

H. 13

No. 142

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March 18, 1964.

CAPITAL MARKET DEVELOPMENTS ABROAD

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

I. United Kingdom: Money and Capital Markets in February, 1964

The rise in Bank Rate from 4 to 5 per cent on February 27 was the dominant factor affecting financial markets in the United Kingdom during February. Earlier in the month yields advanced in money and capital markets prior to the action. In mid-February, the pound was under pressure in the foreign exchange market and selling became heavy after unfavorable trade figures for January were released on February 18. Afterwards, financial markets adjusted quickly to the new Bank Rate.

Table 1. United Kingdom: Selected Money Market and Bond YieldsNovember 1963-March 1964

(In per cent per annum)

	1963	1964				
	Nov. 8	Jan. 24	Feb. 14	Feb. 26	Feb. 28	March 6
<u>MONEY MARKET</u>						
Bank rate	4.00	4.00	4.00	4.00	5.00	5.00
Treasury bill (Tender)	3.75	3.72	3.78	--	4.30	4.30
Day-to-day money	3.50	3.00	3.75	3.75	3.75	4.25
Euro-sterling (3-mo.), Paris	4.31	4.25	4.38	4.50	5.00	4.88
Local authority (3-mo.), London	4.25	4.31	4.38	--	5.19	5.12
Euro-dollar (3-mo.), London	4.12	3.88	3.88	4.06	3.94	4.19
<u>COVERED ARBITRAGE (favor London):</u>						
U.K./U.S. Treasury bills	-.13	-.23	-.32	-.28	-.09	-.02
Local authorities/Euro-\$	-.08	-.35	-.07	--	.22	.15
<u>STOCK PRICES (April 10, 1962=100) ^{a/}</u>	114.1	111.6	111.4	111.9	111.6	113.3
<u>GOVERNMENT BOND YIELDS</u>						
5 per cent 1967	4.45	4.72	4.78	5.10	5.18	5.08
5 per cent 1971	4.80	5.02	5.12	5.30	5.35	5.38
5-1/2 per cent 1982-84	5.35	5.70	5.70	5.82	5.82	5.80
5-1/2 per cent 2008-12	5.58	5.92	5.95	6.08	6.10	6.05
3-1/2 per cent War Loan	5.65	5.98	6.05	6.18	6.20	6.12
<u>EXCHANGE RATES</u>						
Spot (U.S. cents)	279.77	279.79	279.74	279.52	279.77	279.78
3-mo. forward discount (In per cent per annum)	-.21	-.35	-.45	-.40	-.69	-.66

a/ Financial Times--Actuaries 500 share (industrials) index.OFFICIAL USE ONLY
(Decontrolled after six months)

Both the gilt-edged and the Treasury bill markets anticipated the Bank Rate move. Government bond prices, which had levelled off late in January, began to decline again during February. Between January 24 and February 26, yields rose as much as 20 basis points on long-term and about 40 basis points on shorter-term issues. (See Table 1.) The auction rate for the Treasury bill (which was 3.78 per cent on February 14) was already close to Bank Rate. In the February 21 bill auction, the discount houses were left with 56 per cent of the seasonally-reduced offerings because outside competition withdrew in expectation of a higher Bank Rate.

Because of these earlier developments, there were only limited adjustments in money and capital markets after the rise in Bank Rate. The Treasury bill rate rose about 50 basis points, and the covered differential on Treasury bills between the U.S. and U.K. was negligible up to March 6. (See Chart 2 and Tables 1 and 9.) On March 6, bond yields were little changed from their February 26 level.

In the foreign exchange market, the spot pound recovered promptly. Earlier, during the week of February 17, the pound had been under considerable pressure and continued to be weak in the week of February 24, even though selling pressures had eased. With higher Bank Rate, however, the spot rate moved up from 279.52 U.S. cents to 279.77 cents and the discount on the 3-month forward pound widened only from 0.40 per cent to 0.66 per cent per annum. (See Table 1 and Charts 2 and 8.) Reserve losses in February totaled \$48 million.

Bank advances (seasonally adjusted) have continued to rise. In January and February the increase averaged \$40 million per month, as compared to an average monthly rise of £35 million in November and December.

Money market. Credit conditions in the money-market were seasonally tight throughout February and in the first week of March, due to the transfer of tax payments to the Exchequer. The Bank of England offered sufficient relief through purchases of Treasury bills to enable commercial bank credit expansion to continue; but, at the same time, the Bank restrained its operations with a view to keeping day-to-day money rates close to the Treasury bill tender rate. As a result, the market rate for Treasury bills remained firm at 3.64 per cent from February 7 through February 26. (See Table 8.)

Because of unsettled market conditions, the discount houses obtained 56 per cent of the Treasury bill allotments on February 21 and 68 per cent on February 28. On February 21, outside tenders were reduced in anticipation of the Bank rate increase. On February 28 (the day after the Bank rate change), competition was light because of uncertainties about the new bill level. It is reported that many outside tenders were predicated on the assumption that the discount houses would lower their collective bid by considerably more than they actually did.

Short-term funds were in demand throughout February and early March to meet end-financial year requirements in the local authorities market. The yield on 3-months funds held steady at 4.38 per cent until the Bank rate increase, despite the availability of money from the deteriorating gilt-edged market after mid-February. (See Table 8.)

After the Bank rate change, the three-month rate in the local authorities market rose to 5.19 per cent on February 28, but it fell slightly during the following week because of an inflow of foreign funds.

In the local authority mortgage market, business was slow. During the first half of February, there was a reluctance to pay a market rate in excess of the FWLB lending rate; in the week following the Bank rate increase, there was virtually no business owing to market uncertainties; in early March, corporate Treasurers chose to wait for news about the changes in FWLB terms (which are expected before the end of the month) before committing themselves to the currently high market terms.

The FWLB lending rate was increased by 3/8 per cent to 6-1/8 per cent, reflecting the rise in local authority mortgage rates. However, after April 1 the FWLB lending rate will be changed to reflect the cost of Treasury, as opposed to local government, borrowing.

A technique has been devised which will enable the local authorities to borrow on short-term despite the Government's new restrictions (which become effective on April 1). The City of Manchester has issued a one-year negotiable 4-1/2 per cent bond--a maturity one day longer than loans controlled by the new restrictions. Bonds such as these cannot be sold in quantity to the discount houses as the Bank of England has announced that it will not consider these suitable collateral against loans, and the commercial banks are hesitant about purchasing them before their marketability is assured. However, there is still considerable appeal to this type of issue, as no government debt instrument is now available in the market with a maturity longer than 90 days and shorter than 18 months.

Since the Bank rate change, yield spreads on Treasury bills in London and New York have been virtually eliminated. (See Tables 2 and 8 and Chart 3.) Both deposit rates offered by finance houses and by local authorities rose by about 50 basis points in late February. Euro-dollar rates also advanced, widening the differential over negotiable certificates of time deposits to 40 basis points. (See Table 2 and Chart 1.)

Gilt-edged markets. The decline in bond prices which began in November continued through February. (See Table 9 and Chart 6.) From mid-February until February 27, prices fell mainly in anticipation of the Bank rate increase but also because of concern over the future of sterling. After the Bank rate change, prices were marked down immediately, but they recovered in the following week. On March 5, yields were near the levels prevailing before the Bank rate change.

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

	1963		1964					
	Nov.	Dec.	Jan.	February			March	
	29	27	31	7	14	21	28	6
<u>TIME DEPOSITS (3-month)</u>								
U.S. dollar:								
N.Y. - Certf. deposit ^{a/b/}	3.82	3.86	3.88	3.84	3.84	3.84	3.84	3.91
London - Euro-\$	4.12	4.25	3.94	4.00	4.00	4.06	4.12	4.31
Sterling (covered)								
Local authorities	4.12	4.40	3.97	3.94	3.93	4.01	4.53	4.46
Finance Houses	4.10	4.08	3.85	3.90	3.85	3.85	4.35	4.35
<u>YIELD SPREADS (Favor U.K.)</u>								
Treasury bills (3-month) ^{2/}								
Uncovered	.14	.11	.13	.15	.14	.12	.60	.64
Covered	-.05	-.05	-.18	-.29	-.32	-.25	-.09	-.02
Euro-\$ - N.Y. C/D ^{a/}	.30	.76	.24	.16	.16	.22	.22	.40
Euro-\$ - Local Authority (covered)	--	.15	.13	-.06	-.07	-.11	.22	.15

^{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 8. See also Chart 3.

New offerings of U.S. dollar loans in London were much more limited in February than they were in the previous two months (\$40 in December and \$60 million in January). Only one new issue was offered: \$10 million 6-1/4 per cent convertible unsecured debentures (1974-84) by a Japanese firm, Teijin Kabushiki Kaisha. Of this offering only \$2 million was placed in the United Kingdom, the balance being handled by Continental underwriters. However, a number of dollar issues are planned for coming months.

British residents will have an opportunity to invest in the U.S. securities market through a new U.K. investment trust, Securities of America, Ltd. Shares in this trust were offered to the British public (in sterling) starting March 5. The trust will acquire foreign exchange in the investment dollar market. Its attraction is that it will enable small investors to overcome three major problems of investing in the U.S. market: the high unit price of many American stocks, the complexity of securing relief from double taxation liability, and the difficulty in operating in the volatile investment dollar market.

Stock market. The sharp decline in stock prices which began after the New Year came to an end during the first week in February. (See Table 9 and Chart 7.) The market remained unsettled during the remainder of the month. The downward pressure on stock prices exerted by profit-taking came to an end but investors were concerned that the next budget may be somewhat deflationary because of the deterioration in the balance of payments expected over the course of 1964.

There was little reaction to the Bank rate increase in the stock market. Prices were marked down initially, but they recovered in the week ending March 7.

London clearing banks. Bank advances to the private sector expanded by more than £150 million in the month ending February 19. (See Table 3.) In part this represented the usual seasonal expansion of lending activity to finance seasonal tax payments, but preliminary estimates indicate that advances rose £65 million more than is normal for this month. Even though the banks sold £64 million of gilt-edged securities, bank liquidity was reduced: the liquidity ratio moved below the former customary minimum of 30 per cent for the first time since the minimum ratio was reduced to 28 per cent by the Bank of England in October 1963.

In February, the ratio of advances to deposits rose to a post-war peak of 52.8 per cent.

Table 3. United Kingdom: London Clearing Banks' Net Deposits and Selected Assets

(In millions of pounds)

	Changes: ^{a/}						Outstanding Feb. 19, 1964
	1963				1964		
	Sept.	Oct.	Nov.	Dec.	Jan.	Feb.	
NET DEPOSITS	+38	+107	+49	+65	+128	-973	6,876
SELECTED ASSETS							
Claims on the Public Sector							
Government bonds	+19	+21	+25	+ 4	+ 11	- 64	1,111
Treasury bills and loans to the Discount Market	+78	+37	+28	+30	+ 70	-313	1,276
Loans to nationalized industries	-13	+19	- 7	- 5	+ 8	+ 6	79
Total	+84	+77	+46	+29	+ 89	-371	2,466
Claims on the Private Sector							
Advances (net)	-44	- 1	+14	+ 5	+ 39	+154	4,090
Other ^{b/}	+12	- 7	-	+ 2	+ 12	- 7	638
Total	-32	- 8	+14	+ 7	+ 51	+147	4,728
SEASONALLY ADJUSTED							
Advances (net)	+22	+23	+39	+30	+ 14	^{c/} + 65	
Deposits (net)	+31	+72	+84	+ 5	n.a.	n.a.	
LIQUIDITY RATIO	32.1	32.3	32.2	32.7	33.0	29.9	

^{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.

Installment credit. Installment credit outstanding edged up slightly in January, accompanying a rise in retail sales to a level somewhat above that prevailing in the latter part of 1963. (See Table 4.) New credit extended by finance houses rose sharply from the December seasonal low, largely reflecting purchases of new cars.

Table 4. United Kingdom: Installment Credit
(end of period)

	1961	1962	Year	1963		1964		Outstanding
				Nov.	Dec.	Jan.	Jan. 31, 1964	
New Credit Extended, Index of value (1957=100)								
Household goods shops	124	139	145	140	145	110		
Finance houses	96	94	129	157	129	174		
Credit Outstanding (£ mns.)								
Household goods shops	-16	+ 9	+22	+ 5	+11	- 1		339
Finance houses	+ 8	-49	+45	+ 3	- 4	+ 4		618
Total	- 8	+40	+67	+ 8	+ 7	+ 3		957

Foreign trade. Higher imports of fuels and industrial materials accompanying the industrial expansion mainly account for the recent deterioration in the U.K. trade balance. (See Table 5.) There has also been some increase between November and January of finished manufactures, particularly machinery. The Board of Trade expects these imports to continue rising if fixed capital formation continues to expand. Exports have levelled off, reflecting a sharp fall in exports to Germany and Italy. There was little change in exports to the sterling area and to North America.

Foreign exchange markets. The spot rate fell gradually in the first half of February but then dropped sharply to \$2.7943 on February 21, a day which saw considerable selling of sterling. (See Table 8 and Chart 8.) Following the Bank rate change, the spot rate recovered to the level prevailing in the beginning of the month.

The weakness in sterling was also found in the widening of the forward discount in the first half of February to the point where there was the substantial covered interest differential of 30 basis points in favor of U.S. over U.K. Treasury bills. Following the Bank rate change, the forward discount rose only 29 basis points.

The investment dollar premium fell gradually from 12 per cent to 11 per cent during February and remained at this level in the first week of March.

Gold and foreign exchange reserves. Reserves fell by \$48 million in February. (See Table 6.) It is believed that the bulk of the losses took place in the week ending February 21, when some short-term capital outflows were reported.

Table 5. United Kingdom: Foreign Trade
(Millions of pounds; seasonally adjusted; monthly averages)

	1962						1963			1964		
	4th Qtr.	1st Qtr.	2nd Qtr.	3rd Qtr.	4th Qtr.	Nov.- Jan.	Nov.- Jan.	Nov.	Dec.	Jan.		
Imports, c.i.f.												
Food, beverages, and tobacco	123	126	141	148	143	149	147	145	157			
Fuels and industrial materials	197	195	200	209	220	227	216	235	233			
Finished manufactures and other	54	53	56	57	59	63	58	63	67			
Total a/	374	375	395	412	422	440	422	442	457			
Exports, f.o.b.	317	327	335	346	348	343	342	362	326			
Re-exports, f.o.b.	14	12	13	13	13	12	14	12	11			
Trade balance, customs returns	-43	-36	-47	-53	-61	-85	-66	-68	-120			
Trade balance, balance of payments basis b/	-3	+7	-2	-9	-12	-35	-19	-13	-72			

a/ Details may not add to totals due to rounding.

b/ Customs returns adjusted for valuation and coverage, mainly revaluing imports from a c.i.f. to an f.o.b. basis. Fourth quarter and 1964 figures are preliminary and are subject to substantial revisions.

Table 6. United Kingdom: Reserve Position
(In millions of U.S. dollars)

	Changes:						1964 Outstanding Feb. Feb. 29, 1964
	1963						
	Jan.- June	July- Dec.	Nov.	Dec.	Jan.	Feb.	
A. Gold and convertible currencies	- 93	-56	+17	-115	+17	-48	2,626
Less: Central bank loans	a/ --	--	--	--	--	--	
Less: U.S. opns. in sterling b/	+ 51	-18	+10	- 10	--	--	--
Adjusted Reserves	-144	-38	+ 7	-105	+17	-48	2,626
B. Drawing rights on IMF	- 8	- 5	--	--	--	n.a.	c/ 2,439
Total	-152	-43	+ 7	-105	+17	n.a.	5,065

a/ Covers 3250 million assistance received in the first quarter and repaid in June.

b/ As published in the Federal Reserve Bulletin, September 1963, and March 1964.

c/ As of January 31, 1964.

Bullion market. The London gold market was quiet in February, but there was a strong demand between March 3 and March 10. Sparked by rumors of a possible devaluation of the Italian lira, heavy purchases were made by Swiss banks on behalf of Italian customers. This was reflected in an increase in the fixing price to \$35.096 per fine ounce on March 6. (See Table 7.)

The operations of the London gold market and the so-called central bank "gold pool" are described in The Bank of England Quarterly Bulletin for March 1964. Between November 1961 and the end of 1962, the amounts contributed by participating central banks to hold down the price of gold in London are reported to be roughly equal to the amounts distributed to pool members from purchases made at other times. During 1963, more than \$600 million was bought from the London market and was shared out among participating countries.

Table 7. London Fixing Price for Gold
(In U.S. dollars per fine ounce)

December	27	35.077	January	24	35.084	February	20	35.079
January	3	35.072		31	35.078		28	35.080
	10	35.069	February	7	35.078	March	6	35.096
	17	35.087		14	35.076		13	35.077

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 8. United Kingdom: Treasury Bill Yields and Exchange Rates

- 9 -

		3-mo. Treasury bill arbitrage calculation					Spot pound	London deposit rates	
		U.K.	U.S.	Difference	3-mo. pound	In favor U.K. bill	U.S. (cents) ^{a/}	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									
	Dec. 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
	21	3.64	3.52	.12	-.37	-.25	279.43	4.06	4.38
	28	4.16	3.56	.60	-.69	-.09	279.77	4.12	5.19
	Mar. 6	4.16	3.52	.64	-.66	-.02	279.78	4.31	5.12
	13	4.16	3.53	.63	-.65	-.02	279.78	4.25	n.a.

^{a/} Certified N. Y. noon buying rate.

Table 9. United Kingdom: Selected Capital Market Yields

		U.K. Government bond yields					Share yield	Yield gap	Share prices
		5% 1967	3% 1965-75	5-1/2% 2008-12	3-1/2% War Loan	2-1/2% Consols	a/	b/	a/
1963									
	High	5.02	5.44	6.00	6.12	5.98	5.06	--	117.2
	Low	4.38	4.76	5.45	5.68	5.39	4.13	--	95.6
1963									
	Dec. 12	4.68	5.31	5.95	5.95	5.76	4.17	1.59	115.9
	19	4.72	5.33	5.93	5.99	5.84	4.20	1.64	116.4
	24	4.72	5.33	5.93	5.98	5.83	4.18	1.65	116.9
1964									
	Jan. 2	4.72	5.28	5.88	5.95	5.77	4.15	1.62	117.5
	9	4.75	5.30	5.88	6.00	5.86	4.23	1.63	116.2
	16	4.70	5.22	5.93	5.96	5.81	4.35	1.46	113.4
	23	4.72	5.22	5.90	5.99	5.85	4.37	1.48	112.3
	30	4.70	5.26	5.93	6.00	5.86	4.43	1.43	110.3
	Feb. 6	4.75	5.13	5.92	6.03	5.88	4.46	1.42	109.2
	13	4.75	5.29	5.95	6.05	5.91	4.39	1.52	111.0
	20	4.88	5.41	6.05	6.18	6.02	4.45	1.57	110.4
	27	5.15	5.51	6.10	6.21	6.08	4.42	1.66	111.4
	Mar. 5	5.08	5.52	6.05	6.15	5.97	4.35	1.62	113.2
	12	5.08	5.50	6.00	6.10	5.95	4.34	1.61	113.9

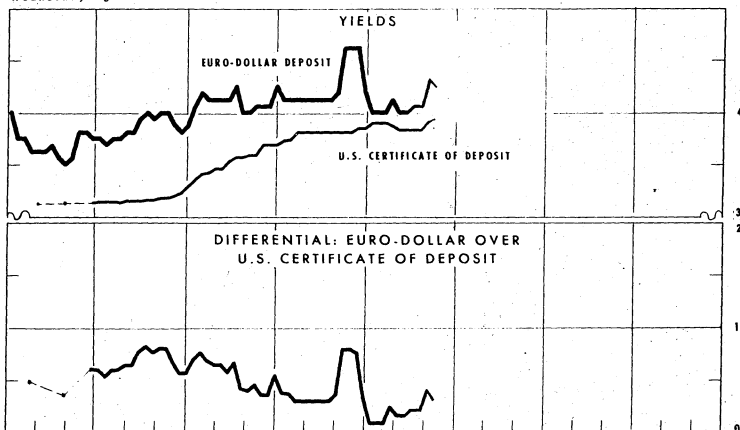
^{a/} Financial Times—Actuaries 500 Share Index (Apr. 10, 1962=100). Share prices are wkly. avgs.^{b/} Difference between yield on 2-1/2 per cent Consols and share yield.

Chart 1
INTERNATIONAL MONEY MARKET YIELDS FOR U.S. DOLLAR INVESTORS

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

Wednesday figures

Per cent per annum



NEW YORK OFFER RATES ON SELECTED 3-MONTH INVESTMENTS

Friday figures

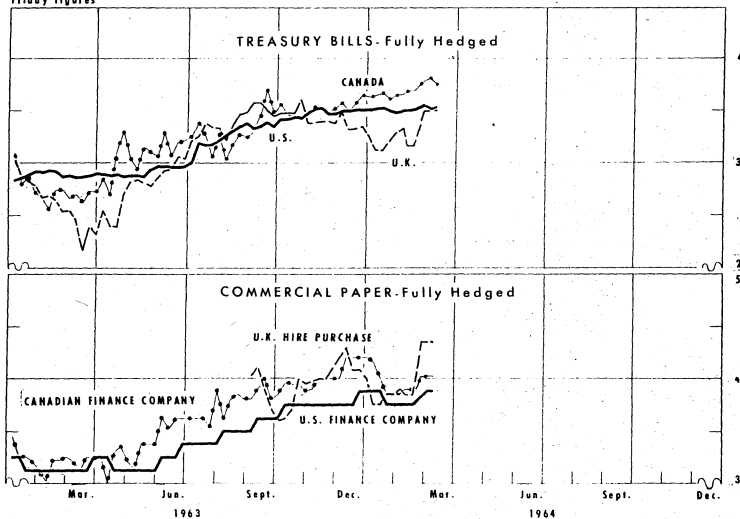


Chart 2

INTEREST ARBITRAGE, UNITED STATES / CANADA

Thursday figures

Per cent per annum

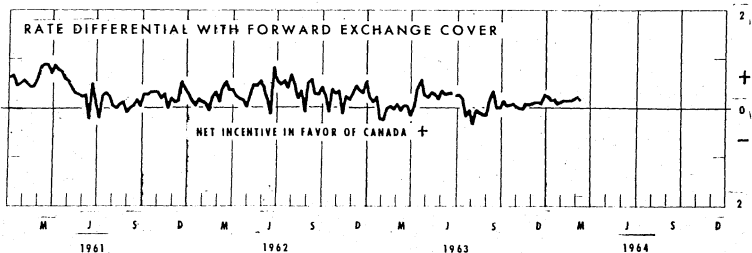
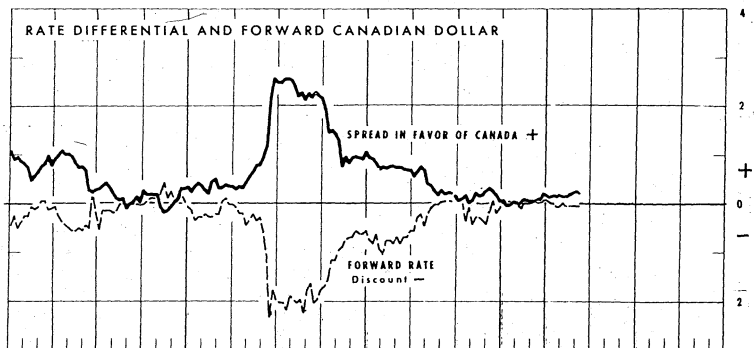
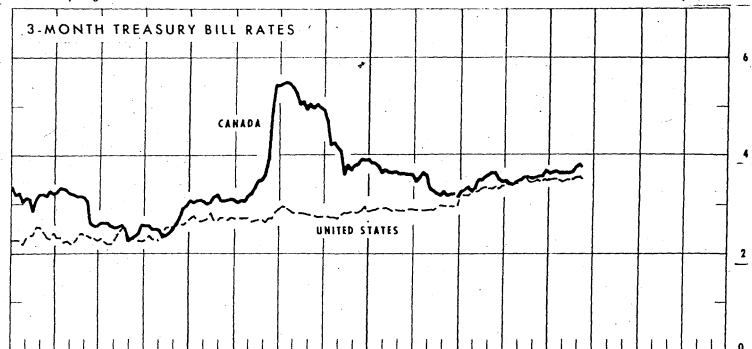


Chart 3
INTEREST ARBITRAGE, NEW YORK/LONDON

Friday figures Per cent per annum

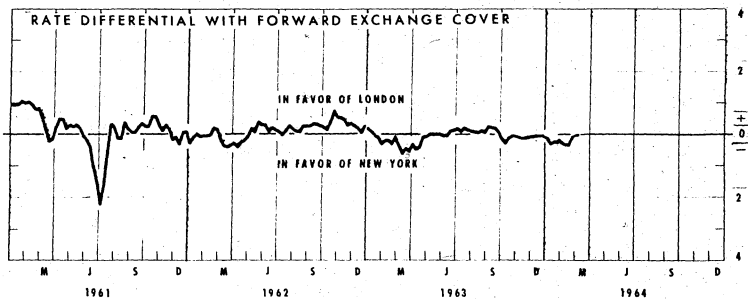
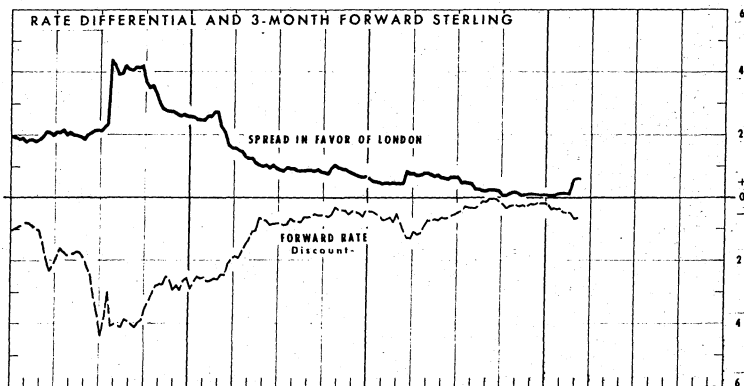
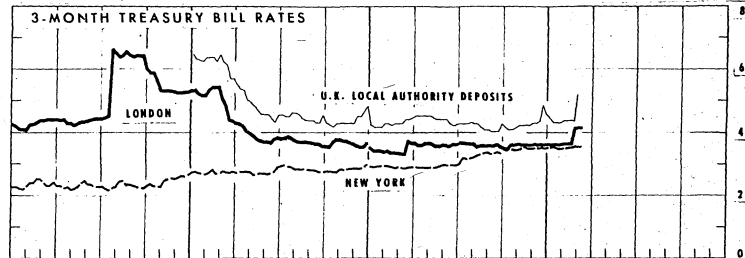


Chart 4

INTEREST ARBITRAGE FOR GERMAN COMMERCIAL BANKS

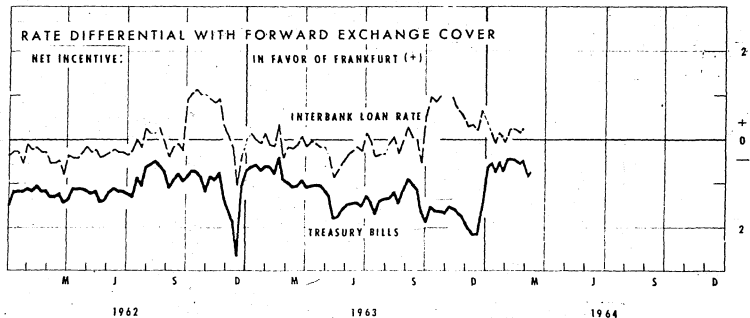
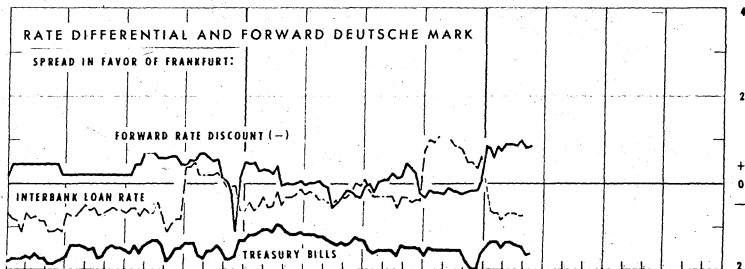
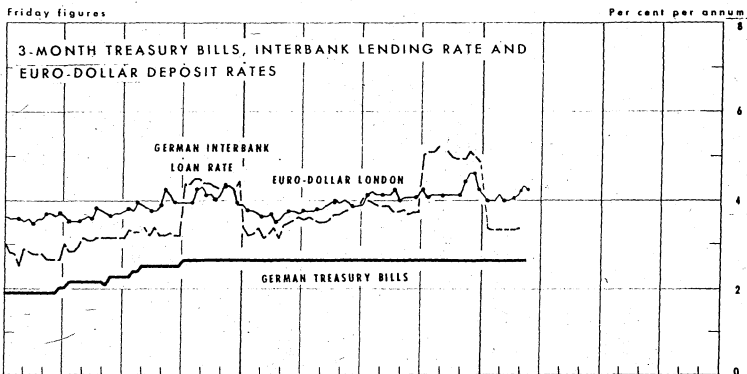
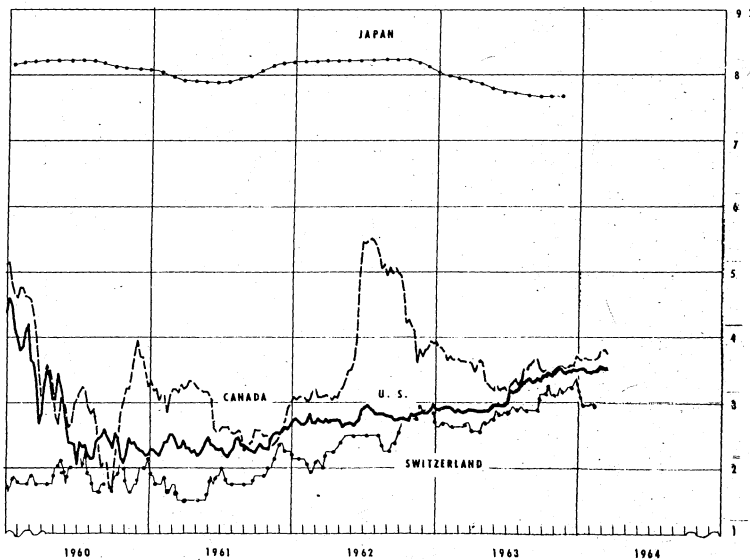
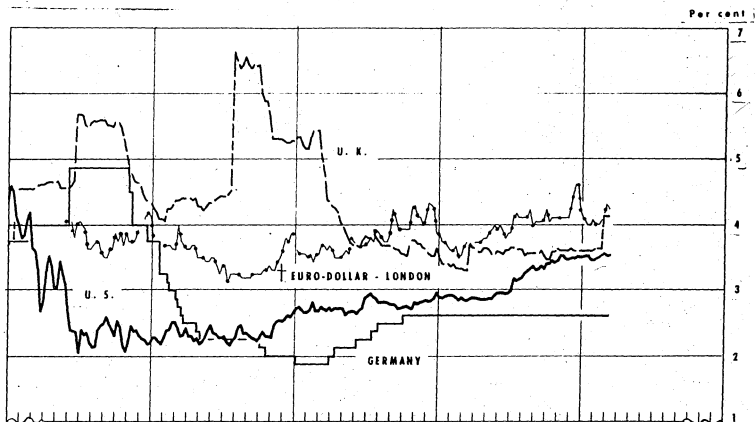


Chart 5
SHORT-TERM INTEREST RATES *



* 3 month treasury bill rates for all countries except Japan (Average rate on bank loans and discounts)¹
+ and Switzerland (3 month deposit rate)
† 3 month rate for U. S. dollar deposits in London

Chart 6

LONG-TERM BOND YIELDS

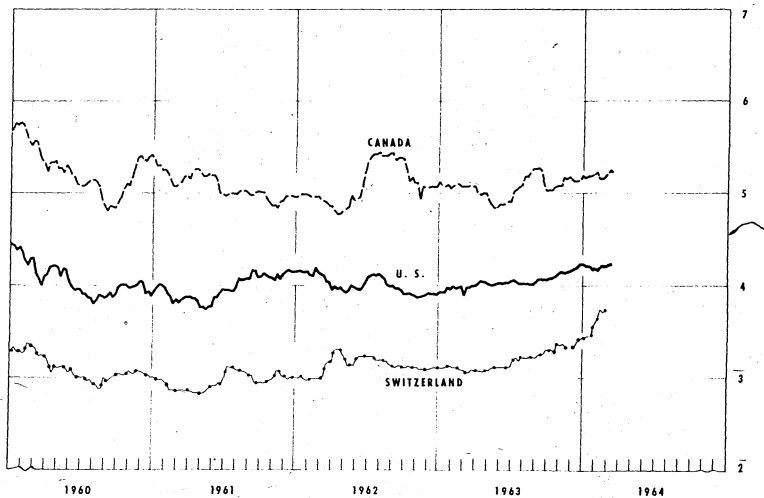
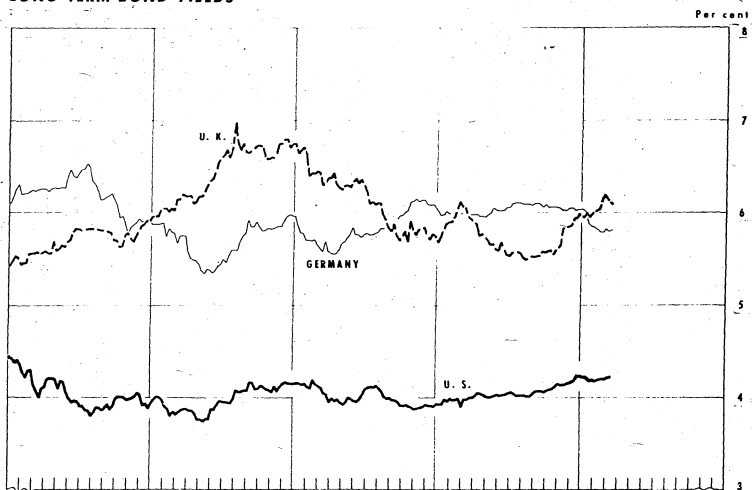
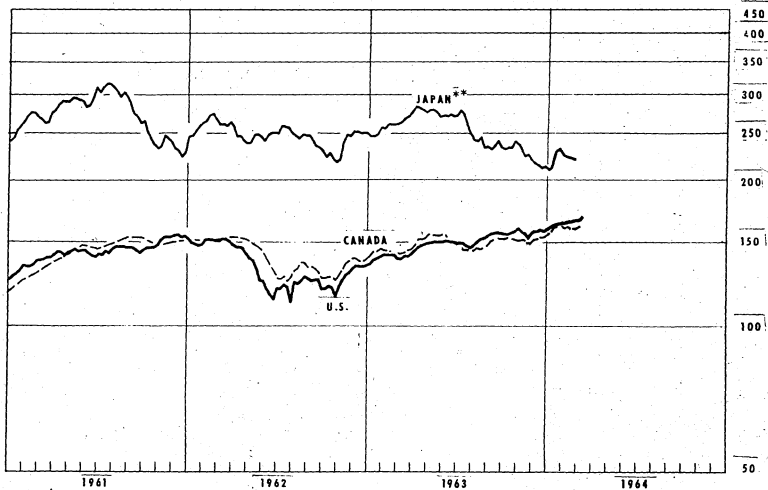
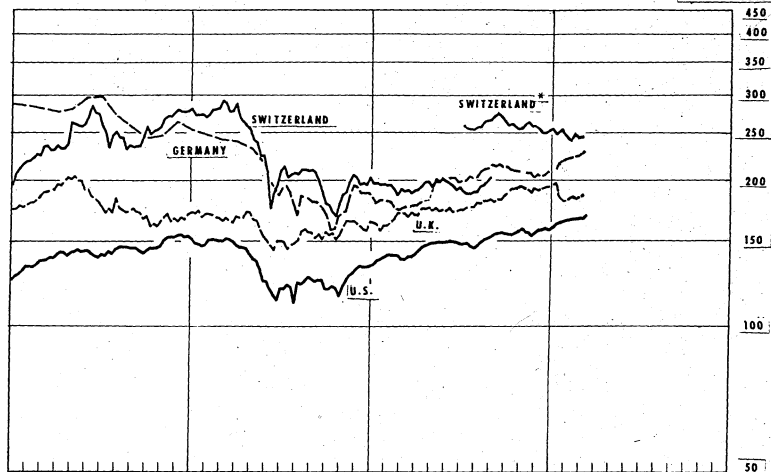


Chart 7

INDUSTRIAL STOCK INDICES

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

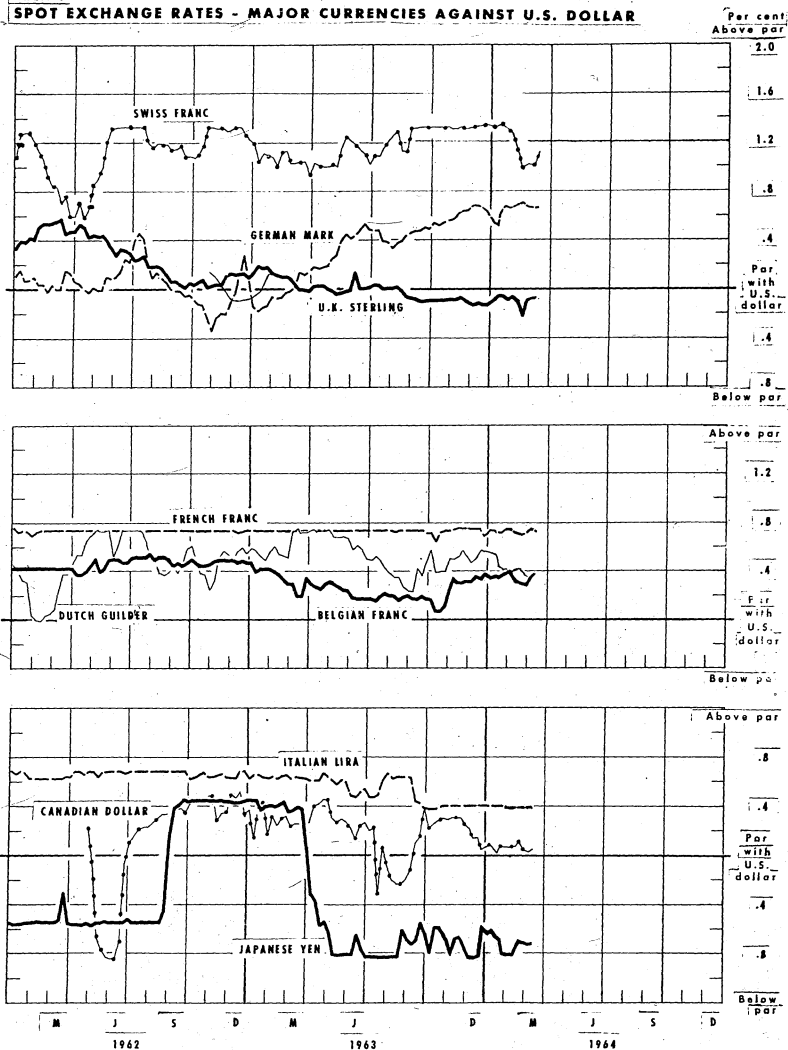
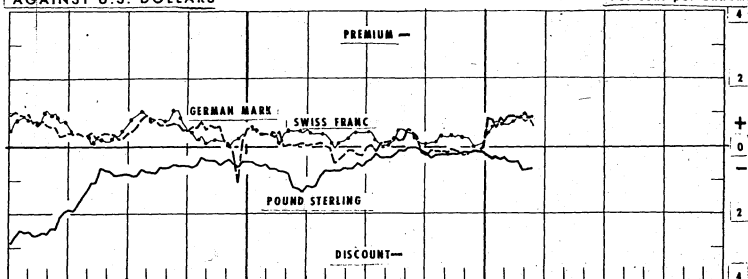


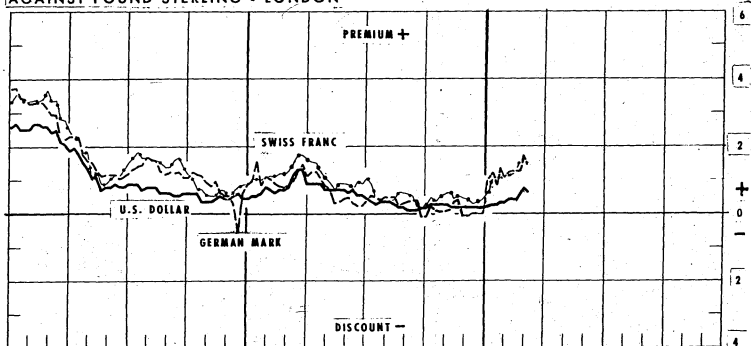
Chart 9
3-MONTH FORWARD EXCHANGE RATE

Friday figures

AGAINST U.S. DOLLARS



AGAINST POUND STERLING - LONDON



AGAINST POUND STERLING - LONDON

