

H. 13  
No. 163

September 16, 1964.

**CAPITAL MARKET DEVELOPMENTS ABROAD**

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

I. United Kingdom: Money and Capital Markets in August

Conditions in domestic financial markets in the United Kingdom were relatively stable during August, despite the weakening position of the pound in the foreign exchange market. In the first two weeks, both the gilt-edged and stock markets recovered from the mid-July shake-out that followed the announcement of a large trade deficit for June. (See Table 1.) At mid-August, the announcement of an only slightly reduced trade deficit for July momentarily retarded this improvement. However, by the end of the month, demand had revived in both markets and share prices were above and bond yields below their August 21 levels. Throughout the month, the Treasury bill yield remained unchanged, but the spot pound declined from 278.84 U.S. cents on July 31 to 278.32 on September 11.

Table 1. United Kingdom: Selected Financial Indicators, July-September 1964

	July	August				September	
	<u>31</u>	<u>7</u>	<u>14</u>	<u>21</u>	<u>28</u>	<u>4</u>	<u>11</u>
<u>Treasury bill</u>							
3 months tender	4.65	4.65	4.65	4.65	4.65	4.65	4.65
<u>Government bonds</u>							
4% 1965	4.93	4.96	4.97	5.04	4.85	4.89	4.93
3-1/2% 1979-1981	5.88	5.88	5.83	5.85	5.82	5.82	5.85
5-1/2% 2008-2012	6.18	6.15	6.13	6.15	6.15	6.15	6.15
3-1/2% War Loan	6.24	6.24	6.18	6.22	6.22	6.22	6.22
<u>Stock market price</u>							
<u>indices</u>							
<u>Financial Times</u>							
Industrial ordinary <sup>a/</sup>	356.6	356.5	365.9	358.4	363.8	366.7	366.4
<u>Exchange rates</u>							
Spot rate (U.S. cents)	278.84	278.85	278.75	278.59	278.43	278.39	278.32
Forward discount (per cent per annum)	-.67	-.72	-.67	-.60	-.65	-.62	-.65

<sup>a/</sup> Previous Thursday.

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During early September, prices of gilt-edged bonds held firm and stock prices advanced further. Market activity was stimulated in part by public opinion polls favorable to the return of the present government. On September 10, the Financial Times industrial stock index was at 366.4 compared with 356.6 on July 31 and 358.4 on August 21. (See Table 1.)

On the external side, reserve losses of about \$92 million in August suggest that the authorities were permitting the exchange rate (instead of the reserves) to absorb selling pressures associated with electoral and export uncertainties. For the first six months of 1964, the \$340 million increase in the sterling balances of the outer-sterling countries were equivalent to about half the U.K.'s own balance-of-payments deficit for the period.

The covered differential in favor of the U.K. Treasury bill over the U.S. bill fluctuated between 31 and 42 basis points during August. (See Table 10 and Chart 3.) However, the covered yield of the U.K. hire purchase deposit was about 50 basis points above the yield on U.S. finance paper during the month. (See Chart 1.) The differential on the Euro-dollar deposit over the U.S. certificate of deposit was stable during August at around 39 basis points after declining during July. (See Chart 1.)

No United States dollar loans in London were reported for August. However, on August 31, a Danish power consortium made known its plans to raise about \$10 million sometime during September.

Money market shows mixed behavior. Call money rates tightened noticeably during the month, but those on Treasury bills remained stable. Rates on local authority deposits eased during the second week, but remained stable thereafter. (See Table 2.) The higher call money rates were generally attributable to tax collections outpacing expenditures and normal seasonal factors. The Bank of England provided support throughout the month by buying bills, but there was no borrowing by the discount houses.

Table 2. United Kingdom: Selected Money Market Rates: July-August 1964  
(per cent per annum)

	July	August			
	31	7	14	21	28
Call money <sup>a/</sup>	4.38	4.25	4.00	4.25	4.50
Local Authority deposits (90-days)	5.06	5.06	5.00	5.00	5.00
Euro-dollar (90-days)	4.25	4.19	4.25	4.25	4.25
Treasury bill-market rate (3-months)	4.50	4.50	4.50	4.50	4.50

a/ Estimated from a range of rates quoted in the Financial Times.

Capital markets continue strong. The demand for gilt-edged bonds which had been strengthening through the first two weeks of August, eased after the announcement of the trade deficit on the 1<sup>st</sup>. This weakness was short-lived, for in the following week most rates declined in response to revived demand. There was no noticeable change in the shape of the yield curve. The stock market exhibited a similar pattern. The growing demand for equities was also interrupted, but only temporarily, and prices began to rise once more during the final week. (See Tables 1 and 3.)

In the local authorities market three developments are worth noting. First, effective August 8, the Public Works Loan Board's rates were raised an average of one-eighth of one per cent. (See Table 4.) The last increase was made in May of this year. Second, the response of the local authorities to the opening of the short-term bond market has been appreciable--the queue has risen to over 150 authorities--and the Bank of England has placed a minimum of one quarter of a million pounds on any single issue, in order to reduce the number of borrowers. Third, an urban district, the first since before the war, successfully floated a 900,000 pound issue in the stock market, thus breaking the three million pound rule that had hitherto been in force, and extending the scope of the local authority bond market.

Table 3. United Kingdom: Selected Capital Market Yields: July-August 1964

	July 30	August			
		6	13	20	27
<u>Government bond yields</u>					
5% 1967	5.40	5.42	5.43	5.45	5.47
3% 1965-1975	5.81	5.80	5.76	5.80	5.79
5% 1986-1989	6.10	6.08	6.05	6.08	6.07
2-1/2% Consols	6.06	6.06	6.01	6.05	6.04
<u>Stocks</u>					
Share yield a/	4.58	4.59	4.51	4.59	4.56
Yield gap b/	1.48	1.47	1.50	1.44	1.48
Share prices a/	116.43	116.40	118.77	116.87	117.53

a/ Financial Times. Actuaries 500 share index (April 10, 1962=100).

b/ Difference between yield on Consols and share yield.

New issues (net of redemption) totaled 47 million pounds in August--down appreciably from the May-July average of 60 million pounds per month. (See Table 5.) The decline was concentrated wholly in the "quoted public companies" segment for local authorities borrowing continued to increase and no overseas borrowing was reported.

Table 4. United Kingdom: Public Works Loan Board Rates to Local Authorities  
(per cent per annum)

Length of Loan in years	Interest				Rates			
	May		Last		August		Last	
	Quota Loans		resort loans		Quota loans		resort loans	
	a	b	a	b	a	b	a	b
Not more than 5	5-1/4	5-3/8	5-7/8	5-7/8	5-5/8	5-5/8	6-1/8	6-1/8
More than 5 but not over 10	5-3/8	5-3/8	6	6	5-5/8	5-7/8	6-1/8	6-1/8
More than 10 but not over 15	5-1/2	5-7/8	6	6	5-3/4	6	6-1/8	6-1/8
More than 15 but not over 25	5-5/8	6	6	6-1/8	5-7/8	6-1/8	6-1/8	6-1/8
More than 25	6	5-7/8	6-1/8	6-1/8	6	6-1/8	6-1/8	6-1/8

a/ Installment loans.

b/ Loans repaid at maturity.

Table 5. United Kingdom: Capital Issues (Net of Redemptions): May-August 1964  
(millions of pounds)

	May	June	July	August
U.K. quoted public companies	48.9	34.0	65.0	28.5
U.K. local authorities	4.5	7.1	10.3	18.5
Overseas borrowers	2.3	9.2	0.9	--
Total	<u>55.7</u>	<u>50.3</u>	<u>76.2</u>	<u>47.0</u>
Gross issues	65.6	54.6	89.0	49.2
Gross redemptions	9.9	4.3	12.8	2.2

Source: Bank of England.

Bank lending increases during the quarter ending in August. Although the effects of the postal strike continue to affect the monthly figures, the average of monthly advances by the London clearing banks during the quarter ending August 15, was substantially higher than earlier in the year. (See Table 6.) Since little seasonal change is expected during this most recent quarter, the average monthly increase is set at 50 million pounds--14 million pounds more than the increase for the first five months on a seasonally adjusted basis.

On the other hand, much more modest increases in installment credit were noted during the quarter ending in June. Total credit outstanding stood at 1,042 million pounds in June; as a result the average monthly increase for the second quarter was 29 million pounds.

Table 6. United Kingdom: Bank Lending<sup>a/</sup> to the Private Sector:  
May-August 1964  
 (millions of pounds)

	May	June	July	August	Average monthly change	
					March-May	June-August
Advances <sup>b/</sup>	4193	4224	4327	4353	15	40
Call loans	228	202	206	202	7	- 9
Other bills	362	336	382	382	2	13
Other investments	123	123	123	123	0	0
Total	4906	4915	5038	5060	25	51

a/ As reported by the London Clearing Banks. Amounts are those outstanding at mid-month.

b/ Less items in transit and advances to nationalized industries.

Source: Bank of England.

Trade deficits continue as exports decline. In July, exports declined for the second consecutive month, but the fall in imports prevented a further deterioration of the trade deficit. In fact, there was some improvement here for on a balance of payments basis the deficit narrowed from 62 million pounds in June to 39 million pounds in July. (See Table 7.) However, for the three months ending July 31 the average monthly payments deficit was 11 million pounds greater than the average for the preceding three months.

Reserve losses not appreciable, but spot rate drops noticeably. The continuing trade deficits and the apparent practice of continental holders to switch from sterling to Euro-dollars has placed some pressure upon Britain's reserve position. Yet, losses to date--including \$92 million in August--have not been appreciable. (See Table 8.) Official policy appears to be that of permitting the exchange rate to absorb the pressure instead of reserves. Indeed, during August the rate was allowed to drop from 278.84 to 278.43 (U.S. cents), (see Tables 1 and 10) although some support was given intermittently.

Table 7. United Kingdom: Foreign Trade, May-July, 1964  
(millions of pounds; seasonally adjusted; months or monthly average)

	<u>May</u>	<u>June</u>	<u>July</u>	<u>May</u> <u>July</u>	<u>change over</u> <u>previous quarter</u>
Imports (c.i.f.)	450	474	430	451	- 2
Exports (f.o.b.)	370	348	331	350	- 9
Re-exports (f.o.b.)	13	12	13	12	- 1
Balance	-67	-114	-86	-89	- 7
Trade balance <sup>a/</sup>	-19	- 62	-39	-40	-11

<sup>a/</sup> Balance of payments estimate.

Source: Board of Trade.

Table 8. United Kingdom: Reserve Position: June-August 1964  
(millions of U.S. dollars)

	<u>June</u>	<u>July</u>	<u>August</u>	<u>Outstanding</u> <u>August 31, 1964</u>
Gold and convertible currencies	-56	-28	- 92	2584
Drawing rights on I.M.F.	+ 2	--	n.a.	<sup>a/</sup> 2441
Total	-54	-28	n.a.	

<sup>a/</sup> July 31, 1964.

Source: Bank of England and International Monetary Fund.

Apart from the selective intervention policy, reserve losses have been modest because the overseas sterling area amassed claims in sterling at a very rapid rate. Over the first six months of 1964 these claims increased by nearly \$340 million or about one-half of Britain's payments deficit for that period. (See Table 9.)

Table 9. United Kingdom: External Liabilities and Claims in Sterling  
End of December 1963 and March, June, 1964  
 (millions of dollars)

	1963 Dec.	1964		Changes	
		March	June	I Q 1964	II Q 1964
Overseas Sterling area	6891	7028	7224	+137	+196
North America	204	227	305	+ 23	+ 78
Western Europe	1282	1246	1198	- 36	- 48
Other	1961	1968	1974	+ 7	+ 6
Total	10338	10469	10701	+131	+232

Source: Central Statistical Office, Financial Statistics.

Forward market steady and arbitrage incentives still favor London. Despite the weakening position of the pound in the spot market, the forward rate held steady at about 0.65 per cent per annum discount throughout the month and the covered differential on Treasury bills favored London from 31 to 42 basis points. This range may be compared with a peak covered differential on Treasury bills in July of 0.55 per cent per annum in favor of London. At that time, the Federal Reserve in agreement with British authorities intervened in the market in order to widen the forward discount and thereby reduce the arbitrage incentive.

With respect to other comparable obligations, the yield on Euro-dollar deposits exceeded that on New York time certificates of deposit by about 40 basis points; the covered yield on the U.S. Treasury purchase deposit was about 50 basis points above the yield on U.S. finance paper; and covered local authority deposit rates exceeded Euro-dollar rates by about 15 basis points. (See Table 10 and Chart 1.)

Bullion market relatively quiet. The London gold market was relatively quiet during August, although demand eased during the first three weeks and the fixing price fell from \$35.084 per fine ounce at the end of July to \$35.072 per fine ounce on August 21. However, bullion was once more in demand during the last week and the price rose to \$35.081. (See Table 11.)

Table 10. U.K./U.S. Exchange Rates and Arbitrage Calculations  
July-August, 1964

	July	August			
	31	7	14	21	28
Exchange rates					
Spot (U.S. cents)	278.84	278.85	278.75	278.59	278.43
Forward (per cent per annum)	-.67	-.72	-.67	-.60	-.65
Three month yields and yield spreads					
Treasury bills					
U.K.	4.50	4.50	4.50	4.50	4.50
U.S.	3.44	3.47	3.48	3.48	3.46
Differential	1.06	1.03	1.02	1.02	1.04
Covered differential	.39	.31	.35	.42	.39
Euro-\$ - Local authority					
Euro-\$	4.25	4.19	4.25	4.25	4.25
Local authority covered	4.39	4.34	4.34	4.40	4.35
Differential	.14	.15	.09	.15	.10
Euro-\$ - N.Y. certificate of deposit					
Euro-\$ <sup>a/</sup>	4.31	4.25	4.25	4.25	4.25
N.Y. certificate of deposit <sup>a/b/</sup>	3.86	3.85	3.86	3.86	3.86
Differential	.45	.40	.39	.39	.39

<sup>a/</sup> Previous Wednesday.

<sup>b/</sup> Secondary market, offering rates for negotiable certificates of time deposit.

Table 11. United Kingdom: London Fixing Price for Gold: July-August 1964

	July	August			
	31	7	14	21	28
Price per fine ounce (U.S. \$)	35.084	35.081	35.079	35.072	35.081

Source: Bank of England.



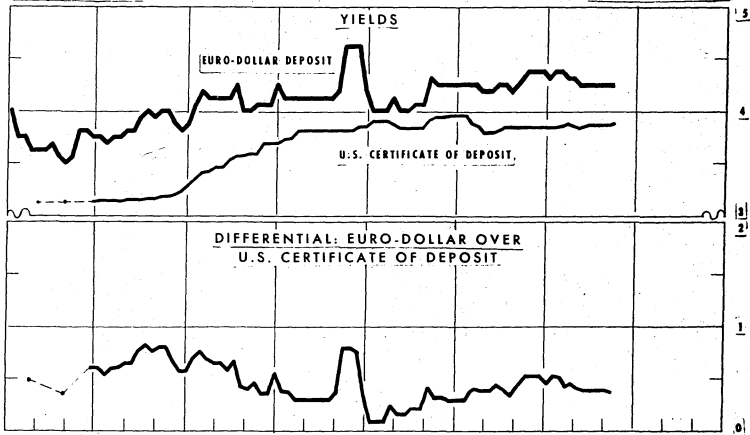
Chart 1

**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

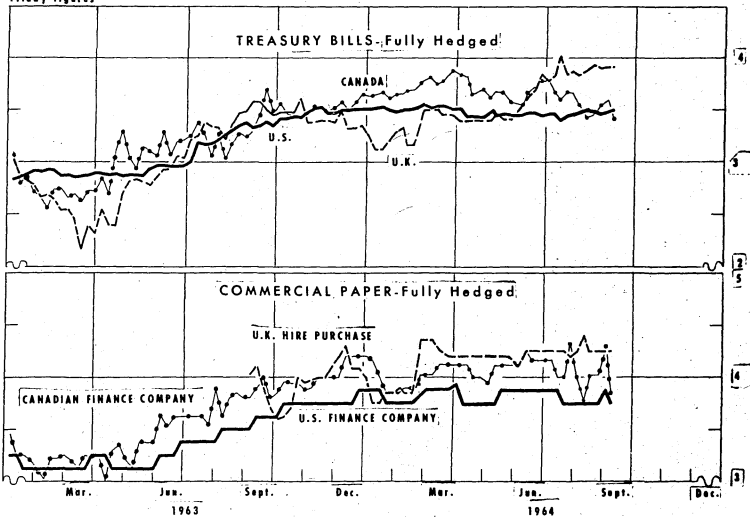
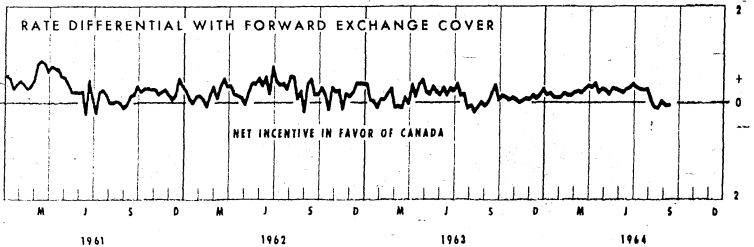
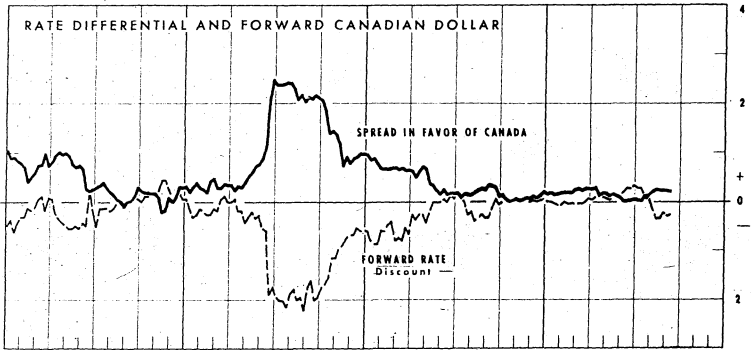
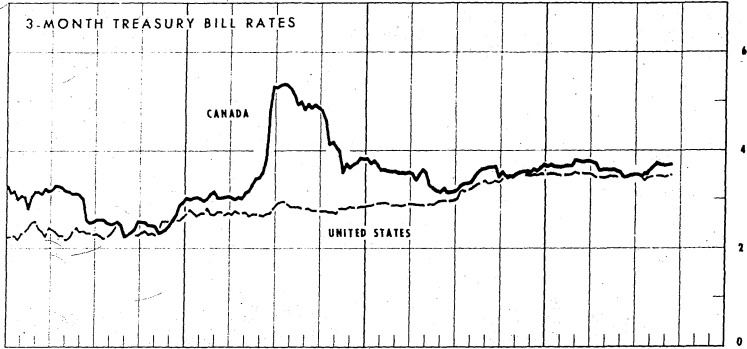


Chart 2

### INTEREST ARBITRAGE, UNITED STATES / CANADA

Friday figures\*

Per cent per annum



\* Thursday figures 1961-1962; Friday thereafter.

Chart 3  
**INTEREST ARBITRAGE, NEW YORK/LONDON**

Friday figures

Per cent per annum

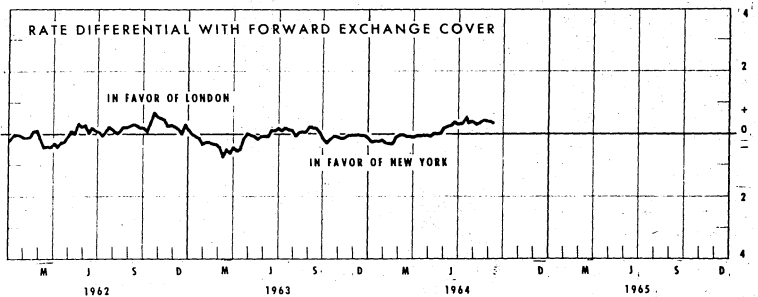
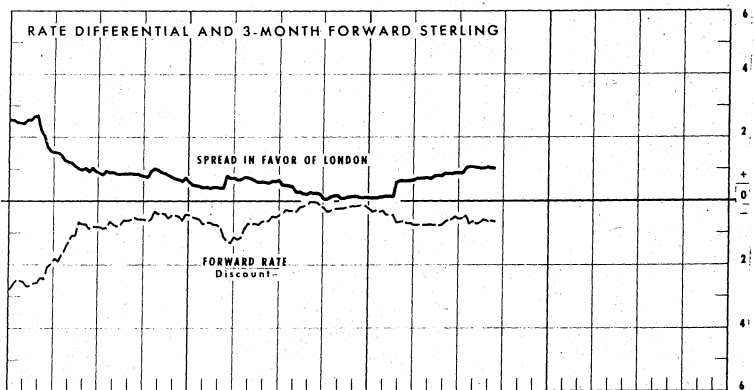
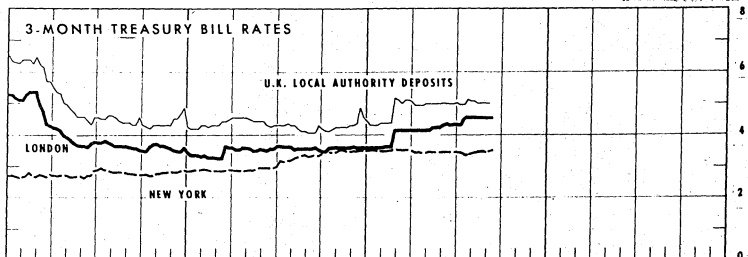


Chart 4  
**INTEREST ARBITRAGE FOR GERMAN COMMERCIAL BANKS**

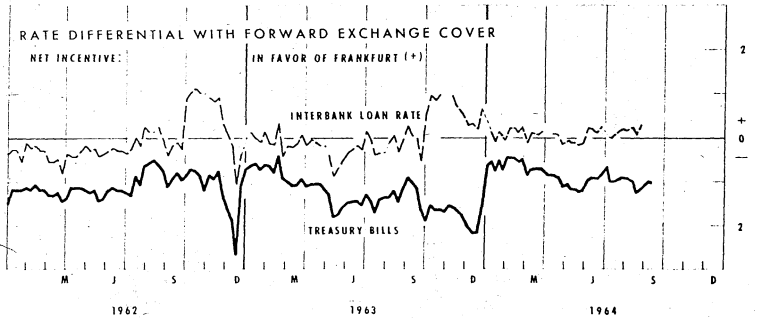
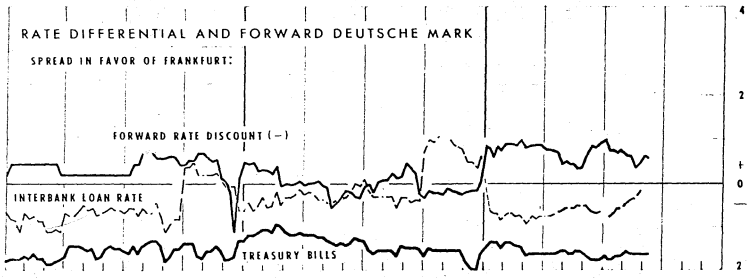
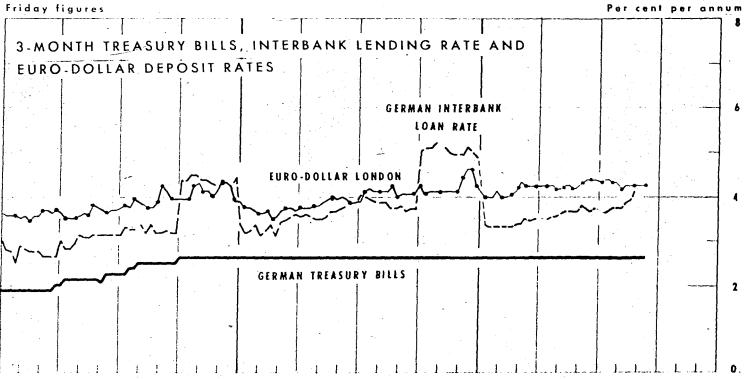
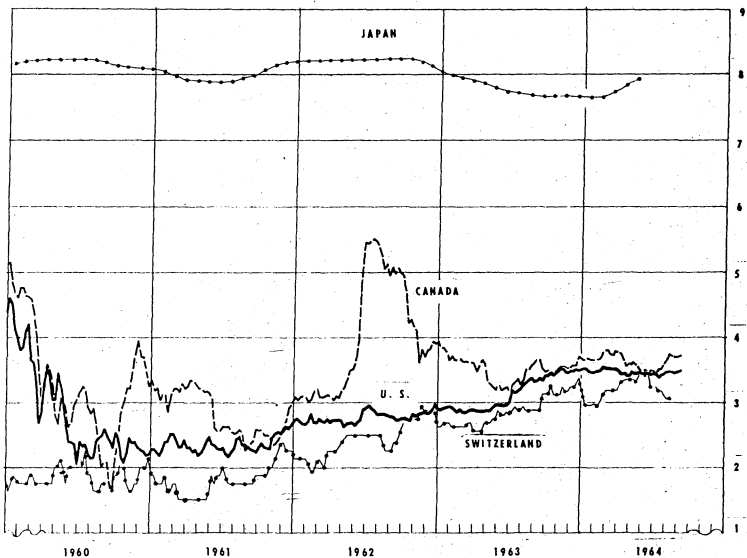
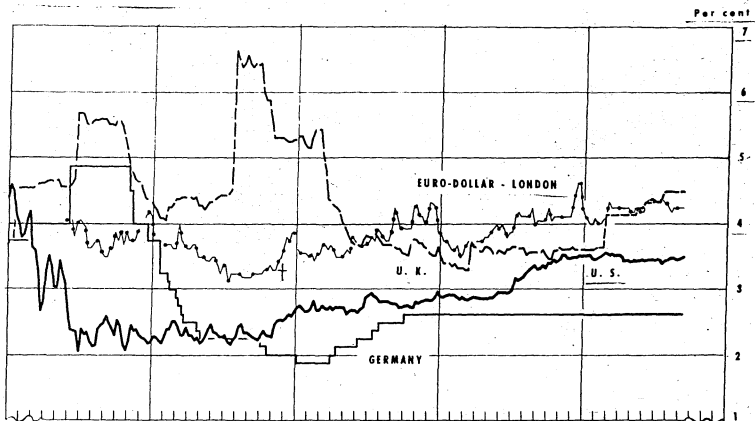


Chart 5  
SHORT-TERM INTEREST RATES \*



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

Chart 6  
**LONG-TERM BOND YIELDS**

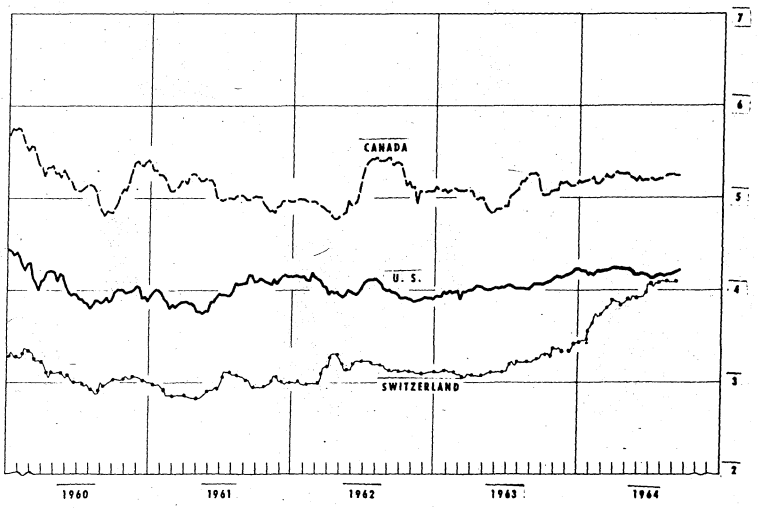
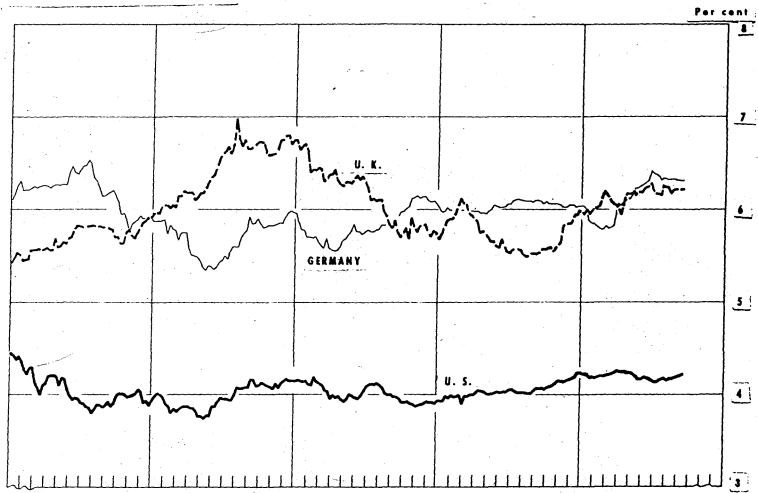
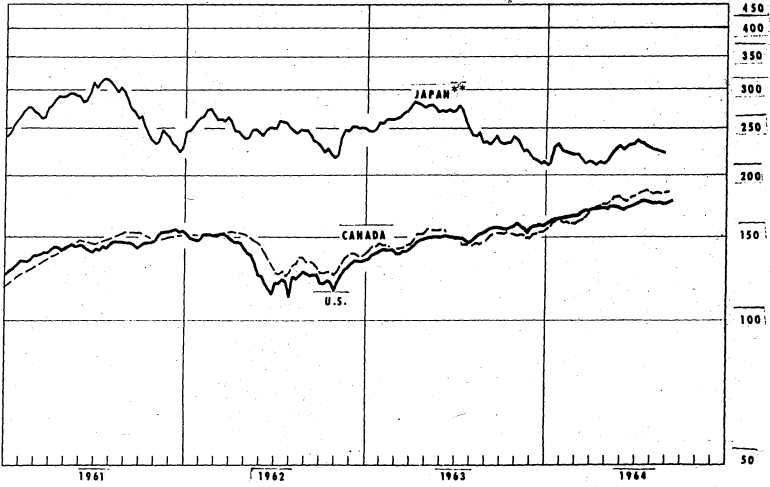
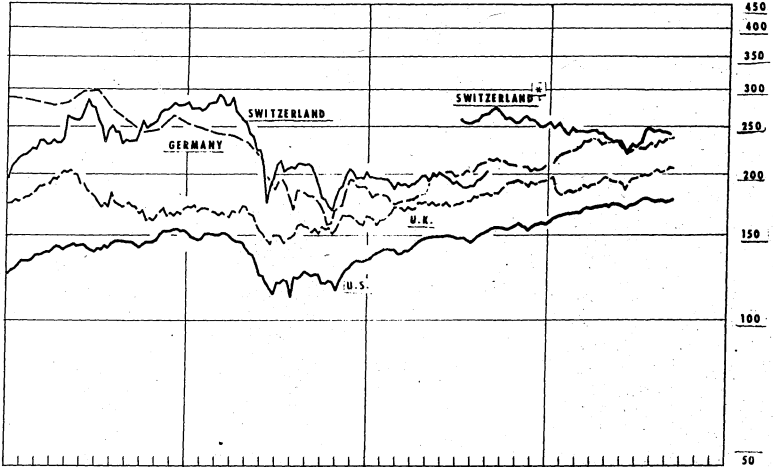


Chart 7  
INDUSTRIAL STOCK INDICES

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**

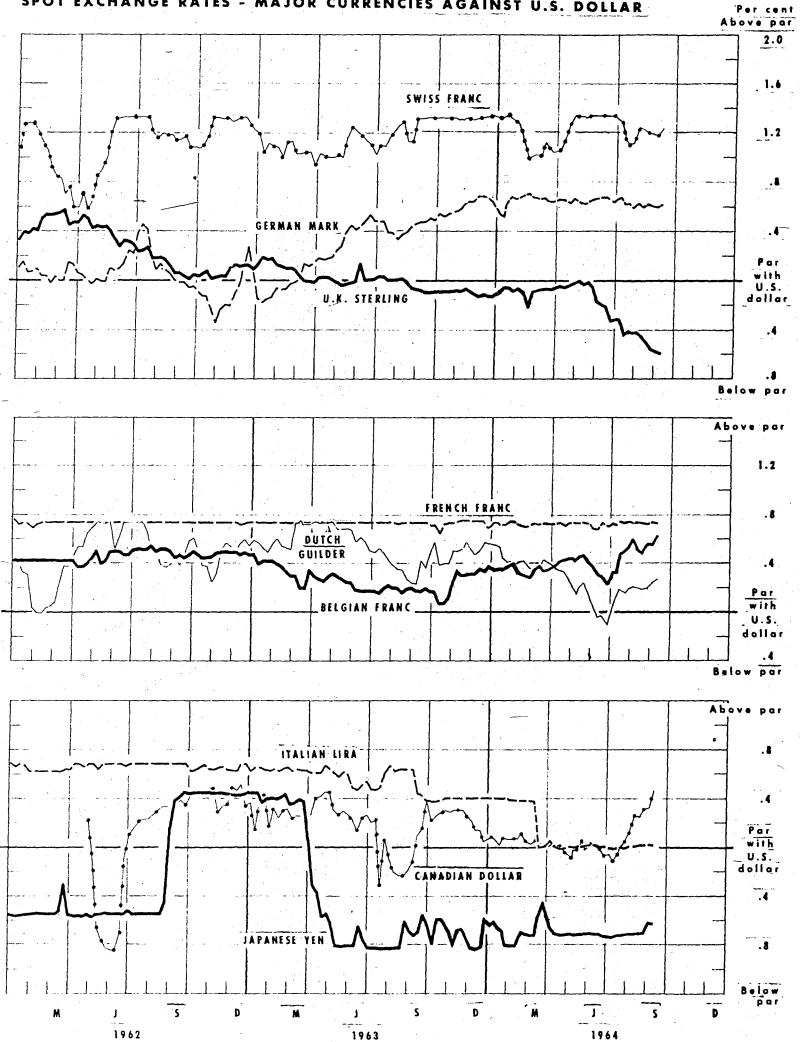




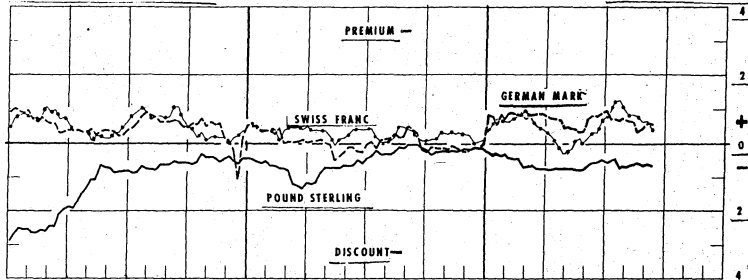
Chart 9

**3-MONTH FORWARD EXCHANGE RATE**

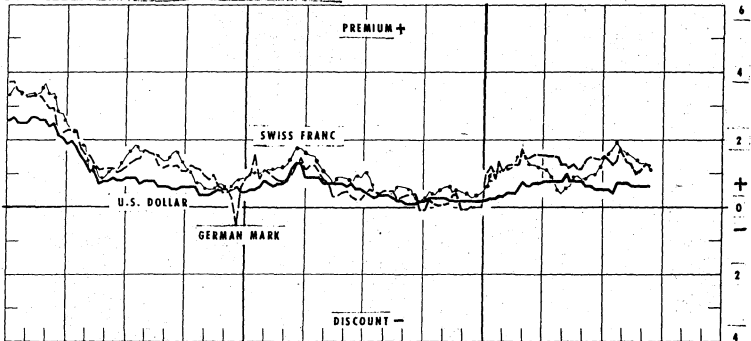
Friday figures

AGAINST U.S. DOLLARS

Per cent per annum



AGAINST POUND STERLING - LONDON



AGAINST POUND STERLING - LONDON

