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Foreign Transactions in U.S.  
Corporate Stocks

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Net foreign purchases of U. S. corporate stocks in recent years have produced significant net inflows of foreign long-term capital into the United States, thereby strengthening the U. S. payments position. However, the sharp decline in U. S. stock prices in recent weeks has raised the question whether net foreign sales of U. S. stocks, and an accompanying capital outflow from the United States, could be expected on the basis of this development. This paper examines foreign transactions in U. S. stocks since 1954 to determine past foreign practices with respect to investments in U. S. stocks.

Net foreign purchases of U. S. corporate stocks were \$110 million in the first quarter of 1962, about the same as a year earlier. Foreign purchases resulted in a net inflow of foreign long-term capital into the United States of almost \$300 million per year during the past three years (1959-1961), and a total net inflow of more than \$1.5 billion during the past decade. Except for 1952 (when net foreign purchases of U. S. stocks were negligible) and 1958 (when there were net foreign sales), foreign purchases have contributed to U. S. receipts from abroad in all years in the past decade. The higher level of net foreign purchases since 1959 suggests that stock transactions have become a somewhat more important element in U. S. international payments.

The principal conclusions of this paper are as follows:

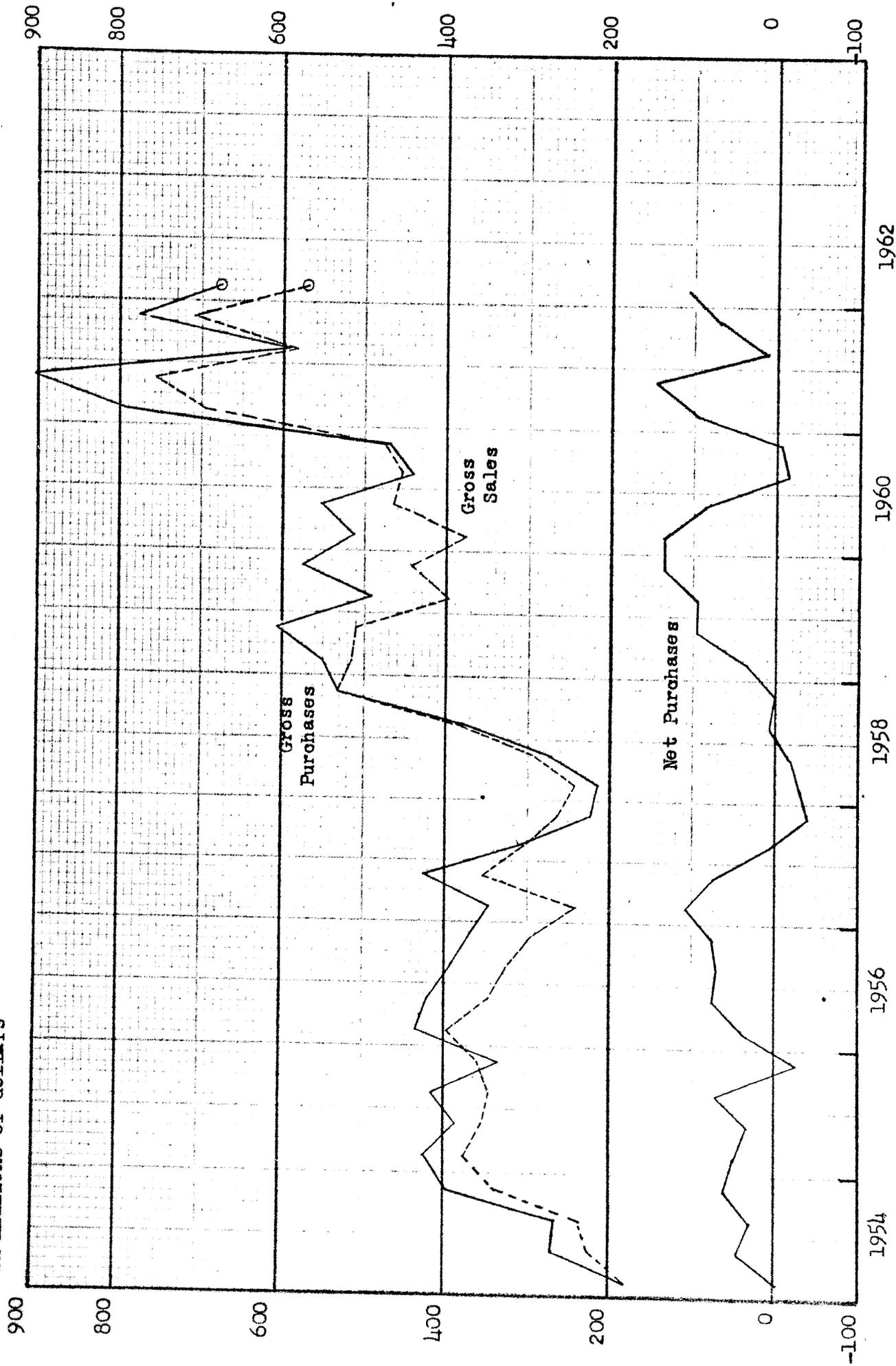
(1) Net inflows of foreign capital through stock purchases have tended to be concentrated in periods of high levels of economic activity in the United States, and in some periods when recovery was underway in this country, such as the second half of 1954 and early 1961. Net inflows have been small or negative during periods of recession.

(2) Variability in net inflows reflects mainly variation in gross foreign purchases of U. S. stocks; there is no evidence at any time over the past ten years of foreign "dumping" of U. S. stocks on a scale significant for the U. S. international payments position.

NOTE: Data on foreign purchases and sales of U. S. stocks are published in the Federal Reserve and Treasury Bulletins. The data are based on reports by banks and brokers and by some commercial concerns. The reporting institution receiving the order from abroad is the one to report the transaction. One possible source of error in the data is the placement of orders by foreigners through institutions that do not report regularly on Treasury Foreign Exchange Form S-1/3, but it is not known whether this potential source of error is likely to be significant. In any event, it is probably possible to regard the reported figures as an index of foreign transactions in U. S. stocks.

Chart 1

Foreign Transactions in U.S. Corporate Stocks  
In millions of dollars



(3) Foreign transactions in U. S. stocks show no evidence of being related in any more direct fashion than indicated in (1) above to changes in prices of U. S. stocks

(4) Foreign transactions in U. S. stocks show no evidence of varying consistently, directly or inversely, with foreign transactions in foreign stocks in the U. S. market; available statistical data are insufficient to show consistent variation of foreign transactions in U. S. stocks with movements of funds into or out of foreign countries through stock market transactions.

Foreign transactions in U. S. stocks

Chart 1 presents quarterly data on gross and net foreign purchases of U. S. stocks. As shown in the chart, foreigners made net purchases of U. S. stocks from the second quarter of 1954 through the third quarter of 1957, except for the last quarter of 1955 which may well be explained by the stock market uncertainty accompanying President Eisenhower's heart attack. Again in 1959, in early 1960, in 1961 and in the first quarter of 1962, there were larger net purchases by foreigners. Net sales by foreigners have been concentrated in the two recession periods, 1957-58 and the last half of 1960 in addition to the sales in late 1955. Since net transactions are a residual of gross foreign purchases and sales, an examination of these latter two series is essential to a study of net transactions.

The single most striking feature of changes in gross foreign purchases and sales of U. S. stocks is the degree to which the two series fluctuate together. As shown in the chart, the quarter-to-quarter changes in the two series were in the same direction in all but 4 of the 28 quarterly changes from early 1955 to early 1962, and the proportion is almost as high if one examines monthly data rather than quarterly. <sup>1/</sup> This fairly pronounced correspondence between changes in gross foreign purchases and sales suggests that in many instances a purchase and a sale may be related to a single investment decision -- that is, that there is a significant volume of shifting within foreign portfolios of U. S. stocks.

A second conclusion from the data on gross transactions is that net foreign sales of U. S. stocks have resulted primarily from decreases in gross foreign purchases rather than from sharply increased gross foreign sales of stocks. Marked declines in gross foreign purchases occurred in the fourth quarter of 1955, in 1957-58, and in the third quarter of 1961, and in each case these declines appear to be the principal cause of the increased net foreign sales, or reduced foreign purchases. A less striking decline in gross foreign purchases in the second half of 1960 contributed to the emergence of net sales, although in this instance gross foreign sales were also somewhat above the average level of the immediately preceding four quarters.

<sup>1/</sup> Correlation of monthly data for gross foreign purchases and sales produced a coefficient of about 0.9. For purposes of comparison, it might be noted that this coefficient was about the same magnitude as that derived from a correlation of the volume of odd lot purchases and sales in the New York market for the same period.

A corollary of this conclusion is that little evidence exists of foreign "dumping" of U. S. stocks as a whole. Between 1955 and early 1962, net foreign sales of U. S. stocks exceeded \$10 million in ten months. However, in only three months (March, 1956; October, 1957; and September, 1960) did gross foreign sales rise by more than \$10 million, and in the first two months cited the increases in sales were accompanied by lesser increases in purchases. These monthly fluctuations are substantially dampened in the quarterly data shown in Chart 1, thus tending to emphasize the short-lived character of the developments lying behind the increases in gross foreign sales.

It is also possible to demonstrate the somewhat greater variability of gross foreign purchases than gross foreign sales by comparing standard deviations of the two series with their respective arithmetic means. However, the economic importance of variation in gross foreign purchases rests less upon such statistical measures than upon the timing of changes in these purchases.

### Price movements

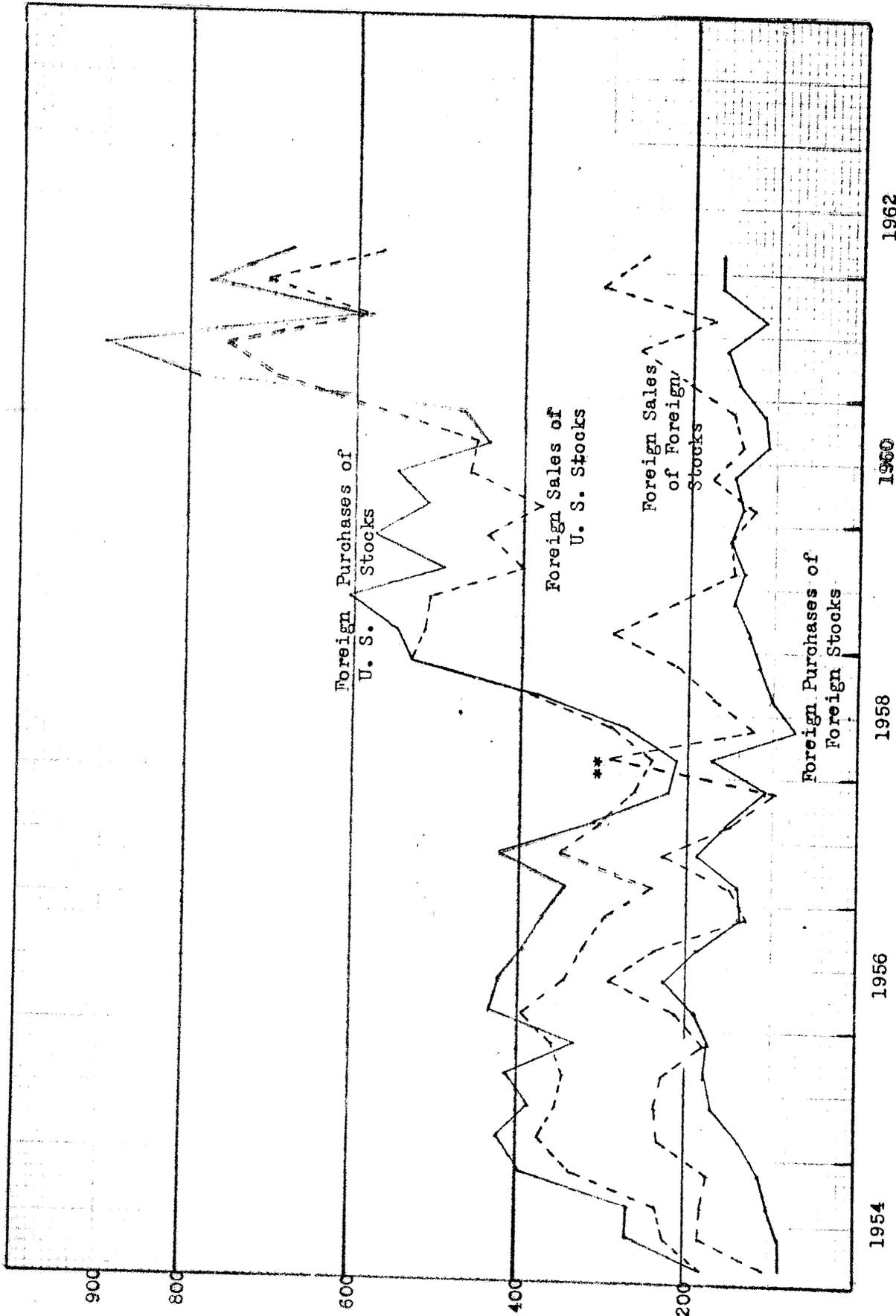
Foreign purchases and sales of U. S. stocks, and by inference the resulting net capital movements, have frequently been associated in the financial press with movements of stock prices. Foreign transactions have been viewed both as a cause and as a consequence of price movements. Although use of aggregate figures on foreign transactions and aggregate indexes of stock prices may obscure important movements in the prices of and trading in major groups of securities within the index, aggregate figures are most appropriate where the principal interest is in net international flows of capital.

Correlation of monthly net foreign purchases of U. S. stocks with changes in the Standard and Poor stock average for the same month produced a coefficient of .03. This figure is not merely low; it is amazingly low. Correlations involving lagged relationships and average price changes over longer periods yielded coefficients slightly larger, but still extremely small. Thus, there is no statistical evidence that net foreign purchases (or sales) are directly related in any significant manner to changes in U. S. stock prices, either as cause or effect.

Efforts to relate foreign transactions in U. S. stocks to changes in prices of foreign stocks proved unsatisfactory primarily because of the diversity of movements of foreign stock prices; in each of the past seven years, except for 1959, one can find at least one major European stock market in which price changes have been, on balance, opposite to those in other major stock markets. It is, therefore, more appropriate to attempt to find relationships between transactions in U. S. and foreign stock markets through examination of capital flows than through guesses as to possible shifts of funds in response to differential price movements.

Chart 2

Foreign Transactions (Gross) in U. S. and in Foreign Stocks  
In millions of dollars



\*\* Reflects in part new issue by Royal Dutch Petroleum Co.

Capital flows

Unfortunately, the data show no consistent relationship between foreign transactions in U. S. stocks and other international flows of funds via stock market transactions. Details are presented below.

(1) Gross foreign purchases of U. S. stocks and gross foreign sales of foreign stocks in the U. S. market fluctuated occasionally in a similar manner from 1955 through 1958, except for the large foreign sales in the first quarter of 1958 in connection with a stock issue by the Royal Dutch Petroleum Co. However, the movements in the two series beginning in 1959 show much less correspondence.

A comparison of net foreign purchases of U. S. stocks with net foreign sales of foreign stocks in the U. S. market, derived from data in Chart 2, reveals little relationship between the two types of transactions; foreigners may at times employ the funds received from sales of foreign stocks in other investments in the U. S. market, but such shifts as have occurred have apparently been sporadic.

(2) German balance of payments data show gross purchases and sales of foreign stocks by Germans and gross purchases and sales of German stocks by foreigners. However, the German data show no correspondence with the U. S. data.

(a) German purchases of foreign stocks, both gross and net, rose to marked peaks in the third quarter of 1959, the first quarter of 1960 and the third quarter of 1960. By contrast, net German purchases of domestic U.S. securities in the U. S. market show only one recognizable peak -- in the first quarter of 1960, when net purchases were \$17 million.

(b) Foreign purchases of German stocks reached a marked peak in the third quarter of 1959, and were maintained at a high level from mid-1960 to the end of 1961. By contrast, net sales of foreign securities in the U. S. market by Germans reached peaks of \$27 million and \$17 million in the first quarter of 1960 and the fourth quarter of 1961, respectively, and were small in the intervening quarters.

(3) Netherlands Bank data give quarterly net transactions in Netherlands and foreign stocks, and in addition annual or semi-annual breakdowns by country of transaction. In principle, such data would seem to offer greater opportunities for identifying unambiguously movements of funds via stock exchange transactions; in practice, there are some discrepancies.

(a) Netherlands data show sizable net purchases of U. S. securities in 1959, negligible net purchases in the first half of 1960, and net sales in the last half of 1960. U. S. data show Netherlands

purchases in the U. S. market of \$40 million in 1959, purchases about one-fourth this amount in the first half of 1960, and net sales in the last half of 1960. The movements are sufficiently parallel, and the amounts of sufficiently close magnitudes to constitute a reasonable confirmation.

(b) On the other hand, Netherlands statistics show U. S. purchases of about \$125 million in both 1959 and 1960, whereas U. S. data show Netherlands net sales of foreign securities of only about one-third this amount in 1959, and about two-thirds this amount in 1960. The differences may in part reflect Netherlands transactions in other foreign securities in the U. S. market, but the absence of a close relationship forces a substitution of surmise for statistics.

Conclusion. If balance of payments data were detailed enough to permit the construction of a matrix of international stock exchange transactions among leading securities markets, one might be able to link changes in net foreign holdings of stocks in one market with changes in other markets. Such a process of linking would not, by itself, represent an explanation of the transactions, although by throwing light on additional factors that contribute to stock market decisions it might aid in determining the reasons for shifts in foreign holdings. Given the current state of the data, however, there appears no sound basis for going beyond a description of aggregate transactions. The conclusions warranted by such a descriptive approach have been cited at the beginning of this paper.