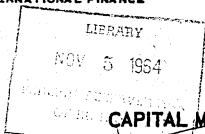


H. 13



No. 169

CAPITAL MARKET DEVELOPMENTS ABROAD

- I. United Kingdom
- II. Nine Charts on Financial Markets Abroad
- III. Latest Figures Plotted in H. 13 Chart Series, 1964

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

Financial markets in the United Kingdom during September and October were dominated by considerations related to the October 15 elections. The firm tone which prevailed in the gilt-edged and stock markets during September and early October gave way to uneasiness when public opinion polls once again began to indicate a Labor Party victory. Throughout the period, the spot pound continued to show weakness, the forward discount widened, but official reserve losses reported for September were not heavy. Nonetheless, up to the week of October 9 the Treasury bill and bond yields were virtually unchanged, stock prices declined only modestly, and the covered differential remained in favor of London. (See Table 1.)

Table 1. United Kingdom: Selected Financial Markets, August-October, 1964

	Actual August 28	Change from previous week to:			
		October			
		2	9	16	23
Interest rates (per cent per annum)					
Treasury bill (tender)	4.65	n.c.	n.c.	+07	n.c.
Government bonds a/					
4% 1965	4.85	-.06	+04	-.05	-.05
3-1/2% 1979-1981	5.82	+03	+02	+01	+04
5-1/2% 2008-2012	6.15	-.03	+02	n.c.	+02
3-1/2% War Loan	6.22	-.02	+02	+01	+01
Stock price index a/ b/	363.8	+ 14	-13.6	+7	-5.2
Exchange rates		(Actual Values)			
Spot rate (U.S. cents)	278.43	278.31	278.34	278.29	278.29
Forward rate (per cent p.o.)	-0.65	-0.75	-0.76	-0.964	-0.915

a/ Previous Thursday.

b/ Financial Times Industrial Ordinary.OFFICIAL USE ONLY
(Decontrolled after 6 months)

In the first days after the election, financial markets behaved erratically. Initially, stock prices--after wide fluctuations--and bond prices were clearly easing downward but they then firmed at the somewhat lower levels. In the foreign exchange market, the spot pound had a somewhat better tone and the forward discount narrowed. But heavy selling pressures were reported during Friday, October 23, when it became known that a major statement of economic policy would be made by the new Labor government on Monday, October 26.

The reaction of financial markets to the actual program was both immediate and favorable: in the stock market, the Financial Times Industrial Ordinary index which rose from a post-elective low of 350.0 on October 19, to 356.6 on October 23, rose further on October 26; and in the gilt-edged market widespread gains were posted. In foreign exchange markets the spot pound rose to 278.53 U.S. cents (up 0.25 U.S. cents from October 23) on October 29, and the forward discount narrowed over the same period from 0.905 to 0.818 per cent per annum.

In September, the Bank of England entered into "Basle type" arrangements with European and North American central banks in preparation for a possible run on sterling. With the exception of the \$500 million swap facility with the Federal Reserve System, the amounts of the individual credit facilities were not made public. However, foreign press estimates of the total amount run as high as \$1 billion.

Not all developments in financial markets in the period under review were election oriented. During September, there was a revival of dollar loans in London totalling \$30 million. In October, the city of Turin floated the very first external sterling loan with a Deutsche-mark option. Although the investment dollar premium inhibited "City" brokers from picking up the issue, subscriptions were so heavy that the amount to be raised was increased from four to five million pounds.

Money markets show mixed behavior. Call money was in short supply during September and the first weeks of October, but the large amounts of assistance given by the Bank of England kept rates somewhat below those prevailing during August. As in previous months, there was no borrowing by the discount houses. Local authority and Euro-dollar 90-day deposit rates moved in opposite directions during this period, perhaps in response to a shifting of funds to Euro-dollar deposits stimulated by election uncertainties. In the Treasury bill market, the rate held firm at 4.50 per cent until October 8. On October 9, it moved up to 4.53 and one week later to 4.59. (See Table 2.) This movement was widely attributed to anticipations of a rise in Bank rate.

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

	August	September					October			
	28	4	11	18	25	2	9	16	23	
Call money <u>a/</u>	4.50	4.38	4.38	4.38	4.44	4.50	4.50	4.50	4.50	
Local authority deposits (90 days)	5.00	5.00	4.94	4.94	5.06	5.12	5.18	5.21	5.40	
Euro-dollar deposits (90 days)	4.25	4.25	4.25	4.19	4.19	4.43	4.50	4.50	4.50	
Treasury bill market rate (91 days)	4.50	4.50	4.50	4.50	4.50	4.50	4.53	4.59	4.59	

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

Election and trade outturns disrupt quiescent capital markets. During September, the demand for gilt-edged bonds remained strong despite the weakening position of sterling and the announcement of continued trade deficits through August. This show of strength continued into the early days of October until public opinion polls began to favor Labor in the election. Market rates then began to rise, and on October 16 when the results were known and when the September trade deficit was announced they rose even further.

The stock market reacted in much the same way to this sequence of events. However, in September prices did fall in response to the announcement of the August trade deficit, and a late rally was staged on the day before balloting. (See Table 3.) Yet the events of October 16 produced strong selling pressure and the Financial Times Industrial Ordinary stock index dropped 10 points.

However, before a week had passed the selling pressure eased in both markets and prices firmed at lower levels. This leveling off was short lived and on October 23, prices again moved downward in anticipation of the new government program to be announced on the following Monday. When the program was actually announced, demand revived in both markets and immediate gains were posted.

New issues (net of redemptions) totaled £ 49 million in September, about the same as in August. However, the composition changed somewhat as foreign borrowers of sterling were again active in the market while borrowing by local authorities declined for the first time in several months. (See Table 4.)

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

	August		September				October			
	27	3	10	17	24	1	8	15	22	
Government bonds										
5% 1967	5.47	5.45	5.45	5.45	5.37	5.37	5.42	5.50	5.52	
3% 1965-1975	5.79	5.79	5.78	5.79	5.79	5.82	5.81	5.84	5.89	
5% 1986-1989	6.07	6.08	6.05	6.05	6.05	6.05	6.07	6.08	6.10	
2-1/2% Consols	6.04	6.04	6.04	6.04	6.03	6.05	6.05	6.07	6.09	
Stocks										
Share yield a/	4.56	4.54	4.55	4.61	4.61	4.59	4.71	4.60	4.69	
Yield gap b/	1.48	1.50	1.99	1.43	1.42	1.49	1.34	1.47	1.40	
Share prices a/	117.53	118.37	118.01	116.53	117.90	118.54	115.70	115.56	113.66	

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

b/ Difference between yield on Consols and Share yield.

Table 4. United Kingdom: Capital Issues (Net of Redemptions)
May-September, 1965
(millions of pounds)

	May	June	July	Aug.	Sept.
U.K. quoted public companies	48.9	34.0	65.0	28.5	33.4
U.K. Local authorities	4.5	7.1	10.3	18.5	10.9
Overseas borrowers	2.3	9.2	0.9	--	4.7
Total	<u>55.7</u>	<u>50.3</u>	<u>76.2</u>	<u>47.0</u>	<u>49.0</u>
Gross Issues	65.6	54.6	89.0	49.2	52.8
Gross Redemptions	9.9	4.3	12.8	2.2	3.8

Source: Bank of England.

The composition of the stock of other credit instruments also changed modestly. In September, outstanding advances by the London clearing banks declined for the first time this year, but the fall was much less than expected for this time of the year. On a seasonally adjusted basis, advances increased by £ 70 million in September--£ 13 million more than in August. Total installment credit outstanding extended by finance houses and department stores rose during August by only 11 million pounds, continuing the slower pace of recent months. At the end of August the total outstanding equaled £ 1,070 million.

Trade deficit continued through September. In August and September, exports continued to exhibit the wide swings of earlier months, but failed to meet the level of imports by ever increasing margins. On a balance of payments basis the third quarter seasonally adjusted current account deficit is estimated at £ 150 million, £ 37 greater than that of the second quarter and £ 81 greater than that of the first. (See Table 5.)

Table 5. United Kingdom: Foreign Trade
June-August, 1964

(Millions of pounds; seasonally adjusted; months or monthly averages)

	<u>July</u>	<u>August</u>	<u>September</u>
Imports (c.i.f.)	430	479	471
Exports (f.o.b.)	331	370	346
Re-exports (f.o.b.)	13	14	14
Balance	- 86	- 93	-111
Trade balance <u>a/</u>	- 40p	- 49p	- 59p

a/ Balance of payments basis.

p Preliminary

Source: Board of Trade.

Sterling weak in pre-election period. The pound continued to weaken throughout September and the early days of October. The spot rate went from 278.39 U.S. cents on September 4 to 278.31 U.S. cents on October 2. Thereafter, until election day it held at these levels and was quoted in New York at 278.37 cents on October 15. Between September 4 and October 16, the forward discount (in per cents per annum) widened by 30 basis points, and the covered differential on Treasury bills narrowed by the same amount. Other arbitrage calculations were similarly affected. The arbitrage incentive swung in favor of Euro-dollar over local authority deposits for the first time since early May. (See Table 6.)

During the immediate post-election period, spot sterling held steady against the dollar and on October 21 was quoted at 278.32 in New York. Over the same period the forward discount narrowed a bit and the small covered differential on Treasury bills remained in favor of London.

Table 6. U.K./U.S. Exchange Rates and Arbitrage Calculations,
August-October, 1964

	August	September				October			
	28	4	11	18	25	2	9	16	23
Exchange rates									
Spot rate (U.S. cents)	278.4	278.39	278.32	278.35	278.33	278.31	278.34	278.28	278.28
Forward rate (per cent per annum)	-0.65	-0.62	-0.66	-0.72	-0.75	-0.75	-0.76	-0.964	-0.905
3-month yields and yield spreads									
Treasury bills									
U.K. (covered)	3.85	3.88	3.84	3.78	3.75	3.75	3.77	3.63	3.69
U.S.	3.46	3.48	3.50	3.52	3.52	3.53	3.56	3.56	3.56
Differential	0.39	0.40	0.34	0.26	0.23	0.22	0.21	0.07	0.13
Euro-\$ - Local authority									
Euro-\$	4.25	4.25	4.25	4.19	4.19	4.43	4.50	4.50	4.50
Local authority (covered)	4.35	4.38	4.28	4.22	4.31	4.37	4.42	4.25	4.49
Differential	0.10	0.13	0.03	0.03	0.12	-0.06	-0.08	-0.25	-0.01
Euro-\$ - New York certificate of deposit									
Euro-\$ a/	4.25	4.25	4.25	4.19	4.19	4.44	4.50	4.50	4.50
New York certificate of deposit a/ b/	3.86	3.88	3.87	3.87	3.87	3.88	3.94	3.94	3.95
Differential	.39	.37	.38	.32	.32	.56	.56	.56	.55

a/ Previous Wednesday

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

However, one week to the day after Labor's victory, it became known that measures to deal with the balance-of-payments difficulties would be made public on the following Monday. The program, announced as scheduled in the form of a white paper entitled "The Economic Situation," called for a 15 per cent surcharge on all imports except food, raw tobacco, and raw materials, and provided for a 1-1/2 per cent tax rebate to exporters. The rebate is an export subsidy since it will be calculated as a percentage of the value of goods shipped as opposed to a percentage of the estimated indirect taxes actually paid by each exporter. After the program was made public, spot sterling strengthened noticeably in foreign exchange markets and was quoted in New York at 278.53 U.S. cents on October 29.

Throughout the first half of October security sterling showed continued weakness and the offer rate fell from 277.95 U.S. cents on October 1 to 277.80 U.S. cents on October 16. However, it has been in demand throughout the past election period and the rate was quoted at 278.25 U.S. cents on October 29.

Official reserves still falling. The decline of £ 45 million in official reserves in September was about one-half the fall recorded in August. (See Table 7.) Nevertheless, the continued reserve losses reflected further weakening in Britain's balance of payments and, more particularly, reduced support from the outer sterling area and from short term capital inflows. During the third quarter, the trade deficit did not widen appreciably, but reserve losses were nearly triple the reserve accruals of the first six months.

Table 7. United Kingdom: Reserve Position:
July-September, 1964
(Millions U.S. dollars)

	July	Aug.	Sept.	Outstanding September 30, 1964
Changes in gold and convertible currencies	-28	-92	-45	2,539
Drawing rights on I.M.F.	-	-	n.a.	a/ 2,441
Total	-28	-92	n.a.	

a/ August 31, 1964.

Source: Bank of England and International Monetary Fund.

Demand for bullion strengthens. During September and October, the price of gold at the London fixing fluctuated around a rising trend, and unsatisfied demands were present on a number of days. At times business was done after the fixing at somewhat higher prices. (See Table 8.) The demand for bullion was particularly strong in the days immediately before and after the election, but eased thereafter.

Table 8. United Kingdom: London Fixing Price for Gold,
August-October, 1964

	August	September					October			
	28	4	11	18	25	2	9	16	23	
Price per fine ounce (U.S. \$)	35.084	35.080	35.081	35.097	35.093	35.120	35.111	35.122	35.104	

Europe and British Commonwealth Section.

- 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 Rate

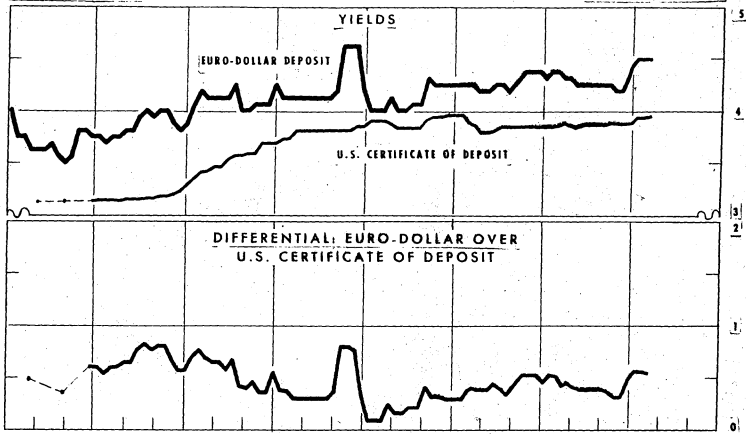
Chart 1

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

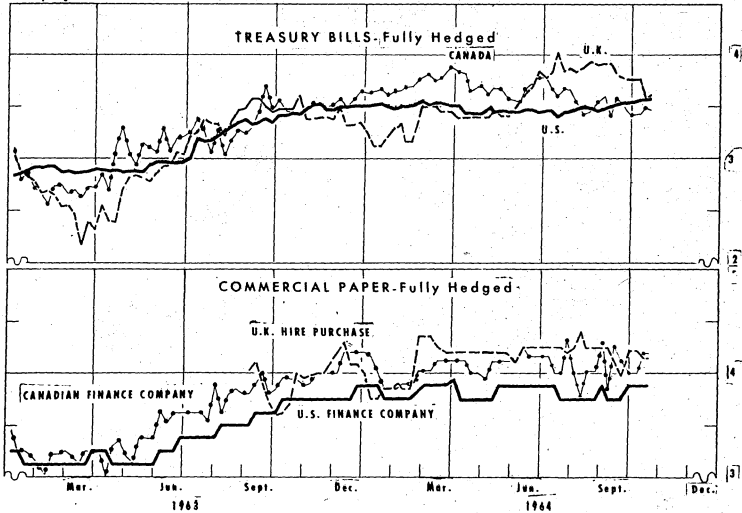
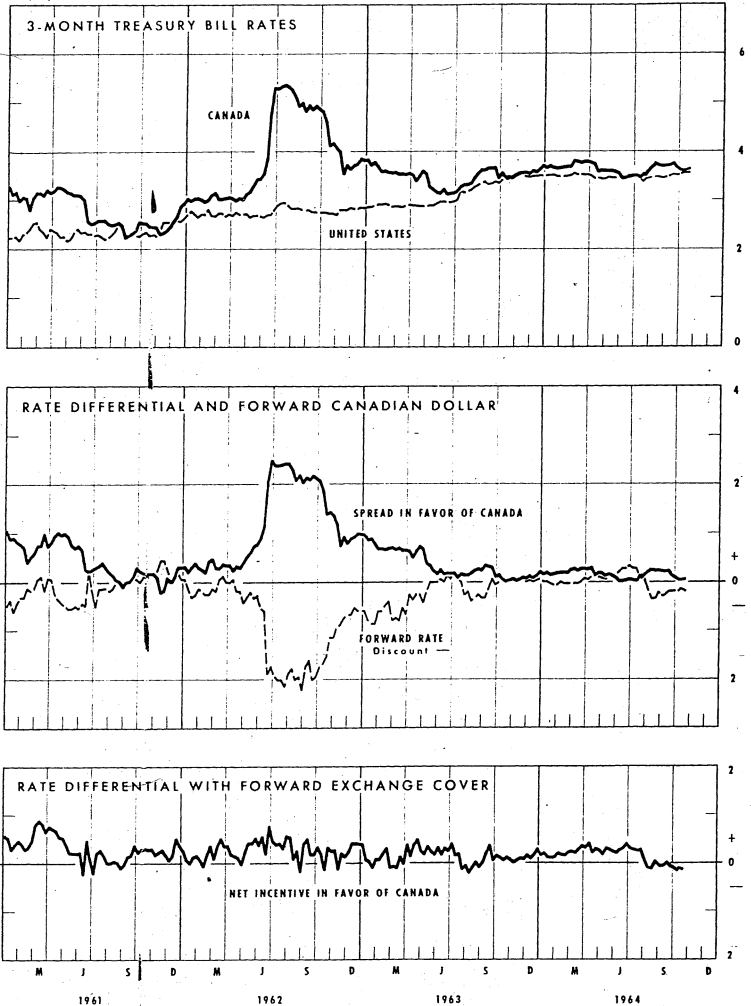


Chart 2

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

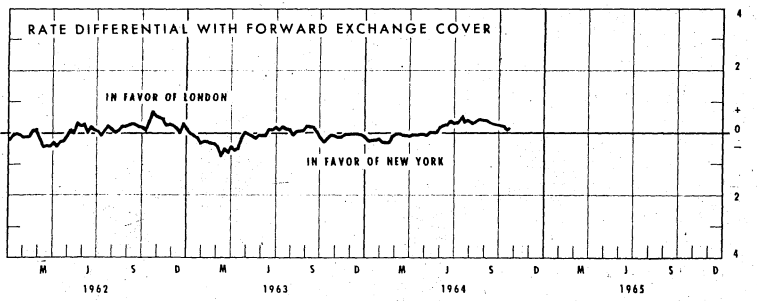
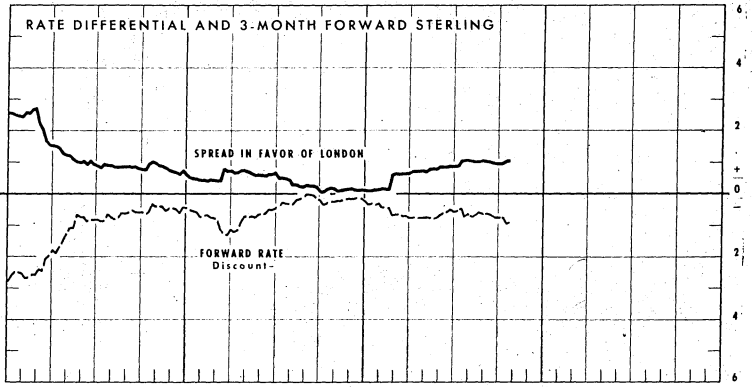
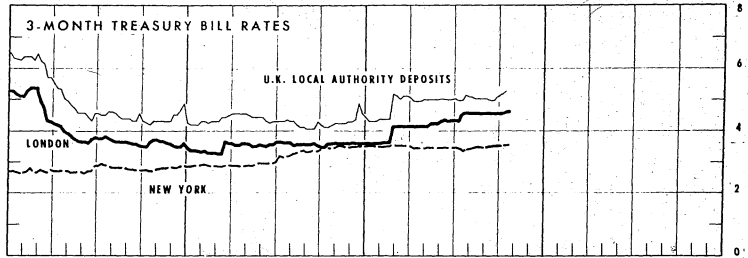


Chart 4
INTEREST ARBITRAGE FOR GERMAN COMMERCIAL BANKS

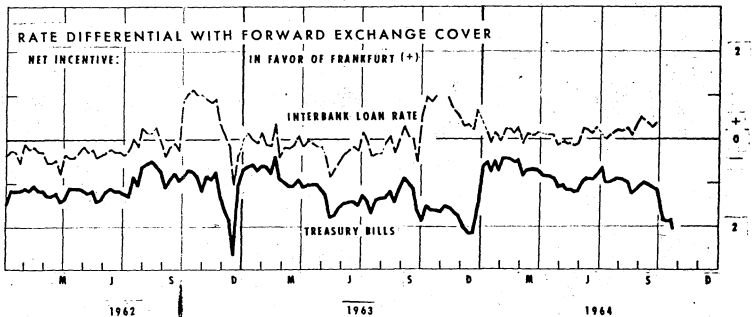
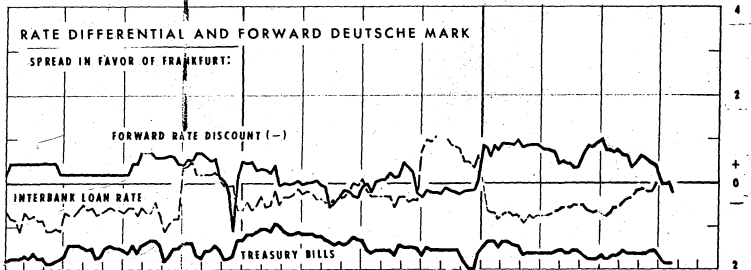
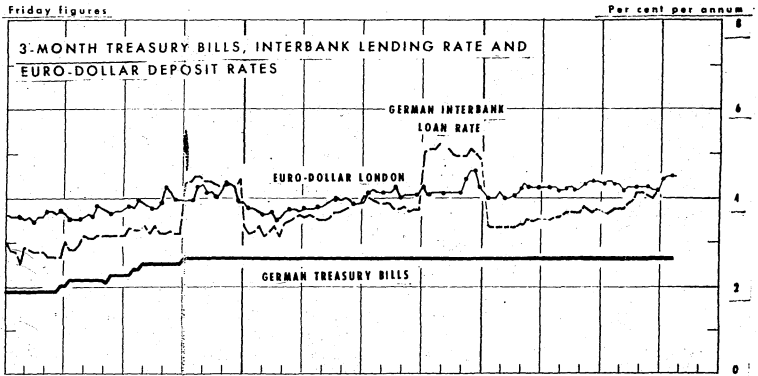
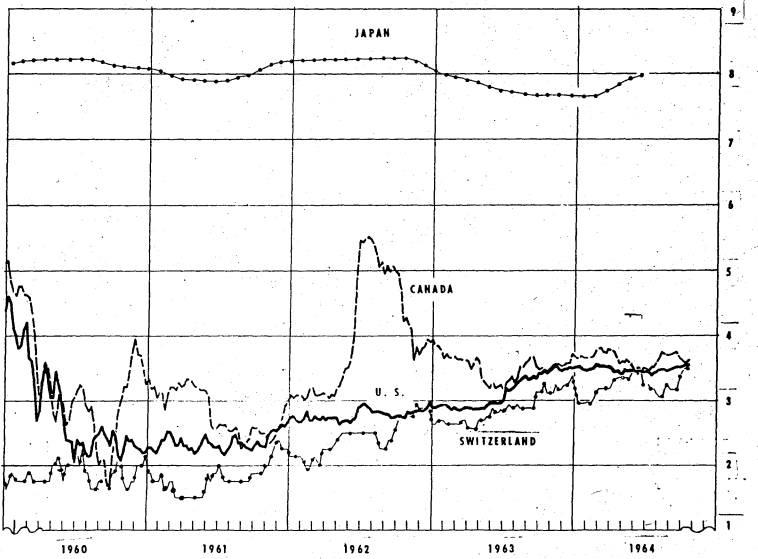
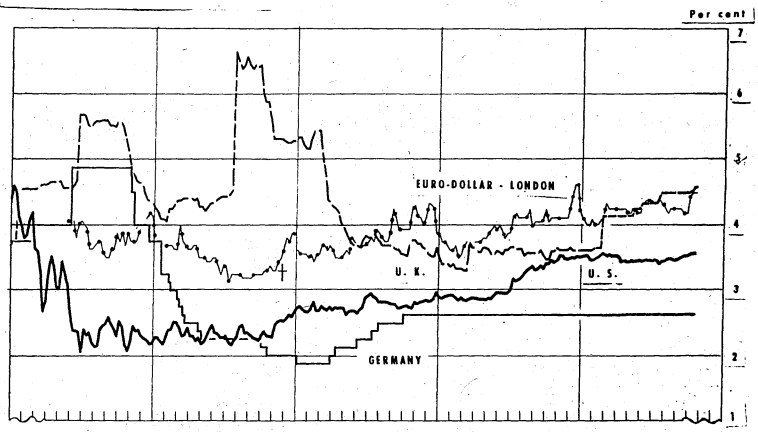


Chart 5
SHORT-TERM INTEREST RATES *



* 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

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Chart 6
LONG-TERM BOND YIELDS

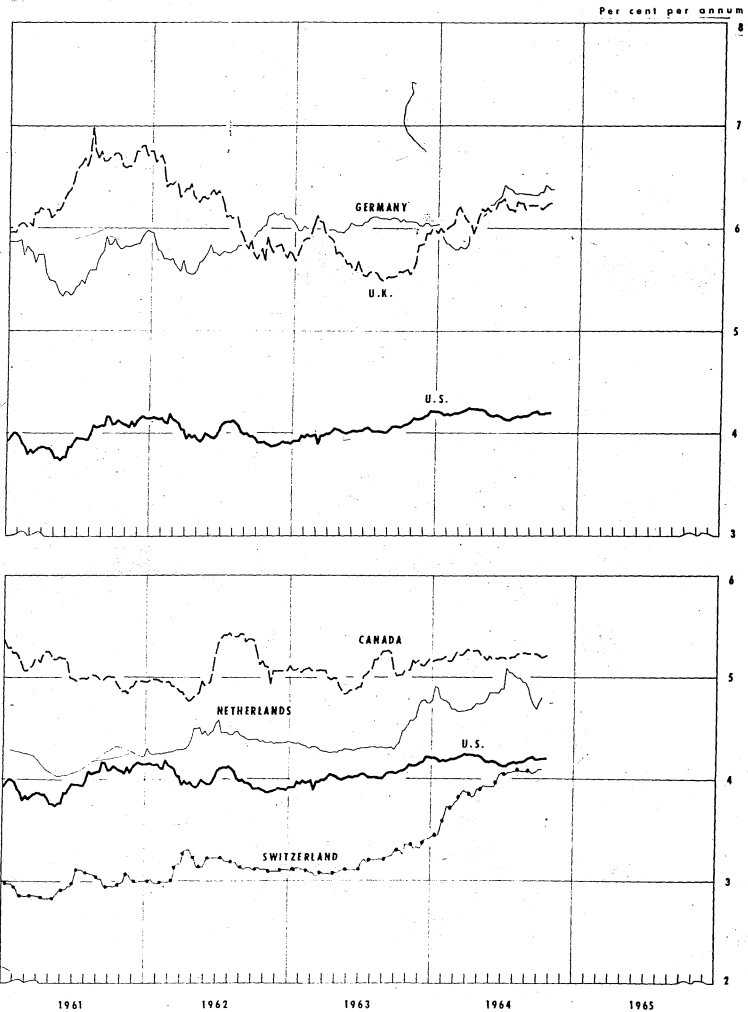
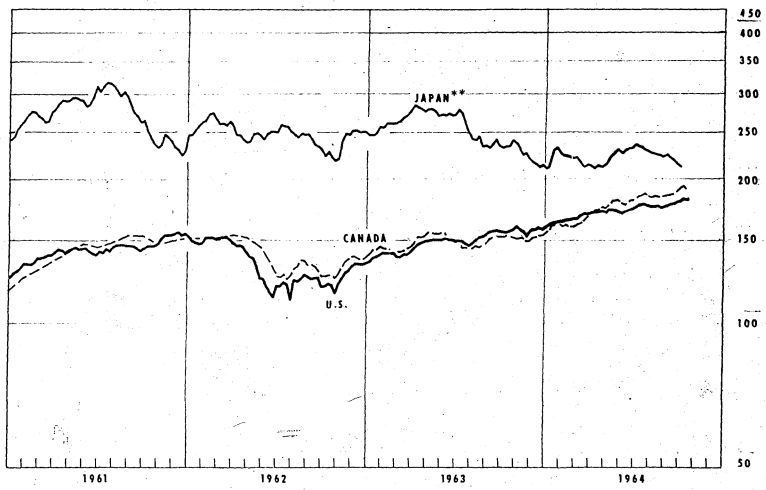
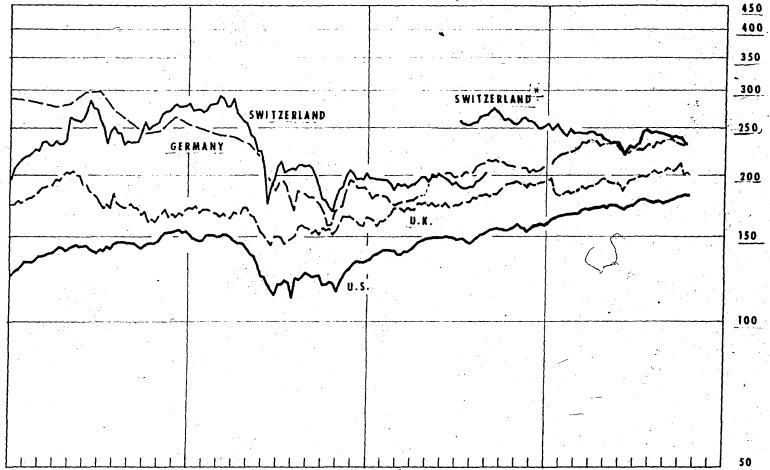


Chart 7
INDUSTRIAL STOCK INDICES

1958=100
Ratio scale



¹ New series Swiss Bank Corporation industrial stock index.
² Japan index of 225 industrial and other stocks traded on the Tokyo exchange.

Chart 8

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

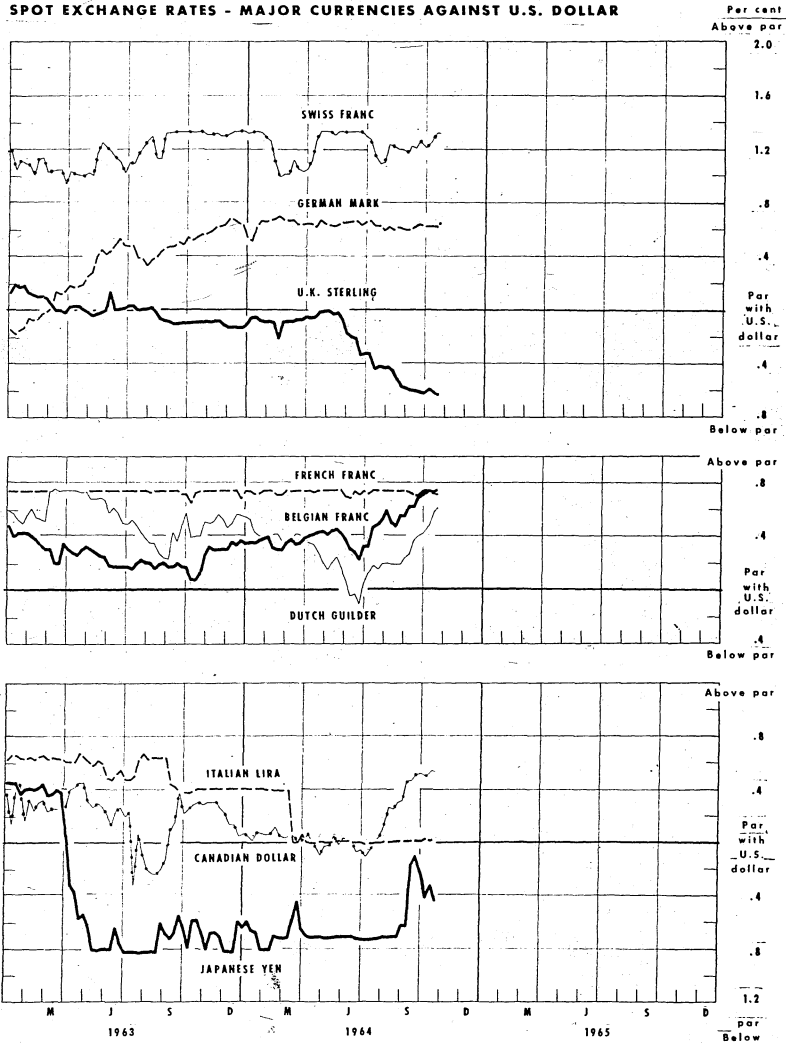
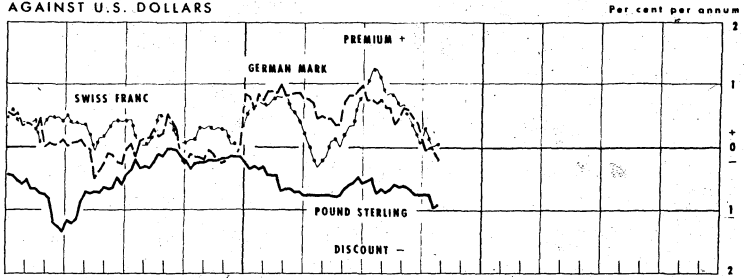
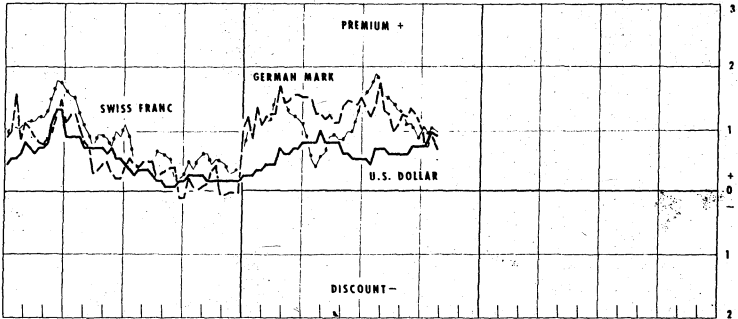


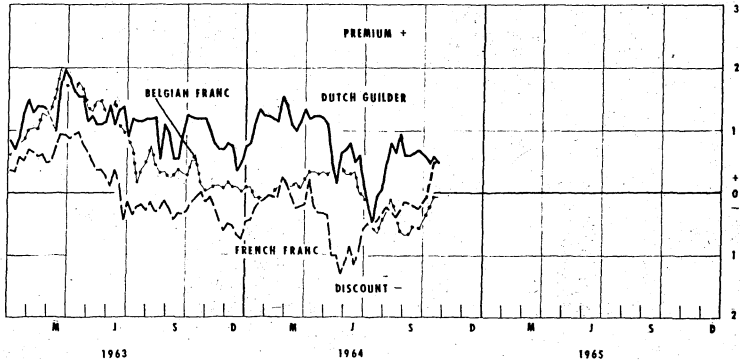
Chart 9
3-MONTH FORWARD EXCHANGE RATES
Friday figures
AGAINST U.S. DOLLARS



AGAINST POUND STERLING - LONDON



AGAINST POUND STERLING - LONDON



III. Latest Figures Plotted In H.13 Chart Series

<u>Chart 1</u>	<u>Per cent per annum</u>	<u>Chart 5</u>	<u>Per cent per annum</u>
<u>Upper panel</u>		(Friday, October 23, except as noted)	
(Wednesday, October 21)	—	Treasury bills:	
Euro-\$ deposit	<u>4.50</u>	U.S.	<u>3.56</u>
U.S. certif. of deposit	<u>3.95</u>	U.K.	<u>4.59</u>
<u>Lower panels</u>		Germany	<u>2.63</u>
(Friday, October 23)		Canada	<u>3.63</u>
Treasury bills: U.S.	<u>3.57</u>	Swiss 3-month deposits (Date: October 15)*	<u>3.50</u>
U.K.	<u>3.61</u>	Euro-\$ deposit (London)	<u>4.50</u>
Canada	<u>3.46</u>	Japan: composite rate (Date: June 26)	<u>7.979</u>
Finance Co. paper: U.S.	<u>3.88</u>	<u>Chart 6</u>	
Canada	<u>4.20</u>	Bonds:	
Hire-purchase paper, U.K.	<u>4.15</u>	U.S. govt. (Wed., October 21)	<u>4.20</u>
<u>Chart 2</u>		U.K. war loan (Thurs., October 15)	<u>6.23</u>
(Friday, October 23)		German Fed. Railway (Fri., October 23)	<u>6.37</u>
Treasury bills: Canada	<u>3.63</u>	Swiss Confederation (Fri., October 9)	<u>4.10</u>
U.S.	<u>3.56</u>	Canadian govt. (Wed., October 21)	<u>5.21</u>
Spread favor Canada	+0.07	Netherlands govt. perpetual (Fri., October 9)	<u>4.81</u>
Forward Canadian dollar	-0.20	* September 23	<u>3.19</u>
Net incentive (Canada +)	-0.13	September 30	<u>3.38</u>
<u>Chart 3</u>		October 7	<u>3.50</u>
(Friday, October 23)			
Treasury bills: U.K.	<u>4.59</u>		
U.S.	<u>3.56</u>		
Spread favor U.K.	+1.03		
Forward pound	-0.90		
Net incentive (U.K. +)	+0.13		