

~~BAMAS~~
CIS 1/16A

DEVELOPMENTS IN THE CAPITAL MARKETS

JULY-SEPTEMBER 1981

Money Markets

Interest rates hardened considerably during the period with the main underlying influences being the level of US rates and the performance of sterling. In addition, the ending of the Civil Service dispute at the end of July and the initial recovery of delayed government revenue which began in August contributed to the tightening in money market conditions.

On two occasions during the period when sterling came under particular downward pressure - at the beginning of July and in mid-September - the Bank of England moved to raise short-term interest rates. The increase in September was also motivated by official concern at the growth of bank lending to the private sector. Following this, the clearing banks' base rates were increased by 2% to 14% on 16 September. After a brief recovery, sterling continued to weaken in the second half of September while money market rates (other than at the very short end where official influence remained dominant) continued to edge upwards. Official policy did not long resist this movement and by 1 October short-term rates had adjusted with base rates at 16%.

On 30 September seven-day inter-bank rate stood at 15 7/8% (12% at end-June) and the three-month rate was at a peak of 17% (12 11/16% at end-June).

Since 20 August the Bank has operated in the money markets by reference to an undisclosed band for very short-term interest rates

in the context of the new monetary control arrangements introduced on that day.* Minimum Lending Rate (MLR) is no longer continuously posted. The new arrangements have generally worked smoothly and as expected despite often highly nervous and volatile markets. The Bank has been able to exercise the desired degree of influence over very short-term interest rates, while giving market forces a greater role than previously in determining the level of longer rates.

Government Stocks

Sentiment in the gilt-edged market was adversely affected for much of the period by the same uncertainties as faced the money markets.

The period began with the issue of the second index-linked stock, 2% Index-Linked Treasury 2006, on 8 July. In the days leading up to the issue sentiment weakened sharply. As a result, the stock was not allotted in full at the tender and the allotment price of £86 was well below that expected by the market. However, heavy demand developed for the balance of the stock the following day and it was sold at £3/8 above the issue price. This encouraged the market as a whole and the Bank was able to make some sales of its 1985 tap stock and, subsequently, of the 1986 low coupon stock.

Thereafter, renewed uncertainties emerged and by 20 July prices were at their lowest for four and a half years with yields on long-dated stocks at around 15 3/4%. However, some demand appeared at these levels and on 24 July the Bank was able to announce new tranches of two existing low coupon stocks and, on 31 July, further tranches of one medium and one long-dated stock. Amounts of these latter stocks were sold on 11 and 12 August amid renewed hopes of a fall in US interest rates and further amounts of the 1985 tap stock were sold on 17 and 21 August before prices dropped sharply.

The market then lapsed into a period of inactivity with prices little changed. However, when the Bank raised its money market rates on 14 September gilt-edged prices reacted sharply and by the following day yields on medium and long-dated stocks had risen to about 16%.

*In practice, a number of the changes in money market operating techniques had been introduced in the months prior to 20 August.

Towards the end of September, sterling came under renewed pressure and with markets in the US responding unfavourably to new fiscal proposals by President Reagan, hopes of any sustained fall in US rates were again deferred. Against a background of rising domestic interest rates, prices of gilt-edged stock again fell back sharply and by 28 September yields on some medium-dated issues had risen to about 16 3/4% (an increase of about 1 3/4% over the quarter as a whole).

Equity Market

Prices in the equity market declined on balance during July although the market took heart in the middle of the month from the success of the BP rights issue (which raised £624mn). During early August a firmer tendency gathered strength on optimism about lower US interest rates and hopes of economic recovery. The broadly-based FT All-Share Index reached an all-time peak of 334.96 on 12 August. Despite some fluctuations the market remained generally buoyant during the rest of August and by 3 September the more narrowly based FT 30-Share Index had reached 573.8, the highest level since 5 May. Thereafter, the market became increasingly unsettled by a succession of large right issues (including one of £87 million by Trusthouse Forte) and by the weakness of the US equity market. The downward trend in prices was given added impetus by the rise in interest rates from mid-September onwards and fears that this would stifle economic recovery. The last week of September saw a collapse of confidence (in common with other financial centres around the world) with the largest falls in prices for seven years. Although the market rebounded sharply on 29 September (rising by 18 points on the day) the 30-Share Index closed the period at 475.4, a net fall of 69.4 points (12 3/4%) over the period as a whole.

Net Domestic Issues

A new local authority stock issue of £75mn was made by Birmingham City Council, £15mn of which was raised during the quarter. This took the form of a "droplock" issue, the first major stock issue of this type in the domestic sterling markets. The interest rate

on the stock will initially vary every six months at a margin of 3/4% over LIBOR. Maturity will be in 1986, unless the par yield on seven-year gilt-edged stocks has by then fallen to 12 3/4% or less. In that event, the droplock will operate and the stock will be converted into a fixed-rate issue with a seven-year maturity carrying interest at 13 1/2%.

In the company sector, share issues totalled almost £590mn compared with £276 in the previous quarter. This reflected mainly the first instalment (£284mn) of the BP rights issue as well as the issue by Trusthouse Forte.

A "bulldog" issue of £50mn with a maturity of 27 years and priced to yield 16.97% was made during the quarter by United Mexican States.

18 November 1981

WORKING PARTY ON TRANSFERABLE SECURITIES MARKET

United Kingdom
Table 1A

Domestic Bond Issues 3rd Quarter 1981

Gross Issues over £2 million

Date of initial payment	Borrower	Amount £ million	Method of issue	Maturity period (years)	Issue price £	Redemption price £	Coupon	Yield at final redemption date	Comments
<u>Non-government</u>									
July	Mount Charlottes	2.9	Rights	19	Par	Convertible	9 1/2%	9.50	Convertible into ord. shares at 11 ord. shares per £1 nominal stock
	Property holdings and Investment Trust	10.1	Rights	25	Par	Convertible	8 1/2%	8.50	Convertible into ord. shares from 1985-2001 at 55 ord. shares per £100 nominal stock
August	Hanson Trust	43.8	Rights	25	Par	Convertible	9 3/4%	9.75	Convertible into ord. shares from 1985-2001 at 5 ord. shares per £2 nominal stock
	TOTAL	<u>56.8</u>							
<u>Government</u>									
July	Index linked Treasury Stock	1,000	Offer for sale by tender	25	-	Par	2%		
	TOTAL	<u>1,000</u>							

£ millions

TABLE 1B

GROSS DOMESTIC BOND ISSUES (EXCLUDING GOVERNMENT ISSUES):
SUMMARY FOR 3RD QUARTER 1981

Issues over £2 million	56.8
Issues of £2 million or less:	
Local authority	211.1
Company	0.4
Overseas borrowers (traditional)	<u>49.9</u>
	<u>318.2</u>

TABLE IIA

GOVERNMENT BOND ISSUES (NET) (a)

Purchase and new issues (+) Sales and redemptions (-)	1979			1980			1981	
	III	IV	I	II	III	IV	I	II
(1) Bank of England and National Debt Commissioners	+1,442	- 845	+1,409	-1,937	+1,902	- 821	+ 158	+ 313
(2) The Public	<u>+2,648</u>	<u>+2,511</u>	<u>+1,086</u>	<u>+3,377</u>	<u>+3,186</u>	<u>+3,043</u>	<u>+3,501</u>	<u>+1,550</u>
	<u>+4,090</u>	<u>+1,666</u>	<u>+2,495</u>	<u>+1,440</u>	<u>+5,088</u>	<u>+2,222</u>	<u>+3,659</u>	<u>+1,863</u>

(a) Although applications to subscribe to new issues of Government bonds are invited from the general public, it is usual for much the greater part of each issue to be taken up by the Issue Department of the Bank of England, which then stands ready to sell it to the public through the Stock Exchange during the following months. Figures of new issues are therefore less useful (and of less economic significance) than those of net purchases by the general public of old and new issues combined.

TABLE IIB

(alternative version)

NET PURCHASES OF GOVERNMENT BONDS BY THE PUBLIC ^{(a) (b)}

(net purchases by the public +/sales -)

£ millions

	1978	1979	1979		1980				1981	
	Year	Year	IV	I	II	III	IV	I	II	
Overseas holders (c)	- 117	+ 1,108	+ 297	+ 17	+1,093	+ 492	+ 29	- 8	+ 35	
Banking sector (d)	-	+ 227	- 18	- 584	+ 552	-	+1,560	+ 572	- 523	
Other holders	<u>+5,169</u>	<u>+ 8,810</u>	<u>+2,232</u>	<u>+1,653</u>	<u>+1,732</u>	<u>+2,694</u>	<u>+1,454</u>	<u>+2,937</u>	<u>+2,038</u>	
TOTAL	<u>+5,052</u>	<u>+10,145</u>	<u>+2,511</u>	<u>+1,086</u>	<u>+3,377</u>	<u>+3,186</u>	<u>+3,043</u>	<u>+3,501</u>	<u>+1,550</u>	
of which:										
Redemptions/ conversions	- 423	- 1,069	- 431	- 298	- 544	- 19	- 262	- 325	- 333	
Up to one-year stocks	-1,450	- 1,748	- 178	- 644	- 574	- 136	- 734	- 608	-1,115	
Over one and up to five-year stocks	+2,169	+ 2,403	+ 159	+ 754	+1,358	- 261	+1,186	+1,248	+ 515	
Over five and up to 15-year stocks	+ 956	+ 3,458	+1,317	- 67	+ 943	+3,130	+1,417	+1,400	+1,695	
Over 15-year stocks and undated	+3,800	+ 7,101	+1,644	+1,341	+2,194	+ 472	+1,437	+1,786	+ 788	

(a) This table provides further analysis of net purchases of Government bonds by the public [line (2) in Table IIA]. Attention is directed to purchases by "other holders" because these will, other things being equal, tend to moderate the growth of the money stock.

(b) At cash value, except for the banking sector, where the figures relate mainly to changes in book value - any difference between the book and cash value being reflected in the residual figures for "other holders".

(c) Estimated: there may be some unidentified overseas holdings under "other holders" but the amounts involved are thought not to be very large.

(d) Other than Bank of England, Banking Department.

BOND AND SHARE ISSUES (EXCLUDING GOVERNMENT AND INTERNATIONAL ISSUES)

£ millions

TABLE III

Bond Issues - Gross

	1979		1980				1981		
	IV	I	II	III	IV	I	II	III	
Financial companies (Fm)	2.1	4.0	-	2.5	-	-	-	-	
(Fs)	15.2	-	-	-	-	-	-	-	
Industrial and commercial companies	4.9	-	13.1	26.7	174.2	19.3	117.4	57.2	
Local authority	<u>129.7</u>	<u>219.9</u>	<u>197.6</u>	<u>185.8</u>	<u>170.7</u>	<u>178.4</u>	<u>247.2</u>	<u>211.1</u>	
Total domestic	151.9	223.9	210.7	215.0	344.9	197.7	364.6	268.3	
Overseas borrowers	-	-	-	73.5	-	39.3	149.4	49.9	
TOTAL	<u>151.9</u>	<u>223.9</u>	<u>210.7</u>	<u>288.5</u>	<u>344.9</u>	<u>237.0</u>	<u>514.0</u>	<u>318.2</u>	

TABLE IV

Bond Issues - Net

	1979		1980				1981		
	IV	I	II	III	IV	I	II	III	
Financial companies (Fm)	- 6.3	1.0	- 5.6	-17.6	- 19.0	- 66.9	- 5.0	- 3.8	
(Fs)	14.6	- 4.3	- 5.4	-10.6	- 3.2	- 0.2	- 2.3	- 1.4	
Industrial and commercial companies	-10.8	-44.7	- 8.4	-31.9	98.2	- 14.6	83.5	- 37.1	
Local authority	<u>-63.7</u>	<u>12.8</u>	<u>-24.0</u>	<u>-24.2</u>	<u>-129.5</u>	<u>- 45.2</u>	<u>19.9</u>	<u>-123.6</u>	
Total domestic	-66.2	-35.2	-43.4	-84.3	- 53.5	-126.9	96.1	-165.9	
Overseas borrowers	- 1.8	-40.4	- 4.9	66.8	- 15.5	28.3	138.1	82.9	
TOTAL	<u>-68.0</u>	<u>-75.6</u>	<u>-48.3</u>	<u>-17.5</u>	<u>- 69.0</u>	<u>- 98.6</u>	<u>234.2</u>	<u>- 83.0</u>	

TABLE V

Share Issues - Net

(Including Preference Capital)

	1979		1980				1981		
	IV	I	II	III	IV	I	II	III	
Financial companies (Fm)	-	-	-	0.7	2.7	- 3.8	- 1.6	1.0	
(Fs)	0.4	1.8	-	30.4	21.9	120.5	79.2	0.5	
Industrial and commercial companies	<u>233.4</u>	<u>69.8</u>	<u>99.2</u>	<u>408.6</u>	<u>348.5</u>	<u>231.4</u>	<u>275.7</u>	<u>588.6</u>	
Total domestic	233.8	71.6	99.2	439.7	373.1	348.1	353.3	590.1	
Overseas borrowers	-	-	-	-	-	-	-	-	
TOTAL	<u>233.8</u>	<u>71.6</u>	<u>99.2</u>	<u>439.7</u>	<u>373.1</u>	<u>348.1</u>	<u>353.3</u>	<u>590.1</u>	

Fm = Banks, discount houses, hire purchase finance houses and special finance agencies.
Fs = Investment trusts and insurance companies.

Notes to Tables III, IV and V

- (i) Estimates of the amounts raised are based on the prices at which securities are offered to the market.
- (ii) Subscriptions are recorded in the periods in which they are due to be paid. If an issue is paid by instalments, only that part paid during the period is included. (In Table I, however, the full amount of each issue is included at the time of payment of the first instalment.)
- (iii) Net issues comprise gross issues less redemptions; conversion issues in lieu of cash repayments are included in the gross figures of issues and redemptions. No allowance is made in Table V for company liquidations or other repayments of share capital.
- (iv) The series relates only to new money raised; bonus issues, share exchanges and issues for other forms of consideration are excluded, as are issues in which the cash raised accrues not to the borrowing company but to its existing shareholders.
- (v) The tables exclude international issues, ie. those which are issued in several countries simultaneously and which are denominated in a currency or currencies which need not be that either of the borrower or the lender (Euro-issues).

TABLE VI
Gross redemption yield on company bonds (1)

		Financial Times Actuaries Series (2) 20/25 years to maturity*
1980	July	13.68
	August	13.65
	September	13.85
	October	13.68
	November	13.65
	December	13.85
1981	January	14.22
	February	14.18
	March	14.09/14.33*
	April	14.42
	May	14.89
	June	15.30
	July	15.87
	August	15.97
	September	16.50

TABLE VII
Price index on company shares (2)

		Financial Times (3) Actuaries Industrial Shares (500) 10.4.62 = 100	Financial Times (4) Actuaries All Share (750) 10.4.62 = 100	Financial Times (5) Industrial Ordinary Share (30) 1.7.35 = 100
1980	July	294.14	280.90	488.54
	August	295.07	282.53	484.89
	September	301.79	292.29	491.72
	October	307.44	298.39	483.80
	November	318.96	304.95	493.45
	December	307.61	292.73	470.10
1981	January	297.77	284.68	459.63
	February	309.19	295.20	487.03
	March	314.14	301.24	497.79
	April	337.09	320.72	559.19
	May	339.79	321.53	557.93
	June	332.11	316.97	545.03
	July	327.42	315.44	528.15
	August	343.25	329.62	554.41
	September	320.64	308.65	525.00

TABLE VIII
Calculated gross redemption yield on Government bonds (1) (6)

		Terms to maturity		
		5 years	10 years	20 years
1980	July	12.67	13.08	13.07
	August	13.55	13.70	13.58
	September	13.10	13.47	13.38
	October	12.91	13.20	13.12
	November	13.14	13.34	13.22
	December	13.29	13.78	13.67
1981	January	13.29	13.97	13.96
	February	13.14	13.84	13.89
	March	12.99	13.66	13.68
	April	13.09	13.66	13.64
	May	13.33	14.40	14.31
	June	14.17	14.69	14.57
	July	14.91	15.28	15.14
	August	14.92	15.23	15.09
	September	15.76	15.81	15.59

Please see over for footnotes

* Series rebased on 16 March.

5/4 (a) B6

- (1) Calculated in conformity with UK market practice in respect of semi-annual interest payments.
- (2) Average of working days.
- (3) Comprised of three main groups of industrial companies:-
 - (i) capital goods;
 - (ii) consumer; and
 - (iii) other.
- (4) Including the shares in the Industrial Share Index and a group of financial companies' shares.
- (5) The leading shares from each sector of the market.
- (6) Taken from a yield/maturity curve, fitted mathematically, which reflects the current cost of issues of new bonds at par. Explanation of the method of calculation appeared in the Bank of England Quarterly Bulletins of December 1972, September 1973 and June 1976. Averages of three daily observations per week.

5/4 (a) B7

SHORT-TERM RATES

Table IX

Last Friday of month	Treasury Bills (Rate at Tender)	Local Authority Deposits (3 months)	Inter-Bank Overnight Lending (1)
1980 October	14.36	16.63-16.75	16.75-18.50
November	12.95	14.50-14.63	13.75-14.50
December	13.02	14.63-14.88	14.44-14.75
1981 January	12.61	13.81-13.88	14.19-14.38
February	11.59	12.63-12.75	14.75-16.50
March	11.53	12.75-12.81	12.00-13.00
April	11.24	12.94	11.75-12.25
May	11.45	12.50-12.63	10.50-11.63
June	11.88	12.44-12.63	10.00-13.00
July	13.80	14.63-14.75	12.00-13.00
August	13.19	14.06-14.13	12.25-14.25
September	15.12	15.63-15.75	14.00-14.25

(1) The inter-bank market is a market in unsecured loans between members of the banking system.

UNIT TRUSTS

Table X

£ millions

	1978	1979	1980				1981		
	Year	Year	I	II	III	IV	I	II	III
Sales of units	529.5	412.0	95.9	122.1	144.8	168.7	247.7	291.4	151.4
Repurchases of units	<u>294.0</u>	<u>353.9</u>	<u>105.0</u>	<u>92.3</u>	<u>118.5</u>	<u>108.0</u>	<u>96.8</u>	<u>118.7</u>	<u>75.9</u>
	235.5	58.1	- 9.1	29.8	26.3	60.7	150.9	172.7	75.5

*Figures for July and August only.