

H. 13
No. 206

July 28, 1965

CAPITAL MARKET DEVELOPMENTS ABROAD

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

I. United Kingdom: Money and Capital Market Developments, June-July 1965

The foreign exchange markets for sterling responded favorably to the stabilization measures announced on July 27. Spot sterling rose from 279.09 (U.S. cents) on July 26 to 279.26 on July 28; however the forward discount widened slightly from 1.96 to 2.02 per cent.

Prior to the announcement of new measures, the foreign exchange market for sterling weakened sharply during the period under review, largely because of disappointing trade returns for May and June. Selling pressure was particularly heavy in mid-June and again in mid-July. Between June 11 and July 23 the spot rate fell from 279.36 to 279.01 (U.S. cents) and the forward discount widened from 1.68 to 1.98 per cent per annum. By contrast there was little activity in domestic financial markets: government bond yields moved fractionally and stock prices eased as buyer interest remained dormant. (See Table 1.)

Table 1. United Kingdom: Selected Financial Market Indicators
June-July 1965

	Actual <u>June</u>	Changes from previous				Actual <u>July</u>
		date to				
		<u>June</u>	<u>July</u>			
	<u>11</u>	<u>18</u>	<u>9</u>	<u>16</u>	<u>23</u>	<u>23</u>
Interest rates						
Treasury bill <u>a/</u>	5.62	-0.02	+0.02	+0.03	0.00	5.65
Government bonds <u>b/</u>						
5% 1967	6.40	+0.10	+0.02	+0.08	-0.08	6.52
5% 1971	6.66	+0.08	+0.01	+0.06	-0.03	6.87
3-1/2% 1979-81	6.50	+0.05	0.00	+0.02	-0.05	6.62
5-1/2% 2008-12	6.75	+0.02	0.00	+0.02	-0.03	6.77
3-1/2% War Loan	6.73	+0.06	+0.06	+0.03	-0.05	6.83
Stocks <u>b/ c/</u>						
Price index	105.56	-2.04	-4.06	+1.00	-0.17	100.27
Share yield	5.61	+0.12	+0.19	-0.06	+0.02	5.94
Exchange rates						
Spot (U.S. cents)	279.36	-0.22	-0.10	-0.03	0.00	279.01
Forward (per cent per annum)	-1.68	-0.28	+0.14	-0.03	-0.13	-1.98

a/ Maximum tender.b/ Previous Thursday.c/ Financial Times 500 industrials.OFFICIAL USE ONLY
(Decontrolled after six months)

Partly in response to the weakening tone of the pound sterling in foreign exchange markets and the halting pace of improvement in the external accounts, Chancellor of Exchequer Callaghan on July 27 announced further measures designed to bolster Britain's external position. These measures fall into three broad categories: (1) curbs on private and public sector spending; (2) steps to restrain imports and spur exports; and (3) measures to cut back the rate of capital outflow.

In order to promote exports the government: (1) reduced from £50,000 to £25,000 the minimum value of a foreign buyer's promissory note qualifying for discount at the fixed rate of 5-1/2 per cent; and (2) reduced the cost of short-term export finance given by banks from Bank Rate plus one per cent to Bank Rate.

To restrain imports, government agencies were instructed to postpone as much as possible the overseas purchase of equipment and stores. In addition, the Bank of England requested the commercial banks to exercise careful surveillance over import finance demands--especially for overseas purchase of manufactures for immediate consumption or inventory build-up. Further, prepayment for imports will not be allowed prior to shipment of the goods. To restrain the capital outflow, the government directed that: (1) official foreign exchange would no longer be made available for direct investment outside the sterling area; (2) special permission would have to be obtained for the granting of bank loans to non-resident controlled U.K. corporations (such corporations will in the future have to satisfy their financing needs by importing capital); and (3) proceeds of life insurance policies and assets of immigrants redesignated as U.K. residents must be surrendered to the government at the official exchange rate. In an attempt to curb domestic demand the new measures provide for a reduction in capital spending by all levels of government. In addition, local authority mortgage lending is to be reduced from the £180 million annual rate for fiscal 1965 to £130 million for 1965-66, and the remaining £481 million of the £360 million allotted to them in the April budget is to be phased more gradually over the next nine months. To further restrain consumer demand, the maximum maturity of hire-purchase contracts was reduced from 36 to 30 months.

Money market conditions remain tight. Tight conditions continued to prevail in British money markets during June and July; however rate movements were diverse owing to special factors. (See Table 2 and Charts 1 and 5.)

Call money was generally on the short side for most of the period under review and the rates tended to rise. (See Table 2.) The Bank of England bought Treasury bills on a number of occasions, in order to ease the situation. However, in early July the discount houses were forced to borrow at Bank rate--at times quite large amounts--in order to balance their books.

Table 2. United Kingdom: Selected Money Market Rates June-July 1965
(per cent per annum)

	June			July			
	<u>4</u>	<u>11</u>	<u>25</u>	<u>2</u>	<u>9</u>	<u>16</u>	<u>23</u>
Call money	5.38	5.38	5.50	5.38	5.38	5.44	5.44
Deposit rates:							
Less than 3 days							
Local authority	6.06	5.94	6.25	6.13	6.00	5.94	6.00
Euro-\$	4.38	4.38	4.38	4.38	4.38	4.25	4.00
90-day							
Local authority:	6.37	6.44	6.56	6.38	6.38	6.38	6.44
Euro-\$	5.12	5.00	4.88	4.88	4.88	4.5	4.56
Treasury bill	5.56	5.49	5.46	5.42	5.49	5.54	5.54

The occasion for borrowing by the discount houses was, as it has been repeatedly in the past, a downward slide in the Treasury bill rate. Between June 4 and July 2 the market rate on Treasury bills fell from 5.56 to 5.42 per cent, and the continuing short supply of Treasury bills led the discount houses to raise their bid at the weekly tenders. After particularly large loans on July 5 and 6, the houses raised their bid on July 9 and again on July 16. As a result, the market rate on Treasury bills climbed to 5.54 per cent on July 16, and has since been maintained at that level.

In the local authority deposit market rates continued the easing tendency that began last April (See Table 2 and Chart 3.) This development suggests that the local authorities might well be meeting their cash needs from sources other than short-term borrowing. First, cash receipts from local taxes are seasonally high during the second calendar quarter. Secondly, the authorities continued to draw heavily upon the Public Works Loan Board and the long-term market for funds during June. For the April-June period borrowing from the government reached £179 million--£26 million in June--while market borrowing in long-forms totalled £64.5 million--£25.5 million in June. The amount borrowed from the government by the end of June accounted for 50 per cent of the total allocated in the April budget for the entire 1965-66 fiscal year. Finally, the continued easing of Euro-dollar rates (See Table 2 and Chart 5) enabled the authorities to offer lower deposit rates without doing serious damage to their competitive position.

Capital Markets still exhibit an uneasy tone. The uneasy tone of British capital markets which has been evident for some time was not materially affected by the new stabilization measures. According to market reports, trading volume remained at a low level on July 27 while stock prices and government bond yields moved only fractionally.

From early June to mid-July bond yields generally eased and stock prices fell off, especially after the mid-month announcements of adverse trade returns for May and June. (See Table 1 and Chart 6.) Reportedly, market activity was at a low ebb, with buyer interest particularly dormant.

Growth of private sector borrowing shows easing tendency. There was a modest decline in the rate of growth of private sector borrowing during the second quarter of 1965 compared to the first three months of the year. In particular, the level of bank advances fell sharply and the growth of building society loans and new issues by U.K. corporations eased. However, installment credit continued its strong advance through April and May. (See Table 3.)

Table 3. United Kingdom: New Borrowing by the Private Sector 1964-65
(£ m)

	1964				1965		Outstanding June 30, 1965
	I	II	III	IV	I	II	
Bank advances <u>a/</u>							
Actual	231	76	135	105	174	-12	4626
Seasonally adj.	50	105	210	210	-35	15	4575
Installment credit <u>b/</u>	26	55	42	31	24 <u>c/</u>	39 <u>d/</u>	1178
Net issues by U.K. corporations	175	138	126	71	87	62	--
Advances by building societies	227	272	285	273	234	220	--

a/ London clearing banks.

b/ Finance houses and department stores.

c/ April-May.

d/ May 31, 1965.

This easier tendency in the rate of borrowing appears to be more than seasonal, suggesting that the general credit squeeze is having some effect. Seasonally adjusted bank advances have shown a slight downward tendency since the first of the year. In addition, corporate issues and advances by the building societies were much lower in the first six months of 1965 than they were during the same period one year ago. Data on installment credit since the increase in early June in down-payment requirements are not yet available.

The prospects for continued easing are at best uncertain. Bank advances should remain in check because of the 5 per cent growth ceiling, and the growth of consumer credit may be halted by the measures imposed by the Board of Trade in June and July. However, U.K. corporations are reportedly turning increasingly to the issues market because of the squeeze on bank loans. In addition, building society loans are expected to rise over the coming months because net deposit inflows have jumped substantially since deposit rates were raised early in June.

No improvement in the foreign trade position. Britain's foreign trade position continued to slip in June: although imports, as expected, fell back from their May peak, exports continued to ease. (See Table 4.)

Table 4. United Kingdom: Foreign Trade 1964-65
(fm, seasonally adjusted, monthly or monthly average)

	1964	1965				
		<u>I</u>	<u>April</u>	<u>May</u>	<u>June</u>	<u>II</u>
Imports (c.i.f.)	475	458	477	501	471	483
Exports (f.o.b.) <u>a/</u>	381	396	400	392	389	393
Difference	-84	-62	-77	-109	-82	-90
Trade balance <u>b/</u>	-46	-13	-30	- 56	-33	-40

a/ Includes re-exports.

b/ Balance of payments basis.

For the second quarter, imports rose 5.5 per cent above January-March levels while exports remained stagnant at the average levels for the first three months of the year. However, the first quarter improvement in the foreign trade position was so substantial that by mid-year exports were 4 per cent above and imports 1 per cent below the average monthly values for 1964. (See Table 4.)

Foreign exchange reserves slip in June. Britain's official holdings of gold and foreign exchange fell by \$67.2 million in June to a level of \$2.8 billion. (See Table 5.) However, British Treasury officials let it be known that during the month the government had made use of central bank credits.

Table 5. United Kingdom: Official Holdings of Gold and Foreign Exchange January-June 1965
(\$ m)

	Changes in:						Total holdings June 30 1965
	<u>Jan.</u>	<u>Feb.</u>	<u>Mar.</u>	<u>April</u>	<u>May</u>	<u>June</u>	
Gold and foreign exchange	-16.8	+64.4	-33.6	+22.4	+506.8	-67.2	2791.6

Table 6. United Kingdom: Exchange Rates and Arbitrage Calculations June-July, 1965

	June			July			
	<u>4</u>	<u>18</u>	<u>25</u>	<u>2</u>	<u>9</u>	<u>16</u>	<u>23</u>
Exchange Rates							
Spot (U.S. cents)	279.42	279.14	279.15	279.09	279.04	279.01	279.01
Fwd. (p.c. p.a.)	-1.82	-1.96	-1.60	-1.93	-1.82	-1.85	-1.98
Three month yields and yield spreads							
Treasury bills							
U.K. (covered)	3.67	3.46	3.79	3.43	3.56	3.61	3.48
U.S.	3.82	3.77	3.74	3.80	3.84	3.82	3.79
Difference	-0.15	-0.31	+0.05	-0.37	-0.28	-0.21	-0.31
Deposit rates							
Local authority (covered)	4.55	4.48	4.96	4.44	4.56	4.53	n.a.
Euro-\$	5.12	5.00	4.88	4.88	4.88	4.75	4.56
Difference	-0.57	-0.52	+0.08	-0.44	-0.32	-0.22	n.a.
Euro-\$ a/ New York C.D.'s a/ b/	5.25	5.06	4.88	4.81	4.81	4.75	4.75
Difference	+0.91	+0.77	+0.59	+0.52	+0.48	+0.44	+0.47

a/ Previous Wednesday.

b/ Secondary offering rates for N.Y. negotiable certificates of deposit.

Sterling weakens sharply in June and July. The sterling foreign exchange markets responded favorably to the latest stabilization measures. Between July 26 and 28 the spot pound rose from 279.09 (U.S. cents) to 279.26; however, the forward discount widened slightly from 1.96 to 2.02 per cent per annum.

Prior to the July 27 announcement of new measures to bolster the pound, the tone of the sterling foreign exchange markets weakened sharply. Between June 4 and July 23 the spot pound fell from 279.42 (U.S.cents) to 279.01 and the forward discount widened from 1.82 to 1.98 per cent per annum. (See Table 6 and Charts 8 and 9.) Selling pressure was particularly acute in mid-June and again in mid-July.

During the period under review the discount on three month sterling fluctuated a good deal making for marked movements in the covered differentials between comparable U.S.-U.K. paper. For the most part however, arbitrage incentives remained against London. (See Table 6 and Charts 8 and 9.) The covered spread on Treasury bills favored New York by amounts varying from 15 to 37 basis points. In the market for deposit pounds, Euro-dollars earned anywhere from 22 to 57 basis points more than covered local authority deposits. Finally, the yield spread between Euro-\$ and New York C.D.'s remained large during the period under review, but it did show a narrowing tendency.

Price of gold rises in the London market. There was a substantial increase in the demand for gold during the period under review and the London fixing price rose sharply. Between June 11 and July 23, the price per fine ounce rose steadily from \$35.0949 to 35.1477. (See Table 7.)

Table 7. United Kingdom: London Fixing Price for Gold June-July 1965
(U.S. dollars)

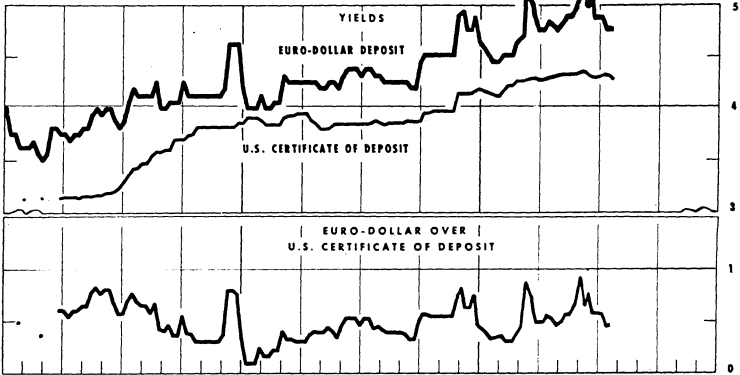
	June			July			
	<u>4</u>	<u>11</u>	<u>25</u>	<u>2</u>	<u>9</u>	<u>16</u>	<u>23</u>
Price per fine ounce	35.1013	35.0949	35.1056	35.1067	35.1063	35.1096	35.1477

Chart 1

INTERNATIONAL MONEY MARKET YIELDS FOR U.S. DOLLAR INVESTORS

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

Wednesday figures



SELECTED INTERNATIONAL MONEY RATES

Friday figures

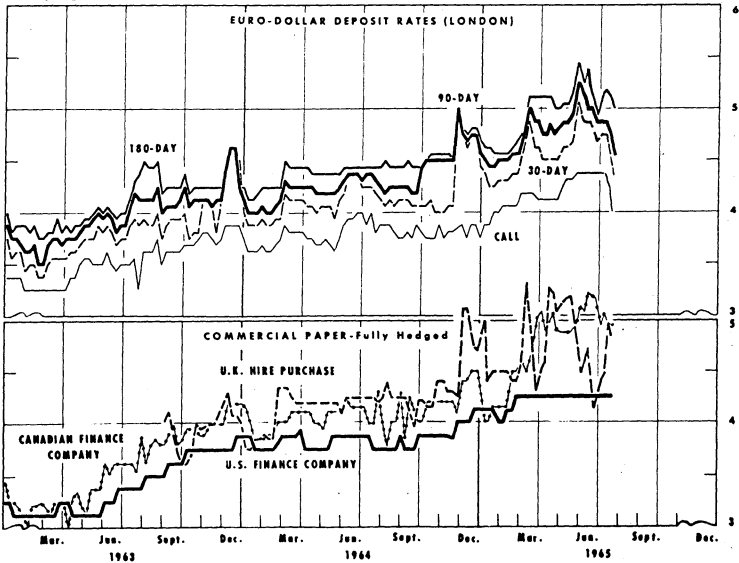
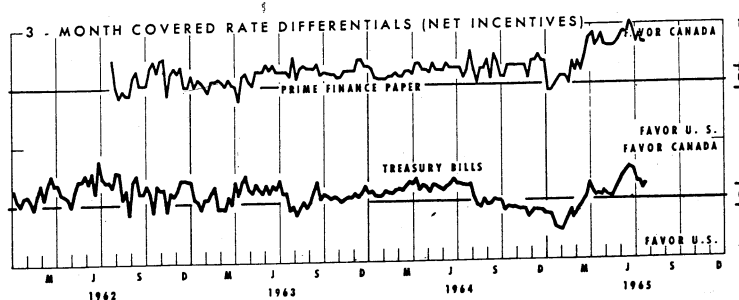
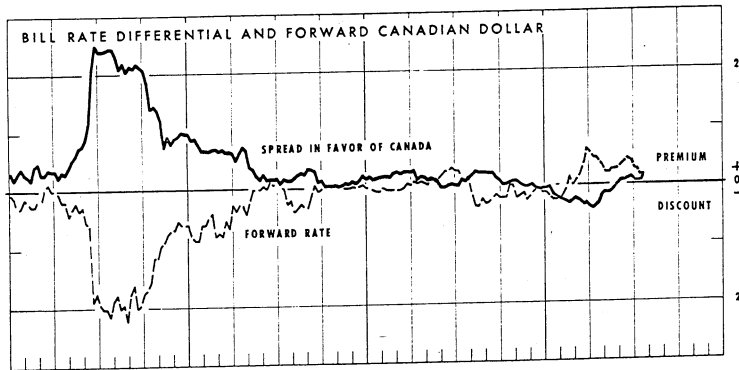
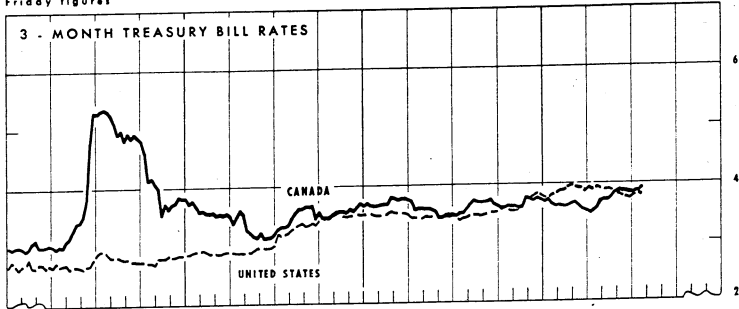


Chart 2

INTEREST ARBITRAGE, UNITED STATES / CANADA

Friday figures*

Per cent per annum



Thursday figures 1962, Friday thereafter.

Chart 3

INTEREST ARBITRAGE, NEW YORK/LONDON

Friday figures

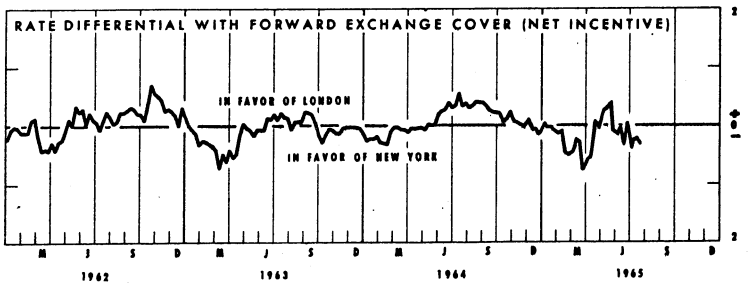
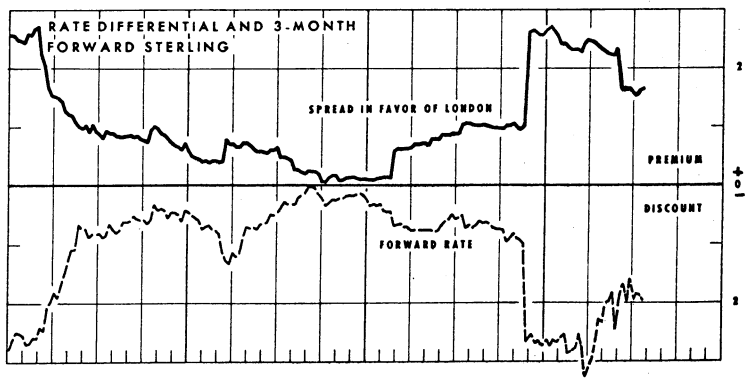
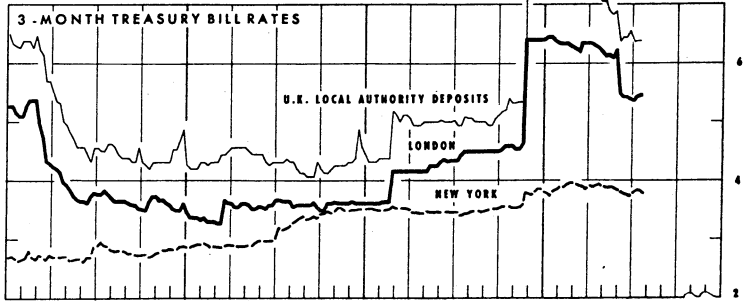


Chart 4

INTEREST ARBITRAGE FOR GERMAN COMMERCIAL BANKS

Friday figures

Per cent per annum

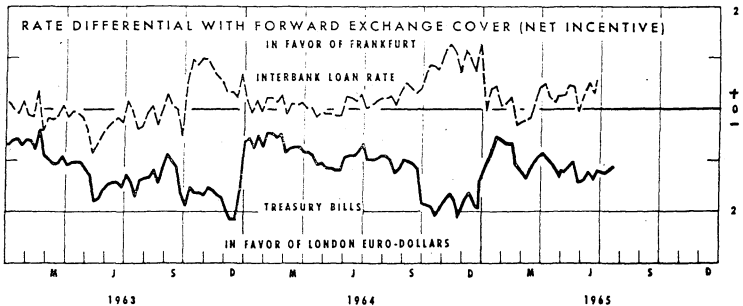
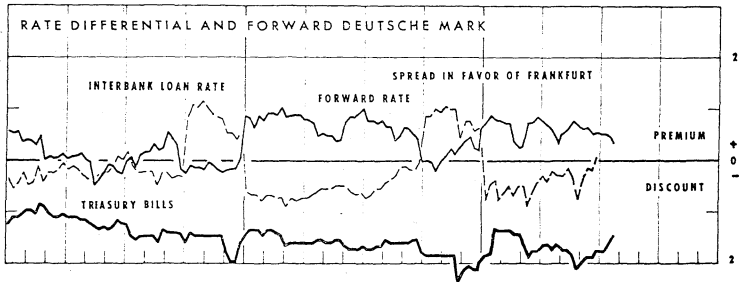
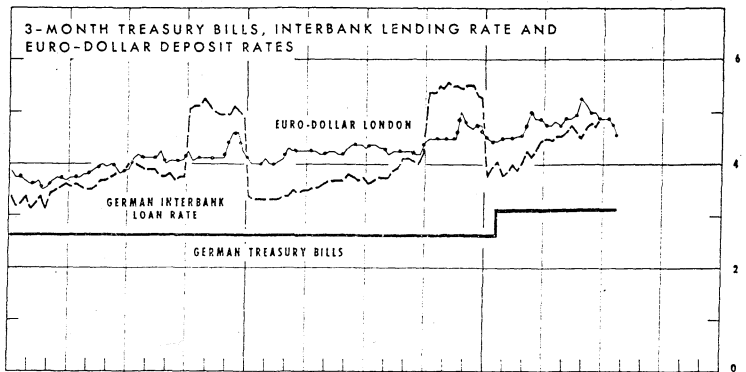
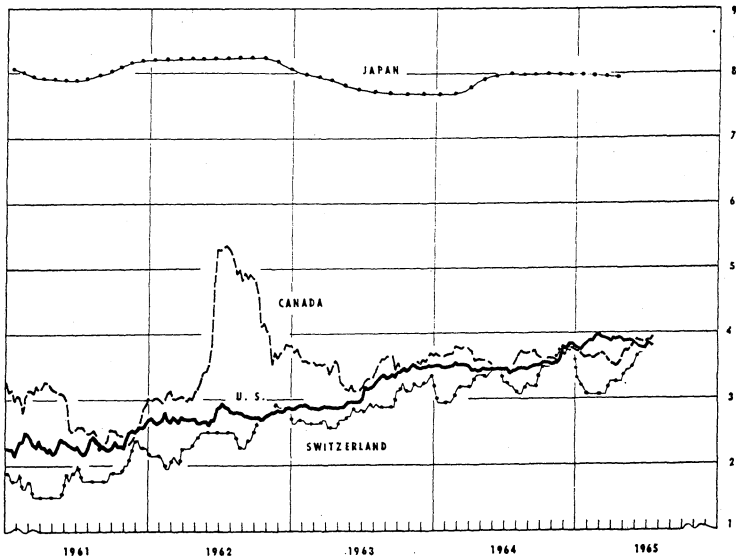
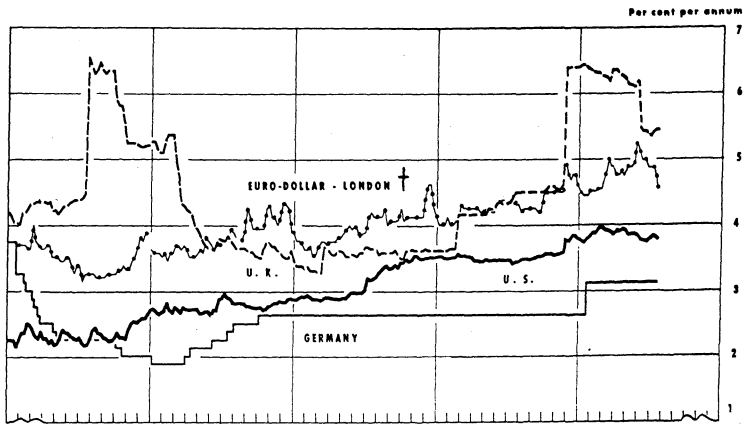


Chart 5
SHORT-TERM INTEREST RATES*



* 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

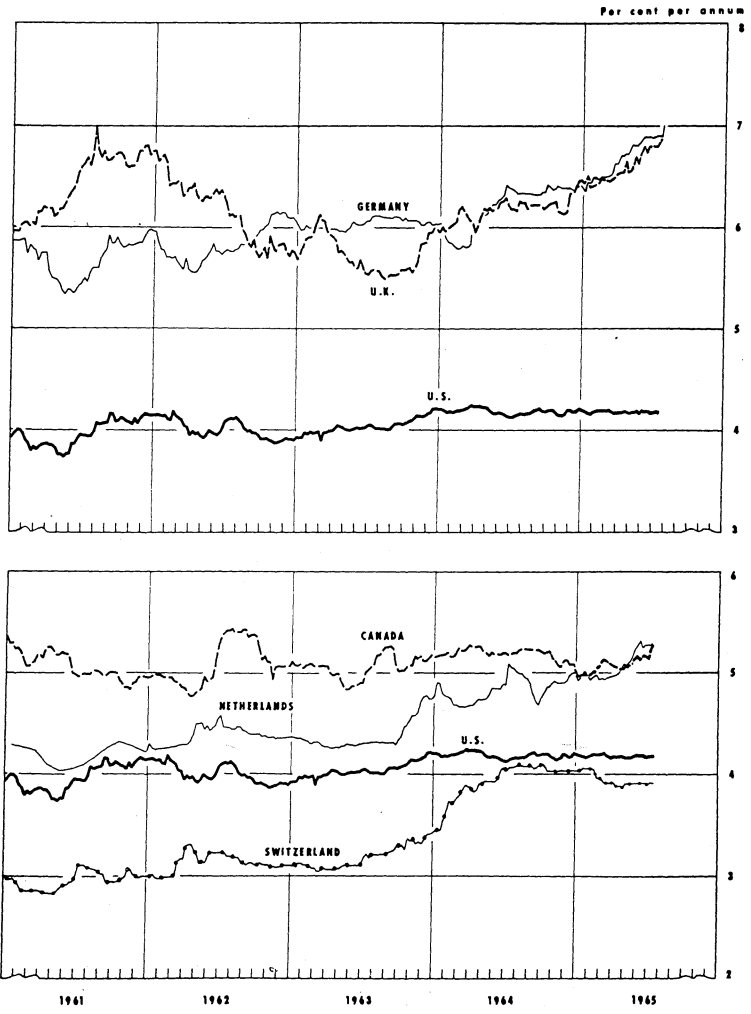
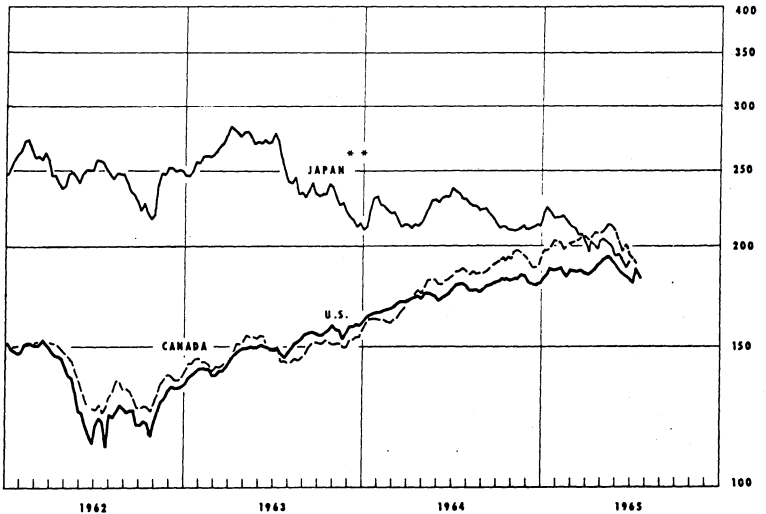
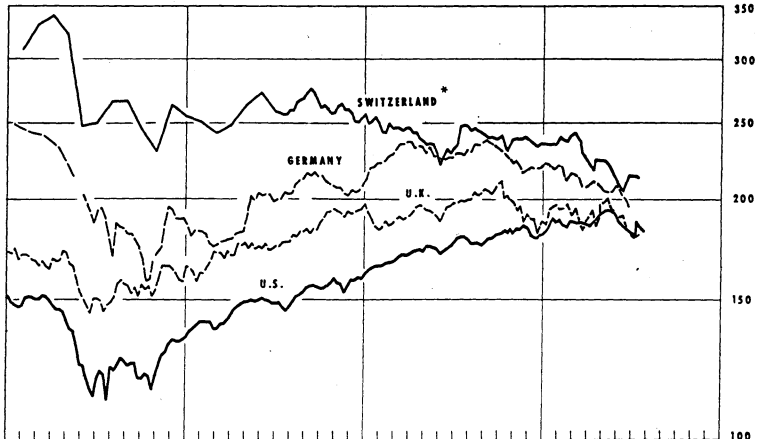


Chart 7

INDUSTRIAL STOCK INDICES

1958=100
Ratio scale



* Swiss Bank Corporation industrial stock.

** Japan: Index of 225 industrial and other stocks traded on the Tokyo exchange.

Chart 8

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

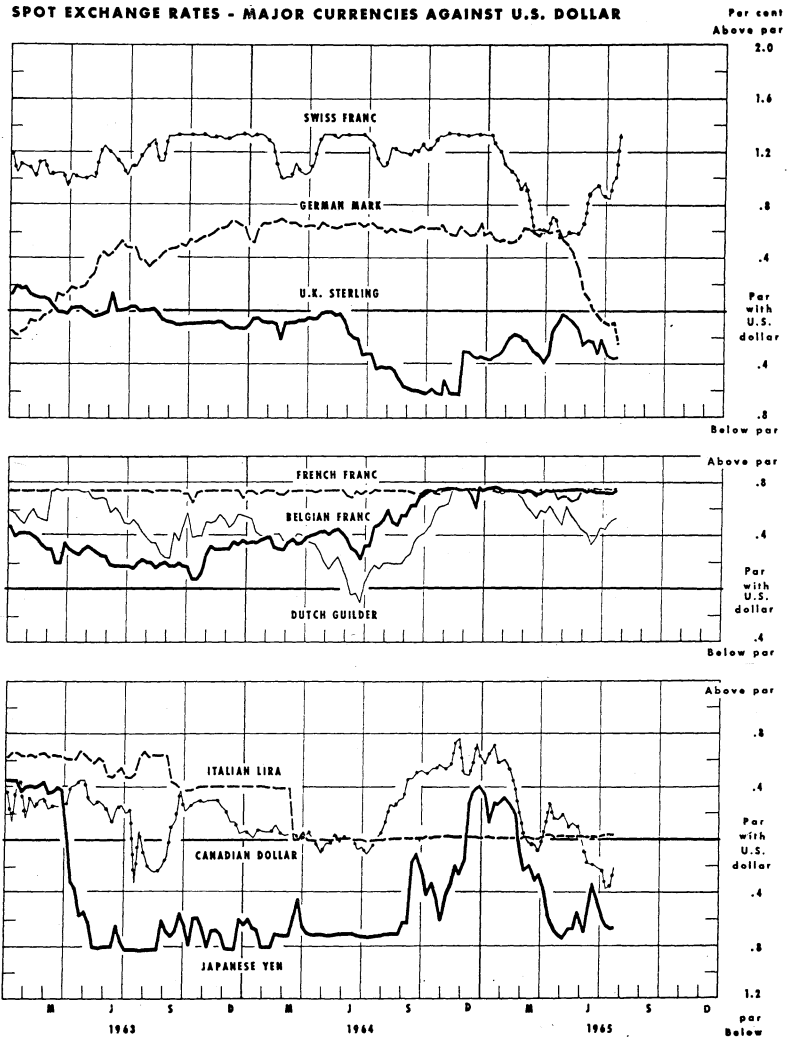
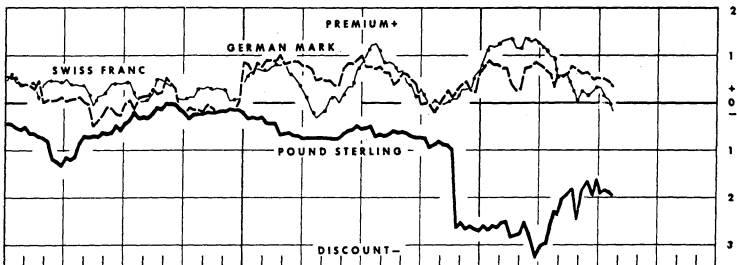


Chart 9
3-MONTH FORWARD EXCHANGE RATES

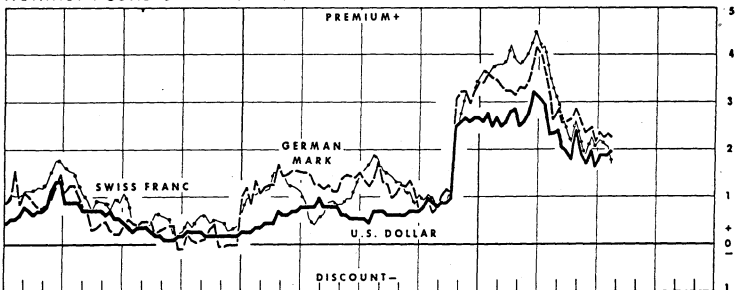
Friday figures

AGAINST U.S. DOLLARS

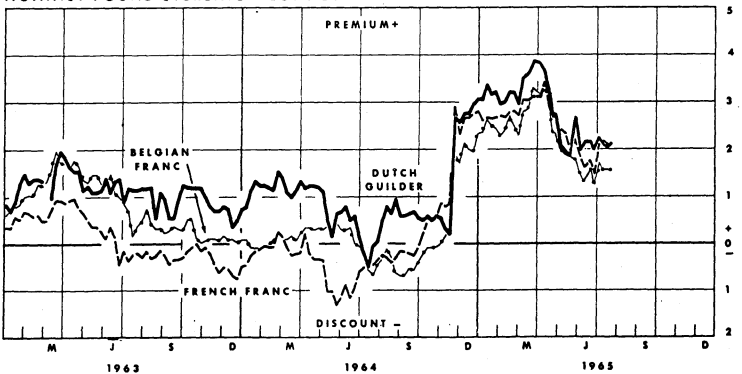
Per cent per annum



AGAINST POUND STERLING - LONDON



AGAINST POUND STERLING - LONDON



III. Latest Figures Plotted In H.13 Chart Series 1965

<u>Chart 1</u>	<u>Per cent per annum</u>	<u>Chart 5</u>	<u>Per cent per annum</u>
<u>Upper panel</u>		<u>(Friday, July 23 ,</u> <u>except as noted)</u>	
<u>(Wednesday, July 21)</u>		<u>Treasury bills:</u>	
Euro- $\$$ deposit	<u>4.78</u>	U.S.	<u>3.79</u>
U.S. certif. of deposit	<u>4.28</u>	U.K.	<u>5.46</u>
<u>Lower panels</u>		Germany	<u>3.12</u>
<u>(Friday, July 23)</u>		Canada	<u>3.92</u>
Euro-dollar deposits: Call	4.000	Swiss 3-month deposits	
7-day	<u>4.125</u>	(Date: <u>June 23</u>)	<u>3.69</u>
30-day	<u>4.375</u>	Euro- $\$$ deposit (London)	<u>4.56</u>
90-day	<u>4.562</u>	Japan: composite rate	
180-day	<u>5.000</u>	(Date: <u>April 30</u>)	<u>7.921</u>
Finance Co. paper: U.S.	<u>4.25</u>	<u>Chart 6</u>	
Canada	<u>4.94</u>	<u>Bonds:</u>	
Hire-purchase paper, U.K.	<u>4.83</u>	U.S. govt.	
<u>Chart 2</u>		(Wed., <u>July 21</u>)	<u>4.18</u>
<u>(Friday, July 23)</u>		U.K. war loan	
Treasury bills: Canada	<u>3.92</u>	(Thurs., <u>July 15</u>)	<u>6.88</u>
U.S.	<u>3.79</u>	German Fed. Railway	
Spread favor Canada	<u>+0.13</u>	(Fri., <u>July 23</u>)	<u>7.00</u>
Forward Canadian dollar	<u>+0.14</u>	Swiss Confederation	
Net incentive (Canada +)	<u>+0.27</u>	(Fri., <u>July 16</u>)	<u>3.91</u>
<u>Chart 3</u>		Canadian govt.	
<u>(Friday, July 23)</u>		(Wed., <u>July 14</u>)	<u>5.27</u>
Treasury bills: U.K.	<u>5.46</u>	Netherlands government	
U.S.	<u>3.79</u>	perpetual	
Spread favor U.K.	<u>+1.67</u>	(Fri., <u>July 9</u>)	<u>5.28</u>
Forward pound	<u>-1.98</u>		
Net incentive (U.K. +)	<u>-0.31</u>		