[redacted]

[redacted]

FROM: [redacted]
DATE: 10 NOVEMBER 1987

[redacted]

[redacted]

MARKET FACTS

In your minute of 9 November you asked for some statistical information on recent developments in the equity and gilt markets. [redacted] is dealing separately with item (iii) on market liquidity, and this note covers item (i) Turnover, and item (ii) Historical and International Comparisons.

(i) Turnover

Equity Market

2. Charts 1 and 2 attached show turnover both between market makers and by customers on a daily basis since 15 October. Chart 3 gives average equity market turnover on a monthly basis since the Big Bang. The main points to note are:

- average daily turnover in the six months to September 1987 was around £2 billion, split approximately 50:50 between intra-market transactions and customer business;
- since 15 October average market turnover has also averaged about £2 billion, but with 60 per cent of this business done by customers. With share prices having fallen by 30 per cent over this period, the fact that turnover has not fallen in value terms implies that the numbers of shares traded has increased markedly over the last month;

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- average daily turnover in the week beginning 19 October reached record levels, of around £3 billion per day. Customer business accounted for 60 per cent of turnover.

3. There is little in this data to substantiate the argument that the stock market fall is a result of traders marking down their prices rather than real selling pressure from institutions. The problem is of course that even daily data can mask the mechanisms by which market movements take place. It is perfectly possible that at critical points during the day, market makers might be leading the market down. The Stock Exchange are themselves now collecting hourly data during the critical period, in an attempt to analyse the mechanisms. This work should be available in a fortnight or so. In the meantime, anecdotal evidence from the Stock Exchange suggests that market makers are acting in the way jobbers did pre-Big Bang, by marking down share prices early in the day to protect themselves against customer led price falls.

4. The information we have received from the Stock Exchange on average spreads since the Stock Market's falls took place are revealing. These spreads are one objective indication of the degree of liquidity in the market. Spreads appear to have widened substantially since 15 October, for all types of equity, as the table below indicates. This is of course another means of self protection for the market maker. (The figures quoted are simply a snapshot on 20 October, and may not give a completely reliable picture)

	Average September 1987	**20 October 1987**
Alpha stock	0.70%	1.37%
Beta stock	1.58%	2.04%
Gamma stock	2.68%	3.65%

[redacted]

The Gilt Market

5. ꞉ugh the gilts market has not performed at all like the equity market in recent weeks, turnover has increased substantially. In the first year since Big Bang, turnover in the gilts market averaged £4-5 billion per day. Roughly half of this was between market makers and half with customers. Since mid-October, turnover has been running at around £6-8 billion per day. The Bank say that the split between intra-market and customer business has remained around 50:50.

(ii) Historical and international comparisons

6. Charts 4 and 5 show UK and US indices on an annual basis since 1900. It is notable that the 1929 crash was considerably more severe in the US than in the UK, but that the 1974 crash, while more pronounced than 1929 in the UK, was relatively minor in the US. By way of illustration, UK share prices fell by 72½% from peak to trough 1972-74 while US prices fell by 48½%. Similar figures (but only available peak year to trough year) for the 1929 crash are a 78% fall in the US compared to 40½% in the UK. So far in 1987, though London has fallen substantially further -32% than New York - 18.6% - since 15 October, their falls since the 1987 high have been broadly comparable, at 36% and 30% respectively.

7. Table 1 shows changes in international equity indices as of close 9 November 1987 on a year earlier, the 1987 highs, and 15 October 1987. The UK performance does not seem exceptional by any of the measures, most striking is the relative buoyancy of the Japanese indices, by almost any measure the most chronically overvalued and out of touch with fundamentals.

8. We have also looked at rates of return on equities measured in terms of profit (earnings) &/or dividends as a measure of how overvalued the equity market was before recent falls. The two measures give conflicting signals when comparing 1974 with recent falls.

[redacted]

Chart 6 shows dividend and earnings yields for the UK since 1963 and Chart 7 since October 15. These charts indicate that while dividend yields in 1987 were below those prior to the 1974 crash earnings yields were still above the lowest levels of the 1970s at around the average for the six years prior to 1974.

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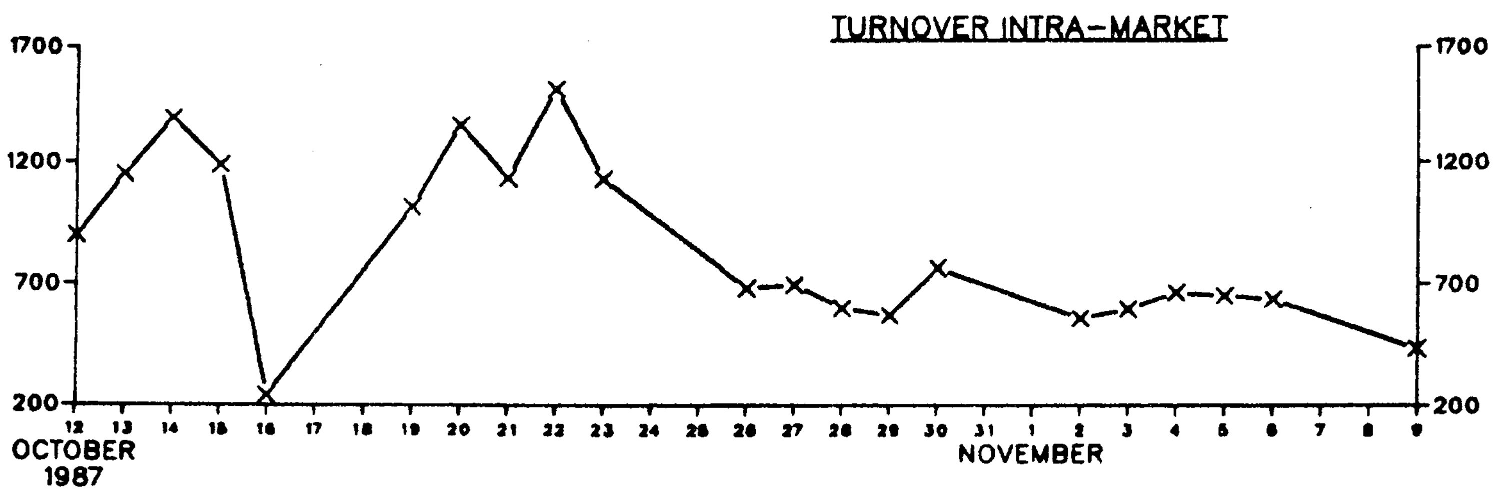
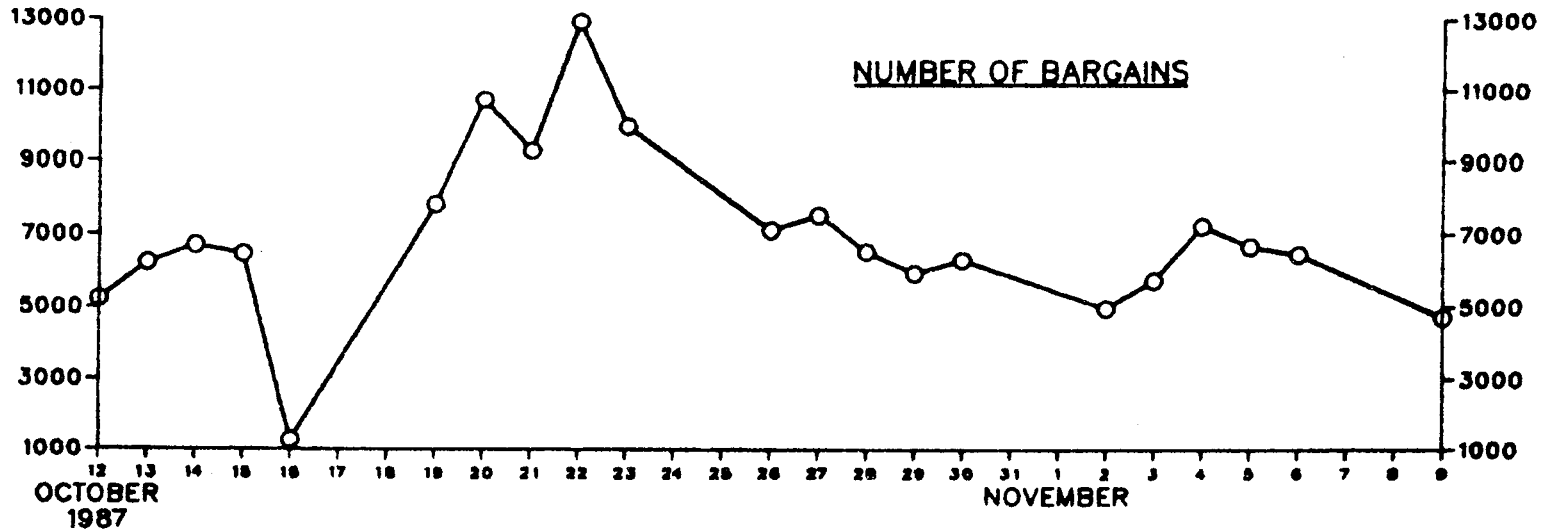
CHART 1

UK LISTED EQUITIES

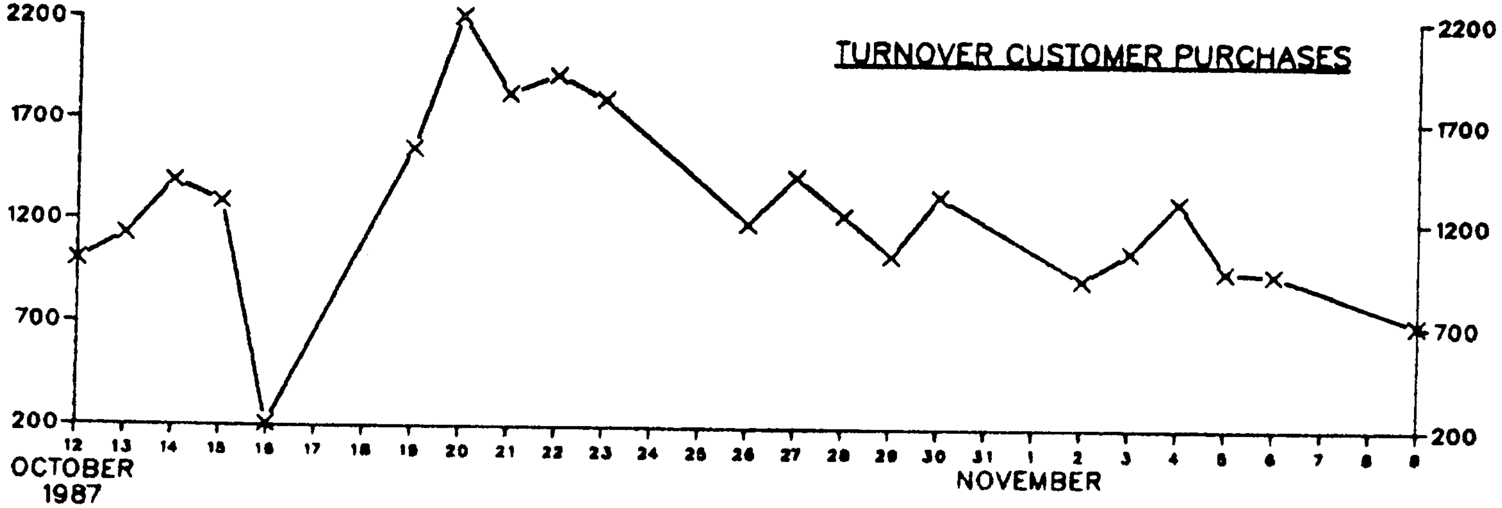


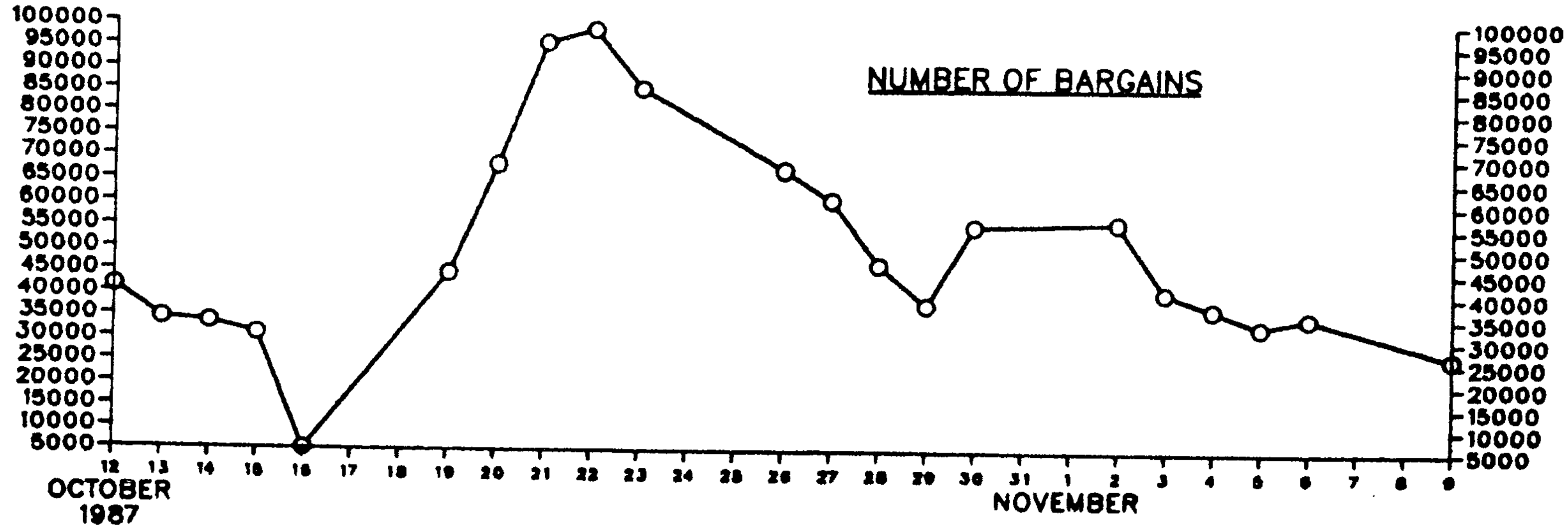


CHARTS.CAPITALS

CHART 2

UK LISTED EQUITIES





CHARTS.CAPITALS

CHART 3.

Fig 2.1

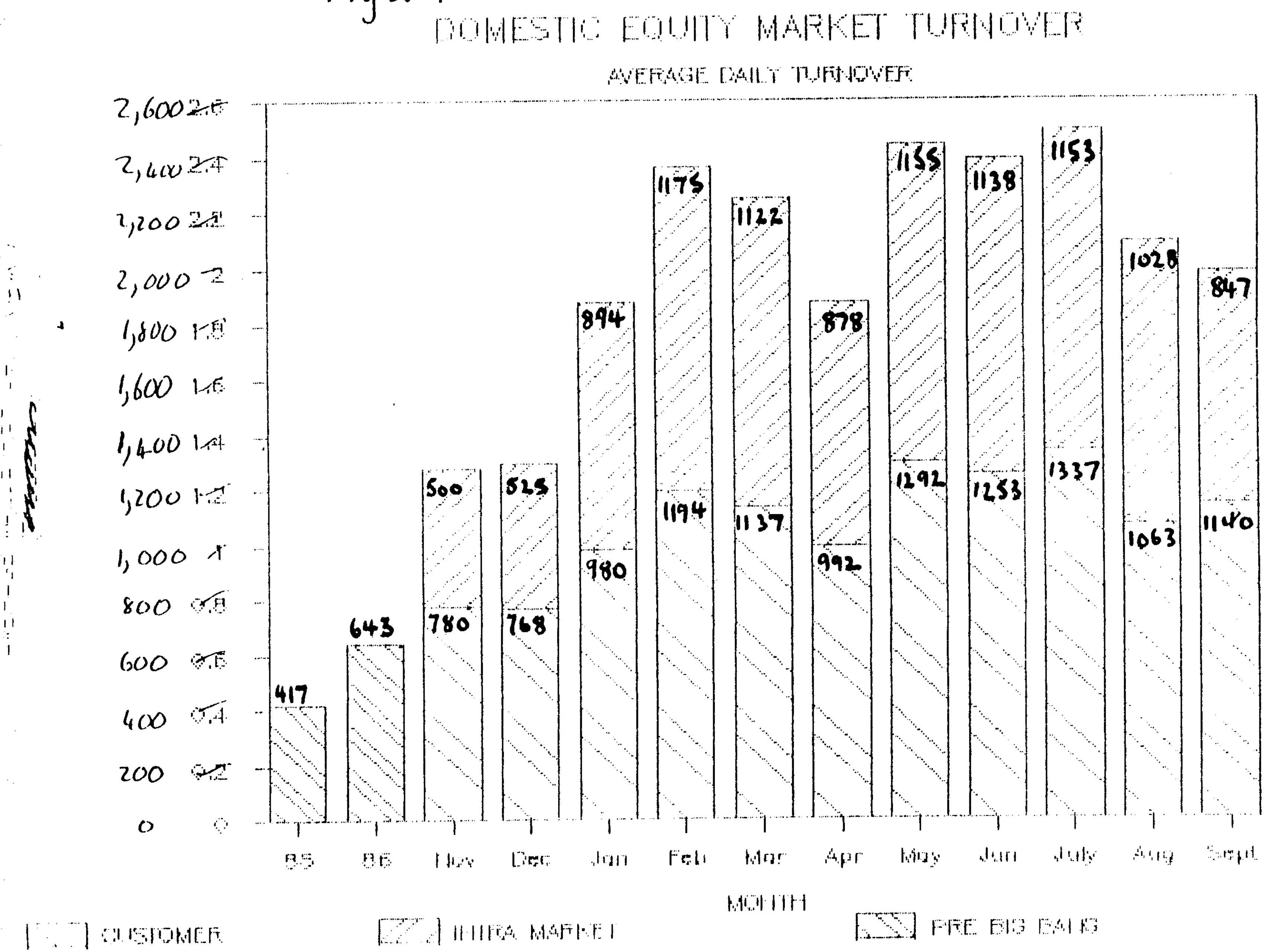


chart 4

Chart UK. 15 Share prices and interest rates, 1900–83

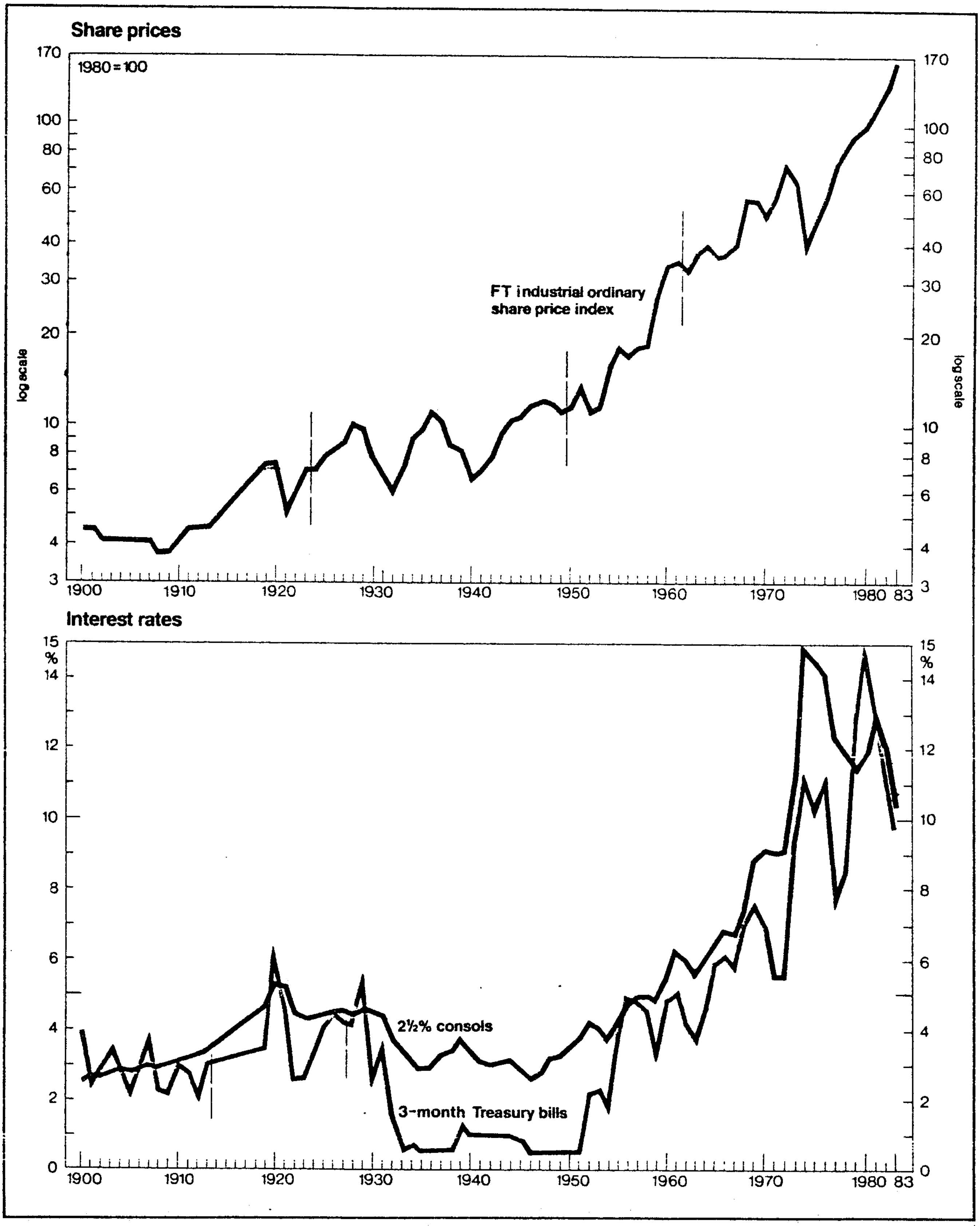
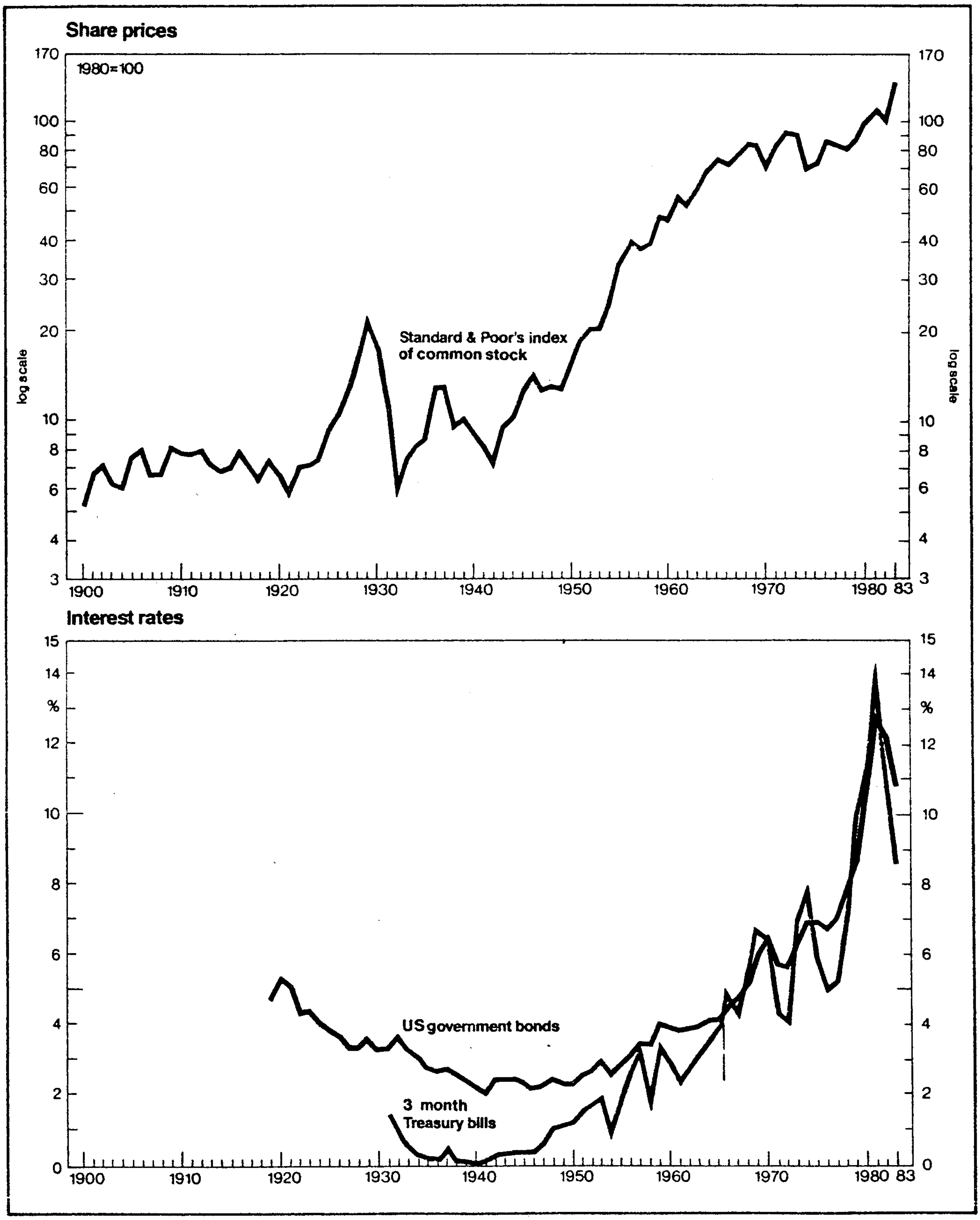


Chart US.15 Share prices and interest rates, 1900–83



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Stock Market Indices Close 9/11/87

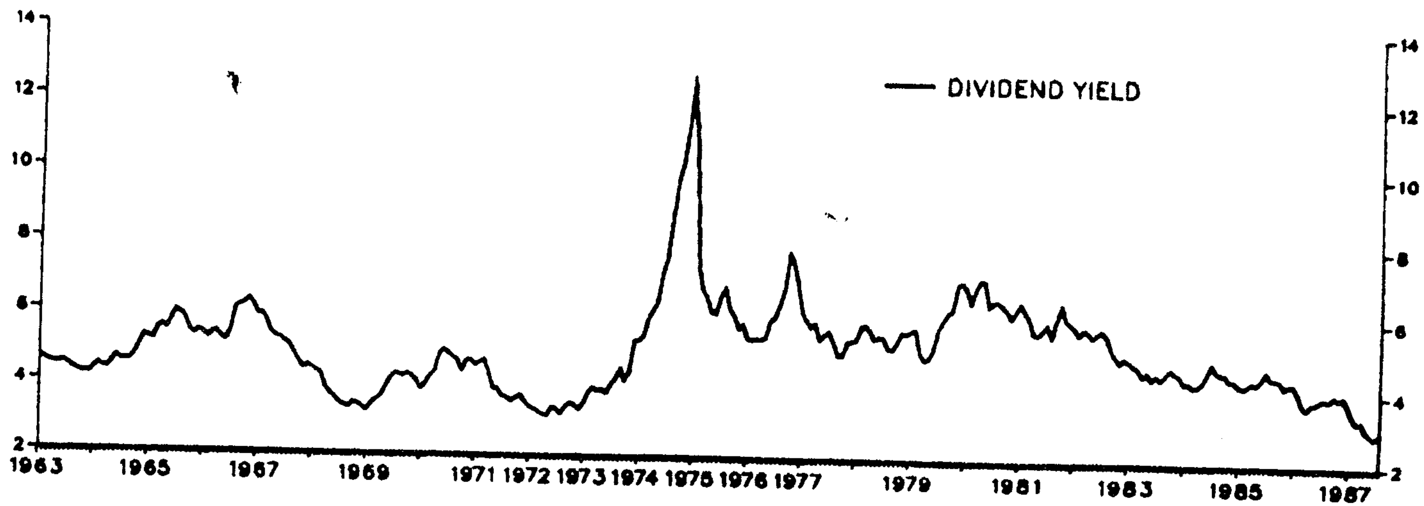
% change on

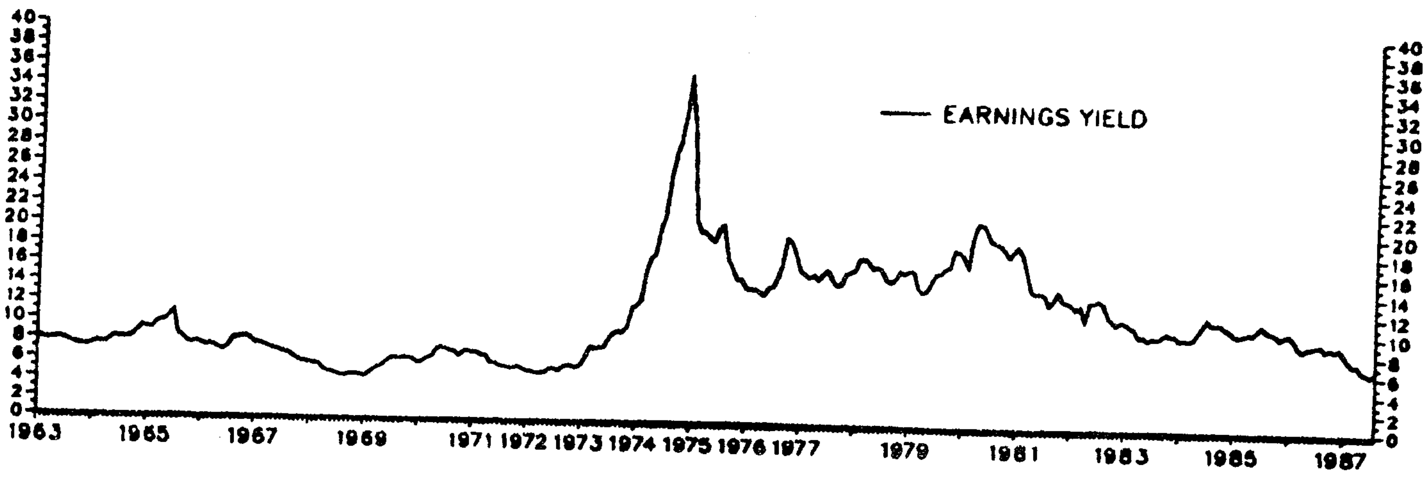
Index	a) year earlier	b) 1987 high	(date of high)	c) 15 October 1987
FTSE	- 5.5	- 35.9	(16 July)	-32.0
Dow Jones	- 0.7	- 30.2	(25 August)	-18.6
Nikki Dow	+36.9	- 15.9	(14 October)	- 9.8
Cac generale (France)	-22.9	- 36.5	(26 March)	-20.2
Commerz bank (Germany)	-34.8	- 36.1	(17 August)	-30.8
Hang Seng (Hong Kong)	- 3.5	- 45.8	(1 October)	-42.1
All 100 (Australia)	-10.8	- 45.7	(21 September)	-41.7
MS Capital International (World) *	+11.3	- 19.4	(27 August)	-17.5

* Close 6/11/87

CHART 6

FT ACTUARIES 500 SHARE INDEX 10th APRIL=10

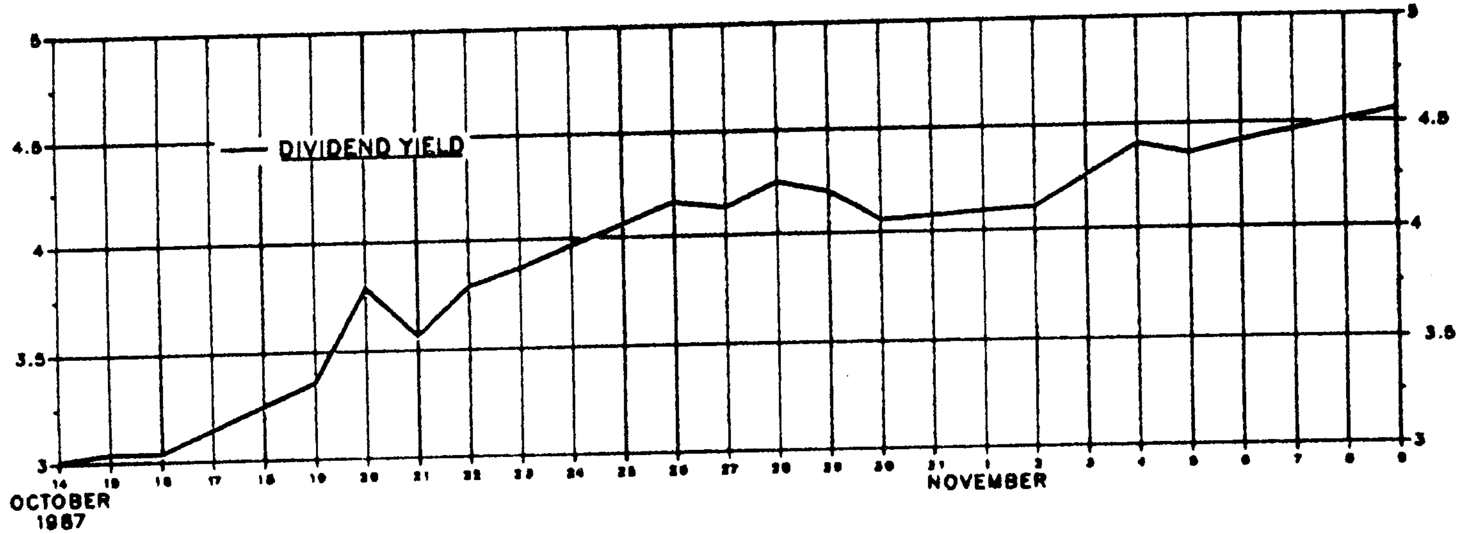


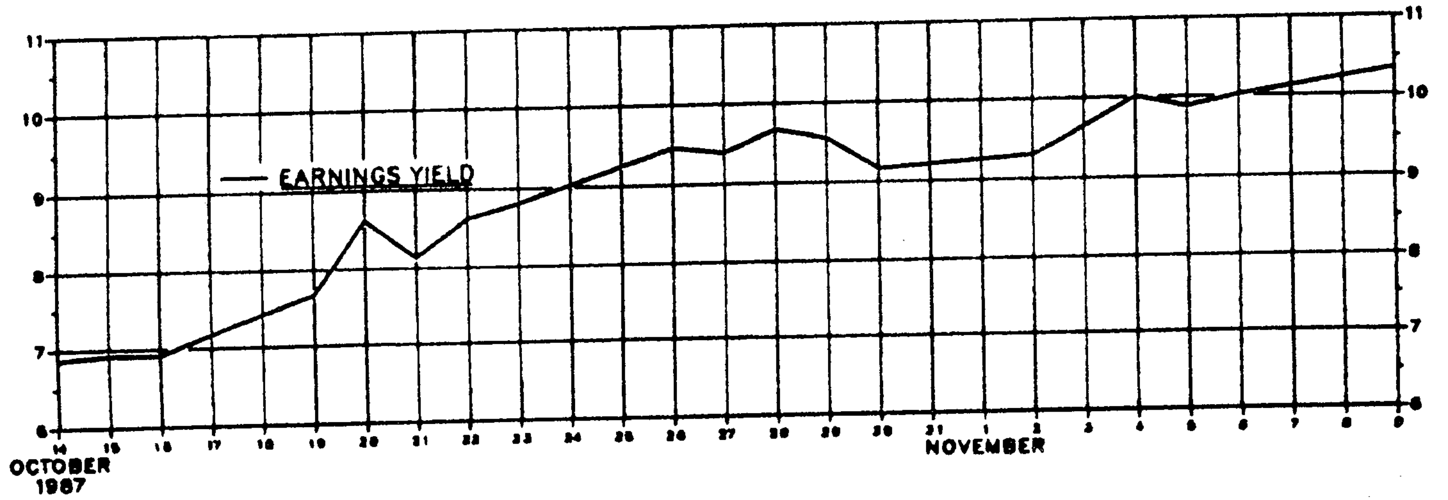


CHARTS.FT1

CHART 7

FT ACTUARIES 500 SHARE INDEX





CHARTS.FT2