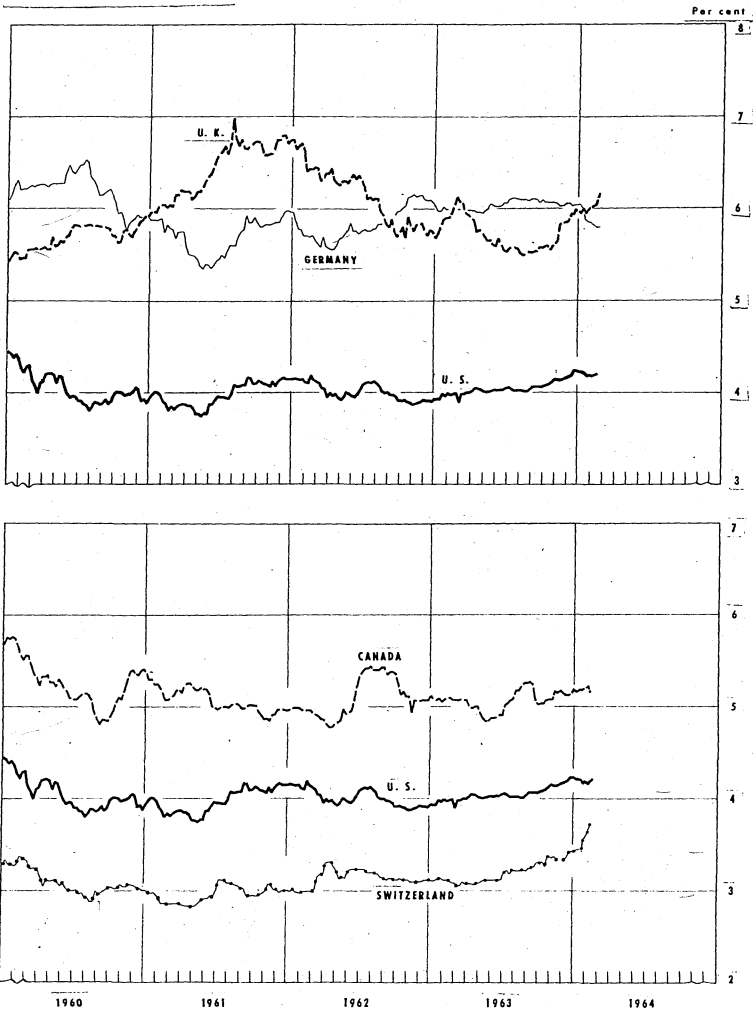
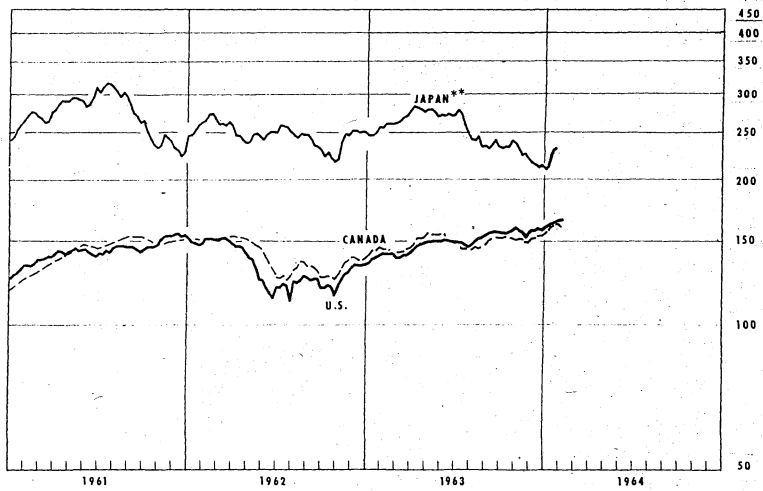
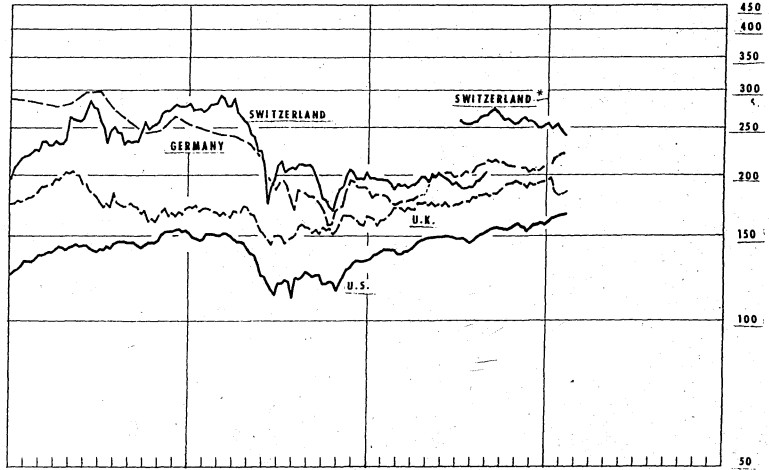


Chart 7

INDUSTRIAL STOCK INDICES

1958=100
Ratio scale



* New series: Swiss Bank Corporation industrial stock index.
 ** Japan: index of 225 industrial and other stocks traded on the Tokyo exchange.

Chart 8

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

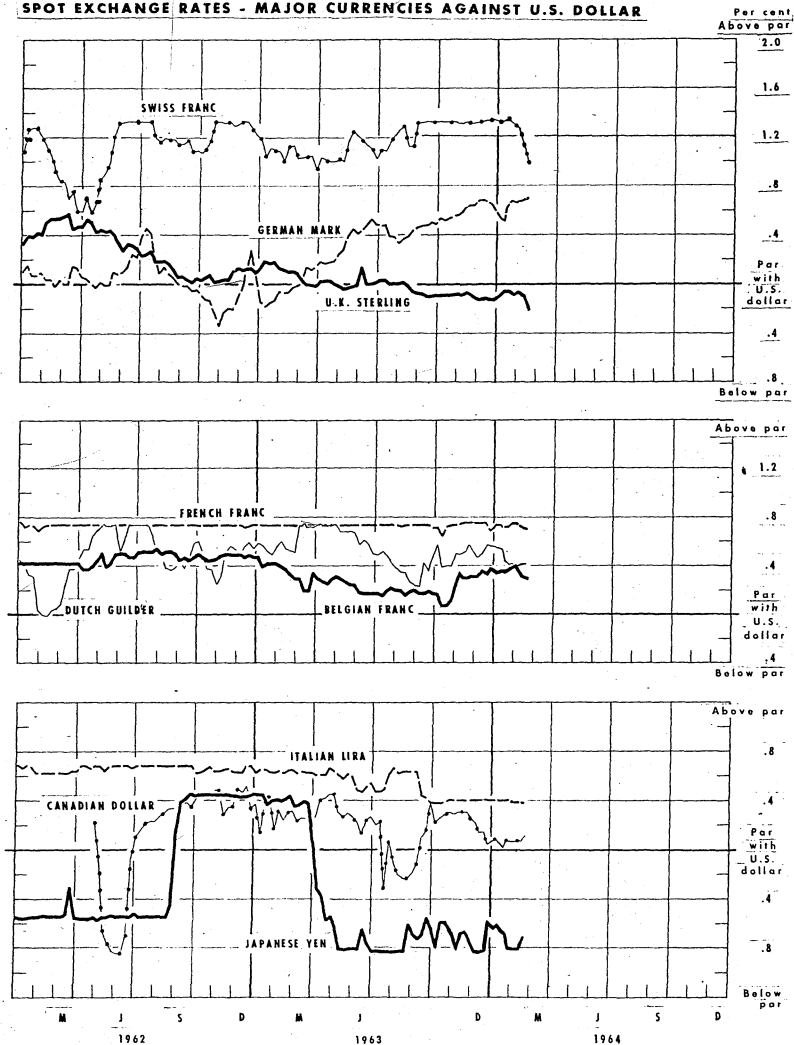
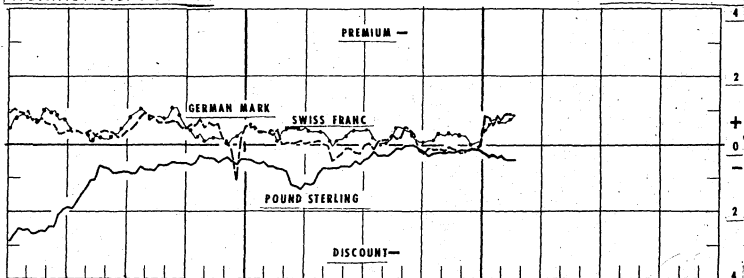


Chart 9

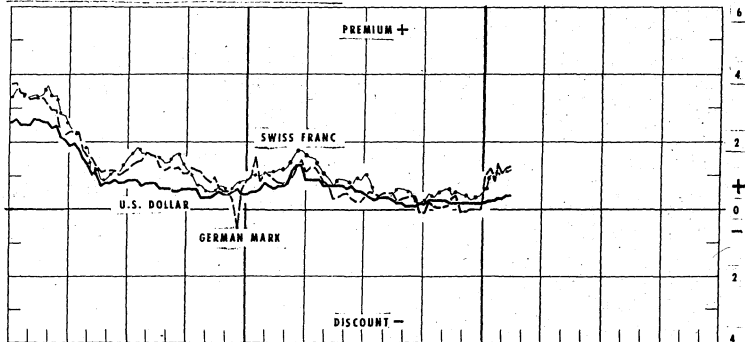
3-MONTH FORWARD EXCHANGE RATE

Friday figures

AGAINST U.S. DOLLARS



AGAINST POUND STERLING - LONDON



AGAINST POUND STERLING - LONDON

