

H. 13

No. 219

October 27, 1965.

CAPITAL MARKET DEVELOPMENTS ABROAD

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

I. Canada: Money and Capital Markets, September-October 1965

Restricted credit availabilities which have been developing in Canadian financial markets over the past few months continued to be evident during September and October. To be sure, yields on government securities declined during the first part of September, but this may have been in part in reaction to a large government bond maturity on September 1. In any case, the easing proved to be temporary: by early October yields were again fluctuating close to the end-August range for most maturities. (See Table 1.) During September and October, short-term rates also advanced slightly. (See Charts 1 and 2.)

Table 1. Canada: Selected Financial Market Indicators, August 26 to October 20, 1965
 (in per cent per annum unless otherwise indicated)

	Actual Aug. 26	<u>Change from preceding date to</u>		Actual Oct. 20
		Sept. 23	Oct. 20	
1. Short-term rates:				
Day-to-day loans <u>a/</u>	3.83	.10	-.15	3.78
30-day prime comm. paper <u>b/</u>	4.81	0	.38	5.19
90-day prime finance paper <u>c/</u>	5.12	-.12	0	5.00
91-day Treasury bill <u>d/</u>	4.08	.01	.06	4.15
182-day Treasury bill	4.30	0	.11	4.41
2. Government bonds: <u>e/</u>				
1-year (1966)	4.92	-.17	.24	4.99
3-year (1968)	5.06	-.08	.16	5.14
7-year (1972)	5.28	-.13	.11	5.26
18-year (1983)	5.36	-.04	.10	5.42
25-year (1990)	5.38	-.02	.07	5.43
3. Stock prices:				
Index <u>f/</u>	195.3	4.8	<u>g/</u> -0.5	<u>g/</u> 199.6
4. Exchange rates:				
Spot (U.S. cents)	92.90	0	.19	93.09
Actual three-month forward discount (-) (in per cent per annum)	-0.07	-0.47	-0.20	-0.74

a/ Average of daily closing rates for week ending Wednesday.

b/ Friday data; mid-range.

c/ Friday data.

d/ Average tender.

e/ Wednesday data; mid-market yield at close.

f/ From Financial Post, (1958=100).

g/ October 13.

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However, the higher level of Canadian security yields did not cause differentials between U.S. and Canadian interest rates to narrow during the period under review. On the contrary, yield spreads in both the longer-term and in the short-term sectors moved in the opposite direction. The narrowing of yield differentials in intermediate and long-term bonds was produced by the fact that the rise in U.S. bond yields exceeded the increases in Canadian yields. (See Table 3.)

The reduced spreads in short-term financial instruments was largely the result of an unexpectedly wide discount which emerged for the forward Canadian dollar during September and October. The discount widened from 7 basis points on August 26 to 74 basis points on October 20. As a result, for the first time in several years, the yield spread favored the U.S. over the Canadian Treasury bill by more than 50 basis points during much of this period. (See Chart 2.) For the same reason, the incentive in favor of Canadian over U.S. finance company paper which has been large since the second quarter also narrowed substantially. (See Chart 1.) However, financial markets reported that tightness in Canadian money markets offset the incentives to move funds out of Canada; instead, the banks repatriated funds from abroad, partly for customary window-dressing needs at the end of their fiscal year in October.

Despite the strong business expansion in Canada, the loans of the chartered banks flattened out during the third quarter. (See Table 2.) The banks also acted to improve their liquidity position. During August and September, their sales of government bonds were on a much reduced scale and they continued to build up their holdings of Treasury bills. (See Table 5.) The "more liquid asset" ratio of the banks (that is, their cash, Treasury bills and government securities) which had been declining steadily earlier in 1965 stabilized during September and October. (See Table 2.)

Table 2. Canada: Selected Chartered Bank Statistics, June-September 1965
(millions of dollars or per cent)

	Actual June 30	Change from previous date <u>a/</u>			Actual Sept. 29
		July	Aug.	Sept.	
Currency and chartered bank deposits of public (less float)	18,548	+116	+112	+227	19,004
Government of Canada deposits	624	+168	-75	-206	511
Total money supply	19,173	+284	+37	+21	19,516
Day-to-day loans	213	-20	-51	+128	270
General loans	9134	+209	+42	+41	9426
Loans to grain dealers	327	+28	-4	-64	287
Total cash reserves <u>b/</u>	1289.5	+124.3	+75.1	-88.2	1400.7
Cash reserve ratio <u>c/</u>	8.09	-0.01	+0.02	-0.02	<u>f/</u> 8.01
Liquid asset ratio <u>d/</u>	16.39	+0.34	-0.04	+0.26	<u>f/</u> 17.27
More liquid asset ratio <u>e/</u>	30.68	-0.36	+0.08	-0.12	30.28

a/ Last Wednesday of month.

b/ Till money plus deposits with Bank of Canada.

c/ Daily average for month; statutory minimum per monthly average is 8.0 per cent.

d/ Daily average for month; agreed (with Bank of Canada) minimum is 15.0 per cent.

e/ As at date listed; conventional minimum is 30 per cent.

f/ Actual at date listed.

Source: Bank of Canada, Weekly Financial Statistics.

Money market tightness continues. During the period under review, money market rates fluctuated generally around their earlier high August levels. (See Table 1 and Charts 1, 2, and 5.) The average of daily closing rates on day-to-day loans climbed 22 basis points to 4.05 per cent during the first week in September but gradually drifted down thereafter. By contrast the rate on 30-day prime commercial paper moved up 31 basis points from 4.81 per cent to 5.12 per cent in the two week period which ended October 6. The 90-day prime finance paper rate receded from the very high level of 5.12 per cent to 5.00 per cent. The average tender for 91-day Treasury bills edged up from 4.09 per cent on September 2 to 4.15 per cent on October 21.

Government bond market absorbs large conversion issue. Government bond yield trends reacted to the announcement of a large conversion issue in mid-August. Residual holders of a \$450 million Government of Canada bond issue which matured on September 1 re-invested the proceeds in the Government bond market, thereby temporarily depressing yields on most maturities. (See Table 1.) Underlying trends in the market for long-term securities were subsequently reestablished. By the third week in October yields on representative issues were roughly at the previous recent highs recorded in mid-August, two months earlier. (See Tables 1 and 3.)

The differential between comparable United States and Canadian Government securities narrowed substantially in early September. (See Table 3 and Chart 6.) A sharp drop in Canadian bond prices in early September was followed late in the month by higher yields on U.S. bonds. The inclusion of a comparison of 1-year bonds in Table 2 reflects the extension on October 9 of the U.S. Interest Equalization Tax to maturities of at least one year; previous coverage was confined to maturities of at least three years.

Local government and private bond yields resume advance. The upward trend in yields on provincial, municipal, public utility, and industrial bonds continued in September in contrast with August, when bond yields in these categories changed little from high levels established in July. (See Table 3.) The 40-bond yield average rose 33 basis points between May 31 and the end of September. The advance was broadly based, but yields on local-government issues advanced most and those of industrials least during this period.

Table 3. Canada/U.S. Comparative Bond Yields, August 18 - October 6, 1965
(per cent per annum; Wednesday data; Canadian bonds, mid-market
yield at close; U.S. bonds, yields on bid side)

	Aug. 18	September					October		
		1	8	15	22	29	6	13	20
<u>1 year:</u>									
U.S. 11/15, 4 per cent	4.08	4.13	4.16	4.15	4.17	4.37	4.29	4.21	4.24
Canada 12/15/66, 4.5 per cent	4.97	4.72	4.76	4.77	4.75	4.93	4.96	4.92	4.99
Differential	+0.89	+0.59	+0.60	+0.62	+0.58	+0.56	+0.67	+0.71	+0.75
<u>3-year:</u>									
U.S. 8/68, 3.75 per cent	4.18	4.23	4.24	4.23	4.25	4.30	4.31	4.29	4.36
Canada 10/68, 5.0 per cent	5.11	4.91	4.98	4.98	4.98	5.03	5.12	5.06	5.14
Differential	+0.93	+0.68	+0.74	+0.75	+0.73	+0.73	+0.81	+0.77	+0.78
<u>7 year:</u>									
U.S. 8/72, 4.0 per cent	4.25	4.26	4.26	4.26	4.26	4.37	4.32	4.31	4.37
Canada 9/72, 4.25 per cent	5.31	5.20	5.19	5.19	5.15	5.20	5.24	5.19	5.26
Differential	+1.06	+0.94	+0.93	+0.93	+0.89	+0.83	+0.92	+0.88	+0.89
<u>19-year:</u>									
U.S. 78-83, 3.25 per cent	5.25	4.28	4.28	4.31	4.31	4.36	4.33	4.30	4.31
Canada 9/83, 4.5 per cent	5.36	5.33	5.32	5.33	5.32	5.36	5.41	5.39	5.42
Differential	+1.11	+1.05	+1.04	+1.02	+1.01	+1.00	+1.08	+1.09	+1.11
<u>25-year:</u>									
U.S. 2/90, 3.5 per cent	4.23	4.27	4.28	4.29	4.29	4.34	4.31	4.29	4.33
Canada 5/90, 5.25 per cent	5.37	5.38	5.36	5.36	5.36	5.39	5.42	5.40	5.43
Differential	+1.14	+1.11	+1.08	+1.07	+1.07	+1.05	+1.11	1.11	+1.10

Sources: Federal Reserve System and Bank of Canada, Weekly Financial Statistics.

Table 4. Canada: Municipal, Provincial, and Private Bond Yields, May-September 1965
(per cent per annum)

		Change from previous date to: a/				
	Level on	June	July	Aug.	Sept.	Level on
	<u>May 31</u>	<u>30</u>	<u>31</u>	<u>31</u>	<u>30</u>	<u>Sept. 30</u>
10 Provincials	5.44	+6	+18	0	+8	5.76
10 Municipals	5.59	+10	+12	+1	+14	5.96
10 Public Utilities	5.52	+11	+11	0	+10	5.84
10 Industrials	5.52	+12	+9	+6	+4	5.83
40 Bond Yield Average	5.52	+10	+12	+2	+9	5.85

a/ In basis points.

Source: McLoed, Young and Weir.

Security purchases by Bank of Canada. From August 25 through October 20 the Bank of Canada added some \$83 million in Treasury bills and \$30 million in bonds to its portfolio of government securities. At the same time, the reserves of the chartered banks actually declined by \$26 million as the Government of Canada deposits with the chartered banks were reduced by \$136 million. Security purchases by the Bank of Canada and by government accounts helped to cushion the impact on financial markets of the pressures on the chartered banks.

Table 5. Canada: Holdings of Central Government
Direct and Guaranteed Debt, June-October 1965
(million of dollars)

	Actual June 30	Change from previous date to:				Actual Oct. 20
		July 28	Aug. 25	Sept. 29	Oct. 20	
Bank of Canada						
Treasury bills	473	-37	+3	-17	+100	522
Other	2751	+52	-40	+57	-27	2793
Total	3224	+15	-37	+40	+73	3315
Government Accounts						
Treasury bills	18	+4	-3	-3	+3	19
Other	494	-54	+22	+19	+15	496
Total	512	-50	+19	+16	+18	515
Chartered banks						
Treasury bills	1271	+45	+44	+25	-13	1372
Other	2457	-116	-4	-20	+39	2353
Total	3728	-71	+40	+5	+26	3725
General Public						
Treasury bills	378	-11	-45	+4	-89	237
Other	6935	+63	+44	-15	-18	7009
Total	7313	+52	-1	-11	-107	7246
Canadian Savings Bonds	5426	-31	-30	-41	-24	5300
Net new issues	--	-85	-9	+9	-14	--

Source: Bank of Canada, Weekly Financial Statistics

Stock market firm despite adverse Royal Commission Report. Average stock market prices fell only slightly after mid-September despite recent criticisms of the Toronto Exchange by a Royal Commission Report. (See Table 1 and Chart 7.) The Financial Post's index of industrial stock prices dropped 2.5 points from 201.3 for the week which ended September 16 to 199.6 for the week of October 13 in contrast to the rise in the index from 195.3 the week of August 26 to 201.3 the week of September 16. The performance of the stock markets in the period under review indicates that Canadian investor confidence was not adversely affected by the recent Royal Commission Report on the Windfall Scandal of 1964 which severely criticized both the operations of the Toronto Stock Exchange and the limited public surveillance of it.

International reserves rise again. Canada's official holdings of gold and dollars increased by \$16.1 million in September, considerably less than the rise of \$106.5 million which occurred in August. (See Table 6.) Complete data are not yet available for September, but in August Canada's net creditor position in the International Monetary Fund improved by \$10.0 million. As a consequence her total reserves at the end of August amounted to \$2,812.0 million.

Because her U.S. dollar holdings increased far more in August than her gold holdings, gold as a percentage of gold and dollars fell sharply from 44.0 per cent in July to 42.5 per cent in August in contrast with the upward trend of the ratio in 1965 (and 1963 and 1964 as well).

Table 6. Canada: Official Holdings of Gold and U.S. Dollars, March-September 1965
(millions of U.S. dollars)

	<u>Level on March 31</u>	<u>Change during the month of</u>				<u>Level on Sept. 29</u>
		<u>June</u>	<u>July</u>	<u>Aug.</u>	<u>Sept.</u>	
Gold	1044.1	+45.0	+7.2	+7.7	n.a.	n.a.
U.S. dollars	1510.0	-119.0	+4.2	+98.8	n.a.	n.a.
Subtotal	2554.1	-74.0	+11.4	+106.5	+16.1	2614.1
Net creditor position in IMF	102.5	+86.5	+15.0	+10.0	+50.0	264.0
Total reserves	2656.6	+12.5	+26.4	+116.5	+66.1	2878.1
Initial drawing right position in IMF	240.0	+86.5	+15.0	+10.0	+50	401.5
Gold as a percentage of gold and dollars	40.9	43.9	44.0	42.5	n.a.	n.a.

Source: Bank of Canada, Statistical Summary

Spot Canadian dollar rises but large forward discount emerges. The premium on the spot Canadian dollar advanced by 11 basis points in the period under review but an unexpectedly wide discount appeared on the forward Canadian dollar. (See Table 7 and Chart 2.) Between August 25 and October 14 the spot rate for the Canadian dollar rose from 92.90 to 93.01 U.S. cents while the forward discount widened from 40 to 67 basis points. Sustained commercial demand, tightness in Canadian money markets, and window dressing by the chartered banks for their end of fiscal year (October) reports were the main influences affecting the foreign exchange market.

An increase of the forward discount on Canadian dollars and a rise in the U.S. Treasury bill rate in the second half of the period under review widened the yield spread on Treasury bills from 3 basis points in favor of Canada on August 26 to 65 basis points in favor of the United States on October 14. (See Table 7 and Chart 2.) Similarly, in the finance paper markets, the widening in the forward discount on the Canadian dollar reduced the covered spread in favor of Canada from 67 basis points on August 25 to 26 basis points on October 14. (See Table 7 and Chart 1.)

Table 7. Canada/U.S. Exchange Rates and Arbitrage Calculations,
September-October 1965

	<u>August</u>	<u>September</u>					<u>October</u>	
	<u>25</u>	<u>2</u>	<u>9</u>	<u>16</u>	<u>23</u>	<u>30</u>	<u>7</u>	<u>14</u>
Exchange rates:								
Spot (U.S. cents)	92.90	92.94	92.96	92.87	92.90	92.93	93.01	93.01
Forward (p.c. p.a.)	-0.07	-0.40	-0.54	-0.47	-0.54	-0.54	-0.60	-0.67
3-month yields and differentials								
Treasury bills								
Canada (covered)	3.87	3.58	3.46	3.55	3.43	3.47	3.45	3.34
U.S.	3.84	3.85	3.89	3.86	3.93	4.02	4.00	3.99
Differential (+ in favor Canada)	+0.03	-0.27	-0.43	-0.31	-0.50	-0.55	-0.55	-0.65
Finance paper a/ Canada (covered)	4.92	4.72	4.52	4.66	4.44	4.52	4.46	4.51
U.S.	4.25	4.25	4.25	4.25	4.25	4.25	4.25	4.25
Differential	+0.67	+0.47	+0.27	+0.41	+0.19	+0.27	+0.21	+0.26

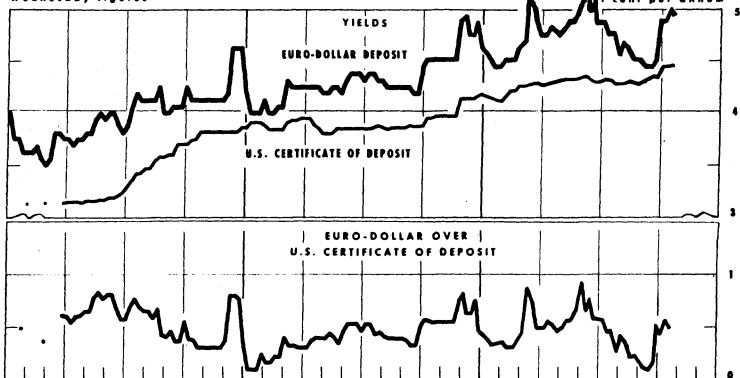
a/ Friday data.

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

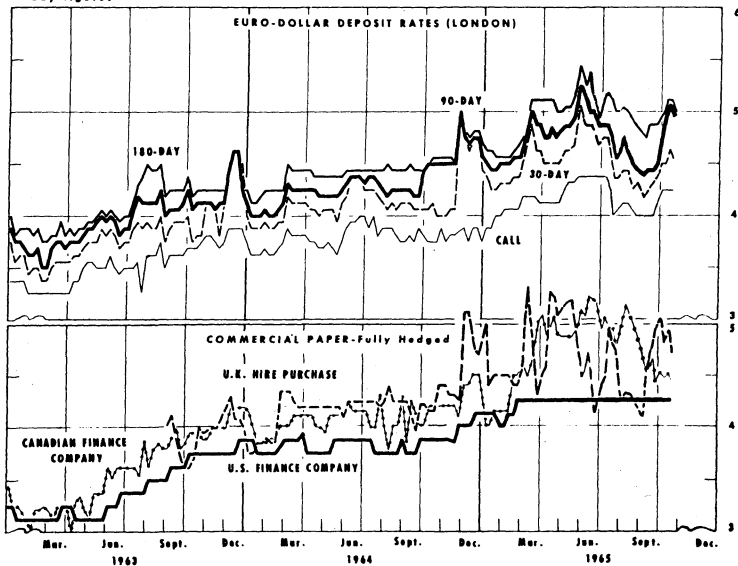
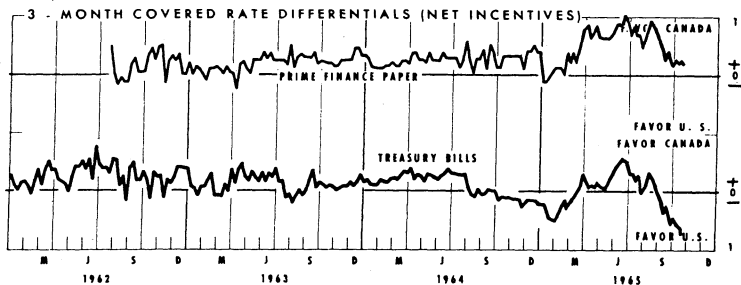
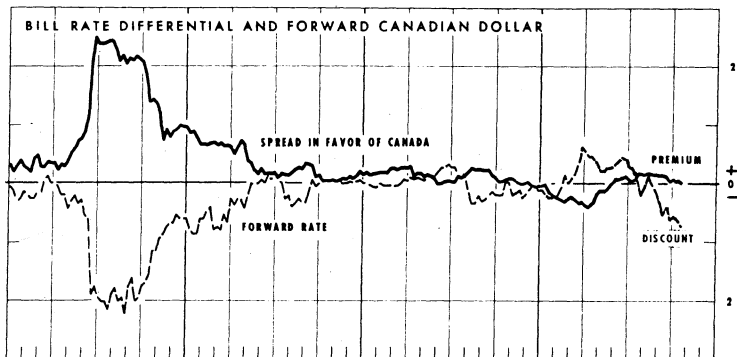
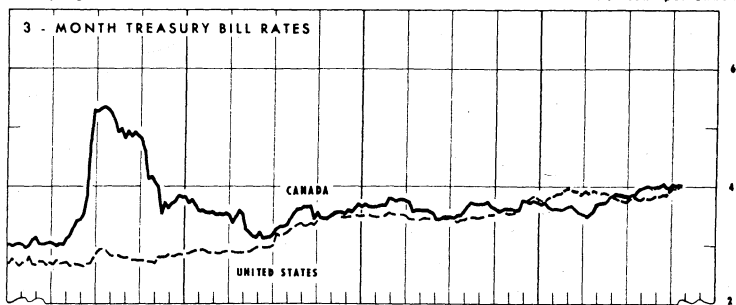


Chart 2

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

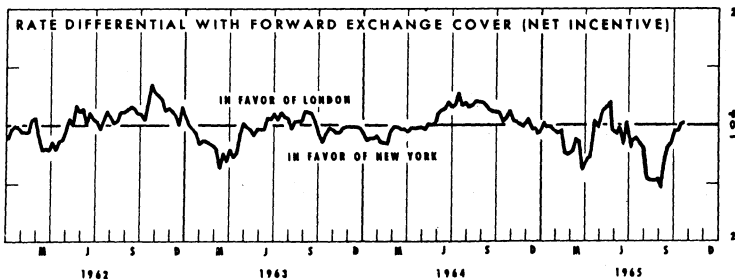
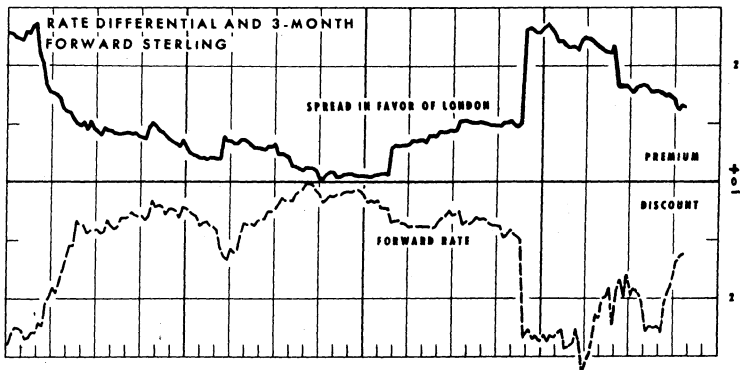
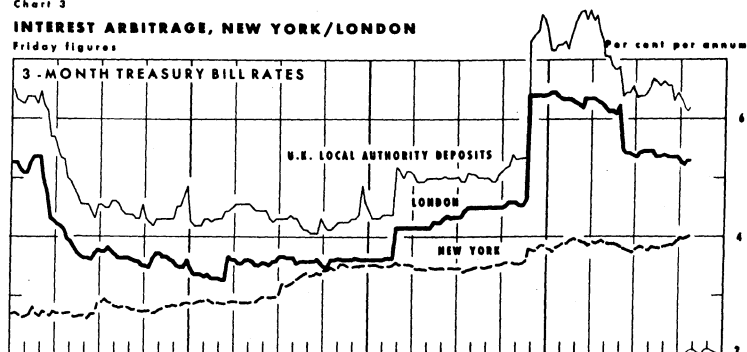


Chart 4

INTEREST ARBITRAGE FOR GERMAN COMMERCIAL BANKS

Friday figures

Per cent per annum

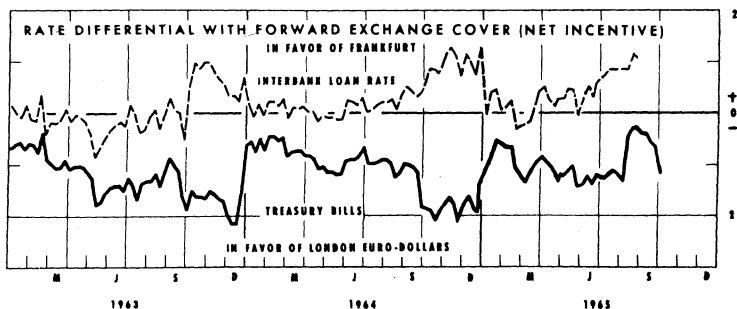
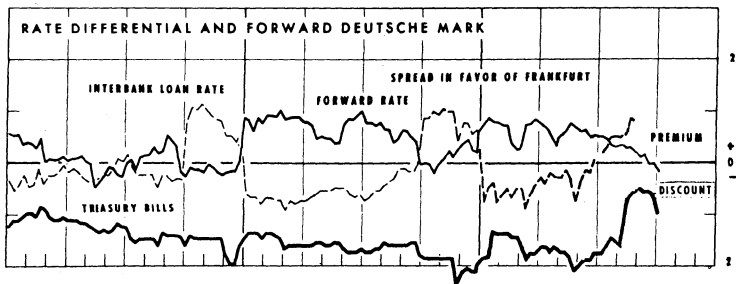
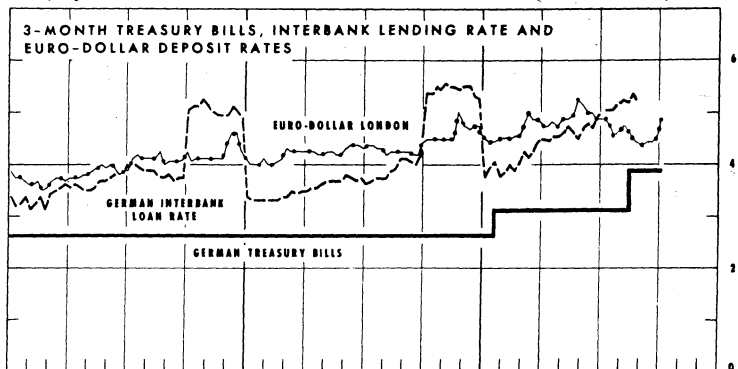
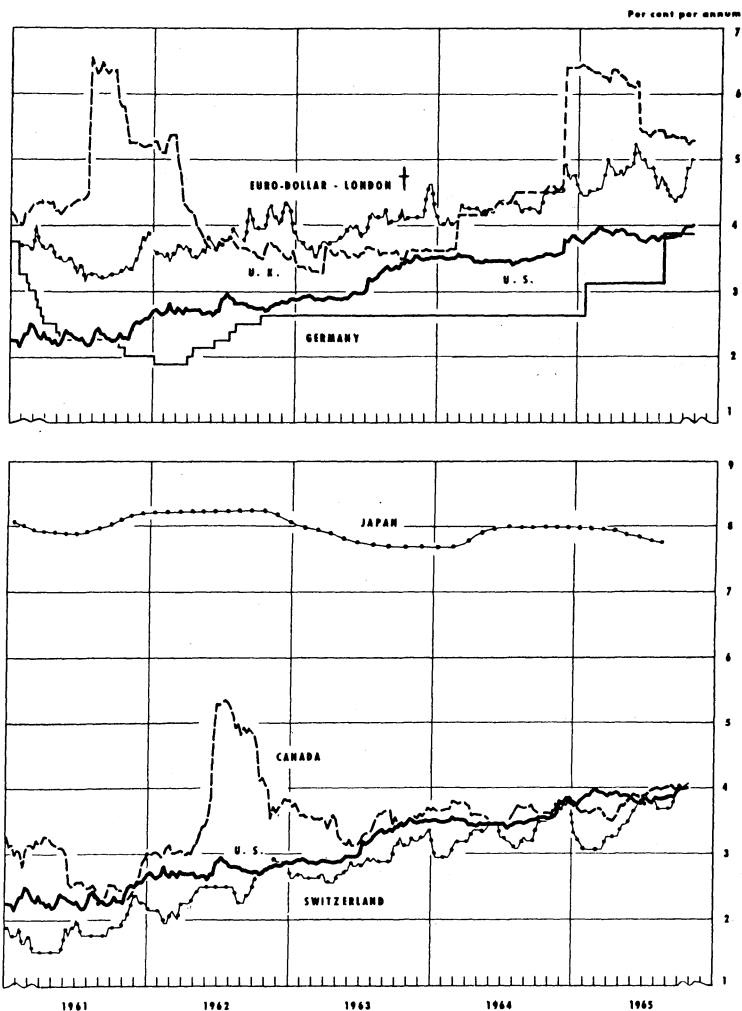


Chart 5
SHORT-TERM INTEREST RATES*



* 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

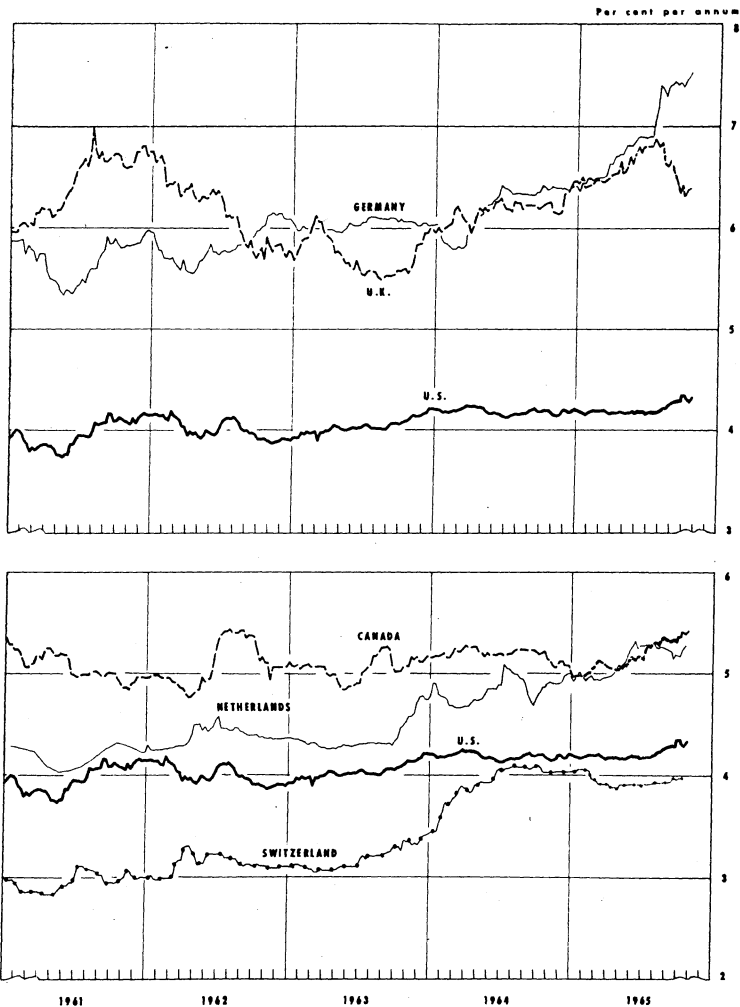
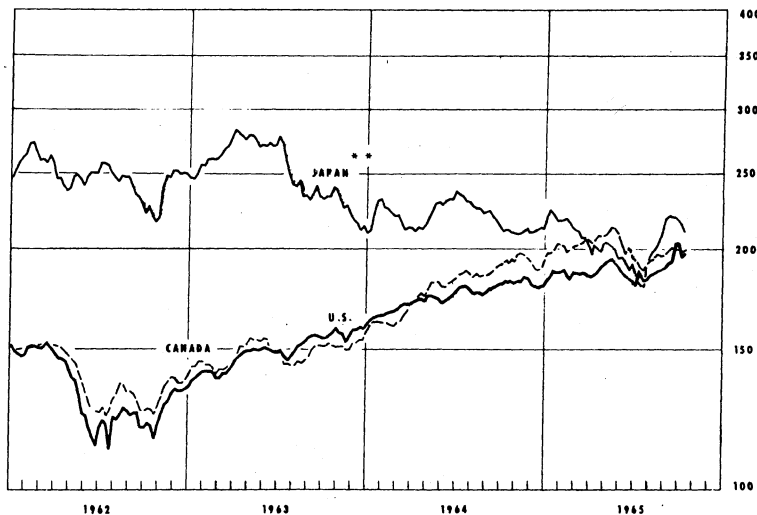
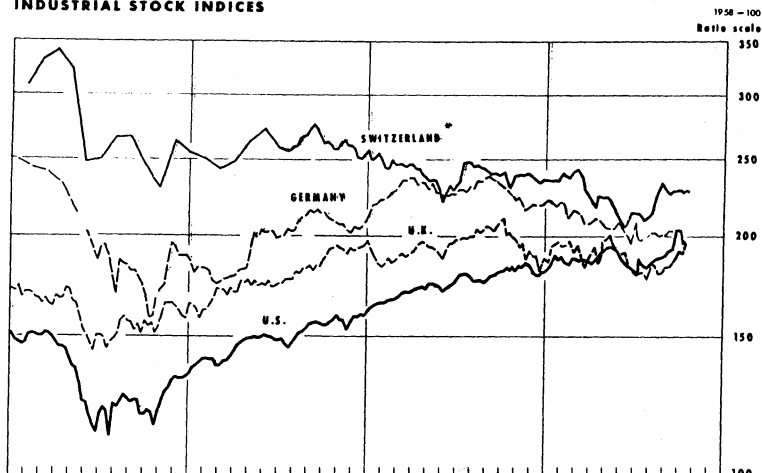


Chart 7

INDUSTRIAL STOCK INDICES



* Swiss Bank Corporation industrial stock.

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

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Chart 8

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

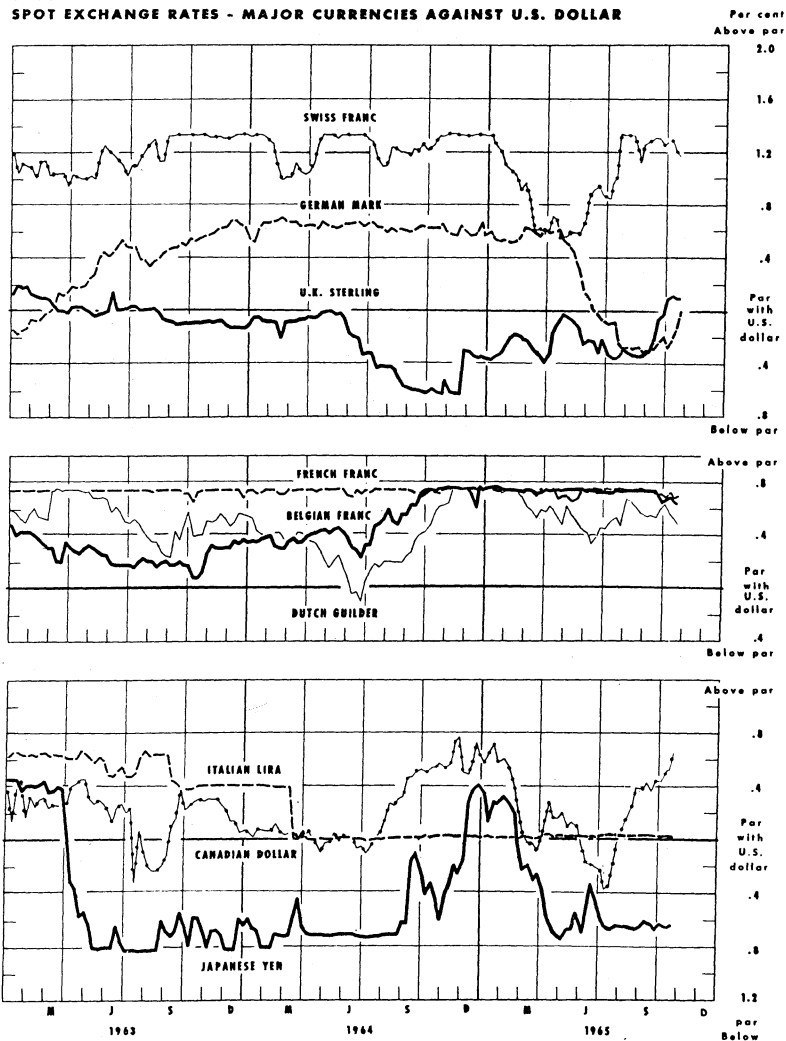
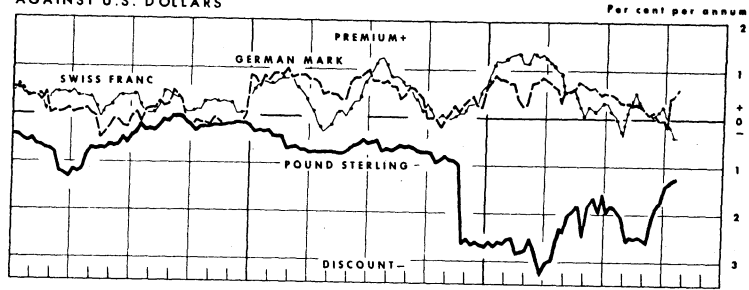
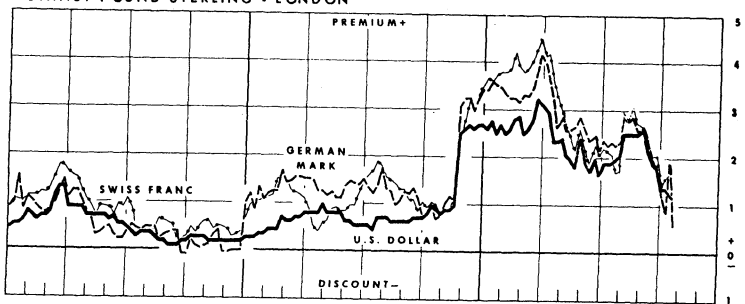


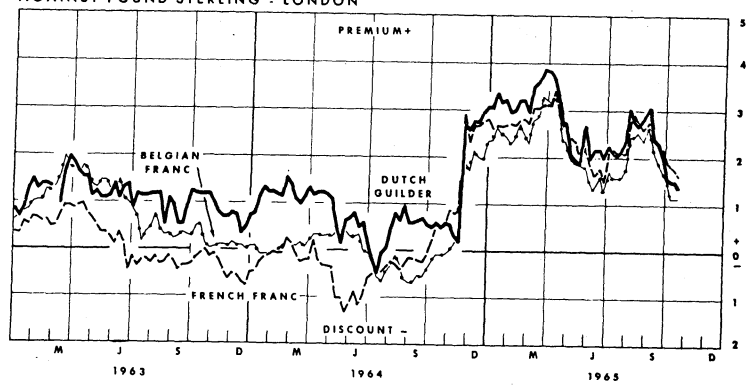
Chart 9
3-MONTH FORWARD EXCHANGE RATES
 Friday figures
 AGAINST U.S. DOLLARS



AGAINST POUND STERLING - LONDON



AGAINST POUND STERLING - LONDON



III. Latest Figures Plotted In H.13 Chart Series, 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>		(Friday, <u>Oct. 22</u> , except as noted)	
(Wednesday, <u>Oct. 20</u>)		Treasury bills:	
Euro-\$ deposit	<u>4.94</u>	U.S.	<u>4.01</u>
U.S. certif. of deposit	<u>4.46</u>	U.K.	<u>5.30</u>
<u>Lower panels</u>		Germany	<u>3.88</u>
(Friday, <u>Oct. 22</u>)		Canada	<u>4.08</u>
Euro-dollar deposits: Call	<u>4.25</u>	Swiss 3-month deposits (Date: <u>Sept. 23</u>)	<u>3.82</u>
7-day	<u>4.38</u>	Euro-\$ deposit (London)	<u>5.00</u>
30-day	<u>4.56</u>	Japan: composite rate (Date: <u>Aug. 27</u>)	<u>7.731</u>
90-day	<u>4.94</u>		
180-day	<u>5.00</u>	<u>Chart 6</u>	
Finance Co. paper: U.S.	<u>4.25</u>	Bonds:	
Canada	<u>4.44</u>	U.S. govt. (Wed., <u>Oct. 20</u>)	<u>4.33</u>
Hire-purchase paper, U.K.	<u>4.71</u>	U.K. war loan (Thurs., <u>Oct. 14</u>)	<u>6.39</u>
<u>Chart 2</u>		German Fed. Railway (Fri., <u>Oct. 15</u>)	<u>7.52</u>
(Friday, <u>Oct. 22</u>)		Swiss Confederation (Fri., <u>Oct. 8</u>)	<u>3.97</u>
Treasury bills: Canada	<u>4.02</u>	Canadian govt. (Wed., <u>Oct. 20</u>)	<u>5.42</u>
U.S.	<u>4.02</u>	Netherlands government perpetual (Fri., <u>Oct. 15</u>)	<u>5.27</u>
Spread favor Canada	<u>0.00</u>		
Forward Canadian dollar	<u>-0.74</u>		
Net incentive (Canada +)	<u>-0.74</u>		
<u>Chart 3</u>			
(Friday, <u>Oct. 22</u>)			
Treasury bills: U.K.	<u>5.30</u>		
U.S.	<u>4.01</u>		
Spread favor U.K.	<u>+1.29</u>		
Forward pound	<u>-1.23</u>		
Net incentive (U.K. +)	<u>+0.06</u>		