DIVISION OF INTERNATIONAL FINANCE

BOARD OF GOVERNORS
OF THE
FEDERAL RESERVE SYSTEM

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CAPITAL MARKET DEVELOPMENTS ABROAD

I. Japan: Money and Capital Markets in October

For the second time in a month, the Bank of Japan on November 27 lowered its basic discount rate by 0.365 percentage points to 6.57 per cent. Earlier on October 27 the rate was cut from 7.3 to 6.935 per cent and reserve requirements were lowered. Both reductions represented an easing of the tight money policy which had been in effect since July and September of 1961.

While the October rate reduction was justified by evidence that the balance of payments problem had been solved, it would appear that outside pressure rather than a new reading of the economic trends was the decisive factor behind the November 27 reduction.

The trade deficit, seasonally adjusted, took a turn for the worse in October as exports fell and imports increased. Wholesale prices also continued their uptrend in October from a June 1962 low. Other factors that indicate some possible pressure on the balance of payments in the coming months include: a heavy schedule of debt servicing as Japan repays the special one-year credits obtained from U.S. banks between November 1961 and July 1962; the recent liberalization of imports on October 1, 1962; and encouragement from the IMF to further liberalize imports. On November 17, the head of the IMF consultations team to Japan stated that Japan's international payments balance had improved to such a point that she was no longer justified in maintaining exchange controls for balance of payments reasons.

Japan is planning to issue new securities in the US in December totaling $29 million. Additional issues totaling $35 million are at present planned for the first quarter of 1963.

Money Market. Money market conditions eased in October as various expansionary developments more than offset a contraction in Bank of Japan credit. On the contractionary side, Bank of Japan loans and discounts declined ¥150 million and bank notes in circulation rose ¥20 million. These developments were more than offset by net Treasury disbursement of ¥209 billion and a rise in Bank of Japan holdings of government bonds of ¥152 billion. Reflecting this easing, call loan rates declined in the money market in October.

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Interest rates. The general level of interest rates is expected to decline in response to the two recent cuts in the Bank of Japan's basic discount rate late in October and November. Commercial bank rates were lowered on October 31 in correspondence with the October 27 cut in the discount rate and a similar action in late November or early December is anticipated.

The average rate for bank loans and discounts continued to rise gradually through August. From a level of 8.23 per cent in July, the rate advanced to 8.24 per cent in August. (See table below). A leveling off or decline in the rate is likely in October or November. In the call loan market, the rate for loans callable at a day's notice fell to 10.22 per cent in October from a level of 11.68 per cent in August and September.

Average Monthly Interest Rates on Bank Loans and Discounts

	1959	1960	1961	1962
March	8.18	8.21	7.92	8.22
June	8.08	8.22	7.88	8.23
September	8.06	8.14	8.00	8.24 1/
December	8.11	8.08	8.20	

1/ August.

Bank loans and discounts. Bank credit rose 1.7 per cent in September compared to a rise of 1.8 per cent a year earlier. The increase in loans and security holdings was less than a year earlier, but bills discounted rose at a faster pace. Deposits increased 5.1 per cent in September against a rise of 3.8 per cent a year earlier.

During the third quarter of this year, bank credit expanded 3.3 per cent compared to 4.4 per cent a year earlier. As indicated in the table below, the rise in all assets was at a slower pace than a year earlier. Deposits picked up, however, rising 6.4 per cent in the quarter against 3.8 per cent a year earlier.

Commercial Banks: Quarterly Changes in Deposits and Principal Assets
(In billions of yen)

				MAIN ASSETS						
		Deposits	Per cent Change	Loans	Per cent Change	Bills Discounted	Per cent Change	Securities	Per cent Change
1960	I	+249	3.4	+176	3.8	+ 54	2.5	+ 78	6.5
	II	+ 96	1.3	+167	3.5	+ 87	3.9	+ 75	5.8
	III	+506	6.5	+244	4.9	+172	7.5	+ 35	2.6
	IV	+607	7.3	+347	6.7	+185	7.5	+127	9.1
1961	I	+502	5.7	+326	5.9	+ 48	1.8	+103	6.8
	II	+169	1.8	+206	3.5	+133	4.9	+104	6.4
	III	+359	3.8	+216	3.6	+206	7.3	+ 43	2.5
	IV	+430	4.3	+232	3.7	+220	7.2	+122	6.9
1962	I	+128	1.2	+256	3.9	+ 14	0.4	- 64	-3.4
	II	+ 61	0.6	+181	2.7	+108	3.3	+258	14.1
	III	+678	6.4	+223	3.2	+213	6.3	+ 41	2.0

The proportion of bank loans and discounts extended for purchases of equipment fell from 17.4 per cent in August to 17.2 per cent in September, the same level as in January-February of this year.

Bond market. New issues of industrial debentures rose sharply in September and helped boost the total amount of new bond and debenture issues to ¥109 billion against ¥91 billion a month earlier. From a range of ¥10-15 billion since October of 1961, new issues of industrial debentures rose to ¥22 billion in September. New issues of public corporate debentures rose to ¥23 billion in August and new issues of bank debentures were relatively unchanged.

Average yields on most bonds and debentures remained unchanged in September from the levels since the first of the year. Yields on industrial bonds, however, rose slightly during the month.

Stock market. Except for a brief rally in the first eight days of the month, the stock market generally eased during October and on the 29th reached the lowest level in two years. This represented a decline of 24 per cent from the year's high on February 14. In November, the market rose substantially and by December 3 had recovered 65 per cent of the ground lost between February and the end of October.

An important factor in the recent market recovery is believed to have been the extension of special loans to the major security companies. In mid-October, the Ministry of Finance authorized a loan of ¥6 billion from various financial institutions to the four major securities companies, and on November 8 it was announced that 14 leading Japanese banks had agreed to supply a similar number of investment trusts with loans totaling ¥9 billion.

Dow Jones Average of 225 Stocks
Tokyo Stock Exchange

Sept.	26	¥1,297	Nov.	7	¥1,372	1961	High	¥1,830
				14	1,413		Low	¥1,250
Oct.	3	1,240		21	1,393			
	10	1,302		28	1,440	1962	High	¥1,590
	17	1,246					Low	¥1,216
	24	1,244	Dec.	3	1,457			
	31	1,260						

Foreign trade. The seasonally adjusted trade deficit, which narrowed sharply during the January-September period this year, widened substantially in October to $69 million or $828 million at an annual rate. This compares with a third quarter trade deficit computed at an annual rate of $156 million and a peak deficit in the fourth quarter of last year of $2,184 million. As indicated in the table below, exports fell $24 million in October to $425 million and imports rose $55 million to $494 million. With the second reduction in the Bank of Japan's discount rate on November 27, encouragement from the IMF to further liberalize imports, and a heavy schedule of debt repayment, some pressure on the balance of payments is expected in the coming months. The seasonally adjusted trade figures (monthly, or monthly averages, on a customs basis in millions of dollars) in the table below are based on seasonal adjustment factors computed by the Bank of Japan under the U.S. census method.

		Exports	Imports	Trade Balance
1960	Year	338	374	- 36
1961	Year	353	484	-131
	I	343	427	- 84
	II	351	464	-113
	III	357	506	-149
	IV	364	546	-182
1962	I	371	492	-121
	January	354	497	-143
	February	382	498	-116
	March	378	481	-103
	II	409	466	- 57
	April	361	482	-121
	May	447	477	- 30
	June	418	435	- 17
	III	434	447	- 13
	July	430	453	- 23
	August	422	447	- 25
	September	449	439	+ 10
	October	425	494	- 69

Exchange reserves and capital flows. In November Japan repaid $50 million of the $200 million borrowed from three US banks between November 1961 and February 1962. As a result of this repayment, reserves fell $12 million from $1,805 million at the end of October to $1,793 million at the end of November. Japan is scheduled to repay $50 million a month of the remaining $150 million between December 1962 and February 1963. Between February and July 1963, Japan is scheduled to repay $125 million borrowed earlier this year from seven U.S. banks.

Japanese reserves had risen $85 million in October to a level of $1,805 million. This reflected a substantial surplus on current account and a net inflow of both long-term and short-term capital. The October gain brought reserves to a level $319 million above the cyclical low last December.

The balance of payments, as measured on an exchange transactions basis, continued to improve in October as the surplus on current account, not seasonally adjusted, rose to $70 million against $62 million in September. Net long-term capital receipts fell to $13 million in contrast to the unusually high figure of $79 million in September. Net short-term receipts were $22 million in October in contrast to a net short-term outflow of $87 million in September. With net capital receipts of $35 million and a net outflow under errors and omissions of $20 million in October, the over-all balance registered a surplus of $85 million.

Japanese short-term liabilities to the United States declined $53 million in September to a level of $1,683 million. As indicated in the table below, this restores the total liabilities to the level prevailing last April and May. The rise in liabilities during the June-August period reflects the inclusion of data from agencies of Japanese banks in San Francisco that had not previously been reporting.

	1959	1960	1961	1962		1959	1960	1961	1962
Jan.	168	362	875	1,515	July	256	586	1,341	1,731
Feb.	175	372	952	1,605	Aug.	269	628	1,335	a/1,736
Mar.	204	420	1,069	1,698	Sept.	262	660	1,288	a/1,683
Apr.	224	456	1,159	1,688	Oct.	262	693	1,281	
May	242	488	1,196	1,678	Nov.	275	711	1,292	
June	260	497	1,272	1,728	Dec.	324	806	1,445	

a/ Preliminary estimate.

Note: Data since June 1962 include reports of certain banks not previously included. The inclusion of these banks increased the reported figure in June 1962 by $48 million.

In December 1962 the Tokyo Shibaura Electric Company expects to issue privately in the U.S. $20 million in 15-year, 6½ per cent, convertible debentures and the Honda Motor Company plans to offer publicly $9 million in stock in the form of American depository receipts. During the first quarter of 1963, Mitsubishi Electric Company and the Japan Development Bank plan to issue publicly $15 and $20 million in bonds, respectively.

Foreign exchange. A strengthening of the exchange rate for the yen in the forward market in October narrowed the forward discount from 1.44 per cent during the first 20 days of the month to .89 per cent during the last three days of the month and the first ten days of November. Between November 12-15 the forward rate weakened and the forward discount rose to 1.06 per cent. (See table below). The exchange rate in the spot market remained at the official support level throughout October and the first half of November.

Customer's T.T. Exchange Rates of Bank of Tokyo in Tokyo

Date	Yen-dollar spot middle rate	Three-month forward middle rate	Forward discount in per cent per annum
Sept. 28	358.90	360.20	1.44
Oct. 5	358.90	360.20	1.44
12	358.90	360.20	1.44
19	358.90	360.20	1.44
26	358.90	359.75	.95
31	358.90	359.70	.89
Nov. 2	358.90	359.70	.89
9	358.90	359.70	.89
15	358.90	359.85	1.06

Asia, Africa and Latin America Section

II. India: Money and Capital Markets During 1962

In mid-summer, prior to the Chinese invasion, the Indian authorities had taken steps to restrict credit availabilities and had begun to explore means of mobilizing the country's private gold hoards which has been roughly estimated by the Reserve Bank at $4 billion. Since the attack, they have offered a wider range of securities to the public, both against cash and against gold, at rates of interest above those previously in effect. They have also taken further steps to divert credit availabilities to specified "essential" purposes. Both the stock and gold markets declined sharply in reaction to the attack.

In July, the Indian authorities undertook a number of measures to tighten credit. The Reserve Bank added to the bank rate (4 per cent) and two penalty rates (5 and 6 per cent) a third penalty rate of 6-1/2 per cent and lowered the ceilings at which each penalty rate applied. In effect, the average rate paid by the banks was raised by about 1/2 per cent. Higher interest rates were offered on new issues of government securities and the rate on post office savings deposits was raised from 2.5 to 3.0 per cent, the rate now paid by most commercial banks.

In mid-September, new measures to restrict bank credit expansion were announced. The overall reserve requirements of the banks were changed as follows (as per cent of deposits):

	Balances at Reserve Bank	Government Securities
Before	5% for demand 2% for time	20%
After	3% for all deposits	25%

After the Chinese invasion on October 20, the authorities took additional steps on two main lines. To control credit, the following steps were taken:

November 1. The Reserve Bank placed an absolute limit on borrowings by each commercial bank, instead of depending solely on the July schedule of graduated interest charges.

November 8. Conference of leading commercial banks, convened by the Reserve Bank, agreed to shift credits from defined nonessential purposes to defense, essential consumer goods and export financing.

November 10. As a seasonal adjustment, the Reserve Bank agreed to make loans above the credit limits announced on November 1 for a temporary period of six weeks.

November 16. Foreign banks operating in India and Indian banks operating abroad were advised by the Reserve Bank to bring foreign funds to India to the maximum possible extent.

To mobilize private gold hoards on a voluntary basis, the Indian authorities took two steps. They encouraged private contribution of gold and gold ornaments to the defense effort and they also offered for the first time in India's history a 6-1/2 per cent gold bond. Rumors about possible confiscation of gold hoards under new legislation passed in August caused gold prices to fall even before the Chinese attack. Following the outbreak of hostilities, prices fell nearly 18 per cent on the Bombay gold market in the first four weeks. On November 14, forward trading in gold was banned.

Stock prices also fell sharply after October 20. As an emergency measure, the exchanges in Bombay and Ahmedabad were closed for one week; the other five Indian exchanges continued trading although minimum prices on individual stocks were in effect in at least three of these markets. Minimum prices also were put into effect in the two closed exchanges when they reopened.

These financial developments took place within what is called the "organized sector" of the Indian financial structure which consists of western-type commercial and cooperative banks. The large "unorganized sector" in India comprises the individuals and family firms who act as traditional money-lenders in rural areas and as deposit-receivers and money-lenders in urban areas. The indigeneous bankers and the money-lenders play an important role in financing the requirements of agriculture, internal trade and small industries. The link between the two sectors has been growing, encouraged by the Reserve Bank, which is attempting to expand its control over the unorganized sector.

Money market. Despite increased restrictions on credit, the rate for day-to-day money has so far been below the 1961 levels. (See Table 1). Money rates follow a strong seasonal pattern and are highest between November and April when crops are harvested. Inter-bank call money is the principal short term money instrument in India. Treasury bills are held mainly by the Reserve Bank of India, and there is no active market for them.

Table 1 Inter-bank Call Money Rates in Bombay
(in per cent per annum)

Average of months	1961	1962
I	5.23	4.72
II	4.86	3.59
III	3.19	2.82
Oct.	4.23	3.05 a/
IV	4.11	

a/ average of Fridays

Bond market. In accordance with the usual practice of floating loans only between May and October (the slack season when the banks have funds available to purchase bonds), the government announced three new issues in July at somewhat higher interest rates than were prevailing in the market at that time as the following yields show (in per cent per annum):

	New Bond Yield	Market Yield
6-year bond	3.90	3.78
10-year bond	4.10	3.98
23-year bond	4.5	--

These are largely held by financial institutions, by State Governments and by the Reserve Bank. Financial institutions are compelled by law to invest a portion of their funds in Government bonds; recent changes in the requirements for the commercial banks were set forth in the summary of this paper. As a rule, the joint-stock companies are not allowed to raise capital during the period when the Central and State Governments are expected to approach the market.

In November, after the Chinese attack, the following new bonds, which are designed to appeal particularly to individual purchasers, were offered for public subscription:

Security	Interest Rate	Maturity (years)	Units of Issue (in Rs.)	Special Feature
National Defense Bonds	4-1/4	10	100	Interest semi-annual
Defense Deposit Certif.	4-1/2 4-3/4	10 12	50 5 to 25,000	Free of income tax; holdings limited
Premium Prize Bonds	--	5	5 and 100	Two drawings for every Rs. 10 million worth of bonds sold.

The interest rates on former Deposit Certificates were 1/2 per cent below those of the new series.

Gold market. The price of gold climbed in India in the first eight months of 1962. On August 31, the price reached $84.85 per fine ounce, the highest level (in terms of U.S. dollars) in effect since the devaluation of the rupee in September 1949. Thereafter the price declined: it fell slightly in September and more rapidly during October and early November. The price of $64.85 per ounce on November 23 was the lowest price in over three years. (See Table 2).

Table 2 Price of Gold Bullion in Bombay
(in dollars per fine ounce) a/

Average of period

1961	I	78.61	1962	I	78.38
	II	78.54		II	80.60
	III	80.01		July	82.35
	IV	79.95		Aug.	82.83
				Sept. b/	81.20

Selected dates

1962	Oct. 5	78.12	Nov. 2	77.54
	12	76.06	9	71.47
	19	75.94	16	68.66
	26	78.66	23	64.85

a/ average spot quotation, converted into dollars at par value

b/ average of Fridays

The fall in gold prices from the August highs followed Parliamentary approval of legislation providing for additional controls over the gold trade. At the time, the Reserve Bank sent notices to the bullion associations requesting information on the gold trade. As a result, rumors began to circulate that the Government was about to freeze or confiscate private holdings of gold and individuals began to withdraw gold bars and ornaments from safe deposit boxes and to exchange gold for rupees and diamonds. This selling of gold accelerated after the Chinese invasion because of fears that gold holdings above a certain level would be confiscated.

The authorities then announced that, effective November 12, gold bonds would be issued for 15 years at a 6.5 per cent interest rate. The gold was to be valued at the world price of Rs 53.58 per 10 grams ($35 per ounce) or less than half the market quotation in Bombay. The bonds were to be redeemed in rupees. Thus, the higher interest rate does not compensate purchasers for the capital loss on the market value of gold. Because the bonds do not include a gold guarantee, the purchaser is not protected against a devaluation of the rupee. Despite these economic disadvantages, the Government hopes that the patriotism aroused by the Chinese conflict will encourage purchases of the bonds.

The Government has also established a National Defense Fund to encourage the voluntary contribution of gold and gold ornaments. However, most contributions are reported to be in the form of cash.

The higher prices on gold in Indian markets reflect the regard among the population of gold as a form of investment, a means of retaining savings, a hedge against inflation, a way of hiding profits from the tax collector as well as the attractiveness of gold for social purposes. The Reserve Bank has estimated that total private hoards in the country might come to as much as $4 billion. The Indian gold price has been double world levels (at the official rate of exchange), largely because restrictions have limited the flow of gold from abroad and the government has been buying all the newly mined gold.

Stock market. Indian stock prices reached a post-war peak in May and thereafter drifted downward in line with the trend of stock prices in other countries. Since the Chinese invasion the decline has accelerated. By November 10, the index average was quoted about 6 per cent below the October 13 level and about 14 per cent below the May peak. (See Table 3).

Table 3 Price Index of Variable Dividend Industrial Securities: All India
(1952-53 = 100)

Average of period					
1961	I	171.2	1962	I	190.0
	II	181.2		II	192.6
	III	179.7		July	184.0
	IV	184.0		Aug.	187.0
				Sept. a/	184.0
Selected dates					
1962	Oct. 6	181.3		Nov. 3	171.8
	13	180.3 b/		10	168.8 c/
	20	179.7			
	27	174.4			

a/ Average of Fridays
b/ Excludes the Calcutta market which was closed for the week
c/ Provisional

On November 5, after a period of very heavy selling, the stock exchange in Bombay (and also Ahmedbad) was closed for one week. When it re-opened on November 12, there were restrictions on new purchases and sales, and floor prices were set for the stocks. Earlier, the stock exchanges at Calcutta, Madras and Delhi had fixed minimum prices, with the result that trading was negligible, due to a lack of buyers, and price quotations were nominal. At present, more than 2,000 securities are listed on the Indian exchanges with a face value of Rs. 13 billion or $2 billion at the official exchange rate. Despite the recent expansion of the market for company securities in India, medium-and large-scale private firms still depend mostly on internal financial resources.

Banking developments. Between October 1961 and October 1962, deposits increased by 13 per cent. (See Table 4). Total bank credit has risen roughly with the increase in deposits. However, the banks' holdings of government securities have not expanded proportionately. In October 1962, they were 34.7 per cent of total bank deposits, well in excess of the new 25 per cent statutory minimum now in effect.

Table 4 Scheduled Banks: Changes in Deposits and Principal Assets
(in billions of rupees - last Friday of period)

		Deposits	Quarterly per cent change	Principal Assets (as per cent of deposits) Total bank credit	Investments in gov't. securities	Cash and balances with Reserve Bank
1961	I	17.46	-	72.48	30.68	6.40
	II	17.76	1.7	71.66	30.94	8.01
	III	17.99	1.3	67.78	34.30	6.48
	Oct.	18.11	-	67.71	35.54	7.29
	IV	18.25	1.4	69.94	31.80	8.30
1962	I	19.17	5.0	73.69	31.50	6.45
	II	20.12	5.0	70.56	30.18	7.37
	III	20.35	1.1	67.72	33.90	6.21
	Oct.	20.47	-	67.65	34.74	6.24

On November 1, the Reserve Bank of India reduced its ceilings for loans to commercial banks and hardened its lending rates. Each bank will normally not be permitted to borrow funds from the Reserve Bank beyond the limit of 100 per cent of its statutory reserve balances at the Reserve Bank. In exceptional circumstances, the Reserve Bank may grant credits above this limit, at an as yet unspecified penal rate of interest (instead of the previous $6\frac{1}{2}$ per cent). On November 10, the Reserve Bank eased this regulation. For a period of six weeks, it agreed to lend to commercial banks at $6\frac{1}{2}$ per cent amounts in excess of the 100 per cent limit, up to the maximum amount borrowed by each bank from the Reserve Bank in the 1961-62 busy season (November-April).

India has 66 domestic and 15 foreign scheduled banks (that is, banks with specified minimum paid-up capital and reserves), but the State-owned Bank of India accounts for nearly 30 per cent of deposits in these banks. (The 212 non-scheduled banks account for only 2 per cent of total commercial bank deposits). Most of the banks provide short-term credits in the form of loans, overdrafts and cash credits, which are often rolled over from one period to another. Bills purchased and discounted account for only 15 per cent of total bank credit.

Exchange reserves. Indian foreign exchange reserves have been declining since the end of 1961 and at the end of October were valued at $442 million, only $22 million above the Rs. 2 billion ($420 million) which the Reserve Bank is required to hold as currency cover (57.5 per cent of which must be held in gold). (See Table 5). The total decline during 1962 (excluding a drawing of $25 million from the IMF on July 27) has been $146 million. The increases shown in Table 5 for 1961 were mainly the result of a net drawing from the Fund of $122.5 million in July 1961.

Table 5 India: International Monetary Reserves
(in millions of dollars - last Friday of period)

		Gold	Foreign Exchange	Total	Change from preceding period
1961	I	247	286	533	
	II	247	239	486	-47
	III	247	272	520	+34
	IV	247	316	563	+43
1962	I	247	272	520	-43
	II	247	204	452	-68
	III	247	197	445	- 7
	Oct.	247	194	442	- 3

Asia, Africa and Latin America Section.

II. Nine Charts on Financial Markets Abroad

Chart 1 - Interest Arbitrage, United States/Canada
Chart 2 - Interest Arbitrage, New York/London
Chart 3 - Interest Arbitrage for German Commercial Banks
Chart 4 - Interest Arbitrage, Frankfurt/London
Chart 5 - Short-term Interest Rates
Chart 6 - Long-term Bond Yields
Chart 7 - Industrial Stock Indices
Chart 8 - Spot Exchange Rates - Major Currencies Against U.S. Dollar
Chart 9 - 3-month Forward Exchange Rates

Chart 1

INTEREST ARBITRAGE, UNITED STATES/CANADA

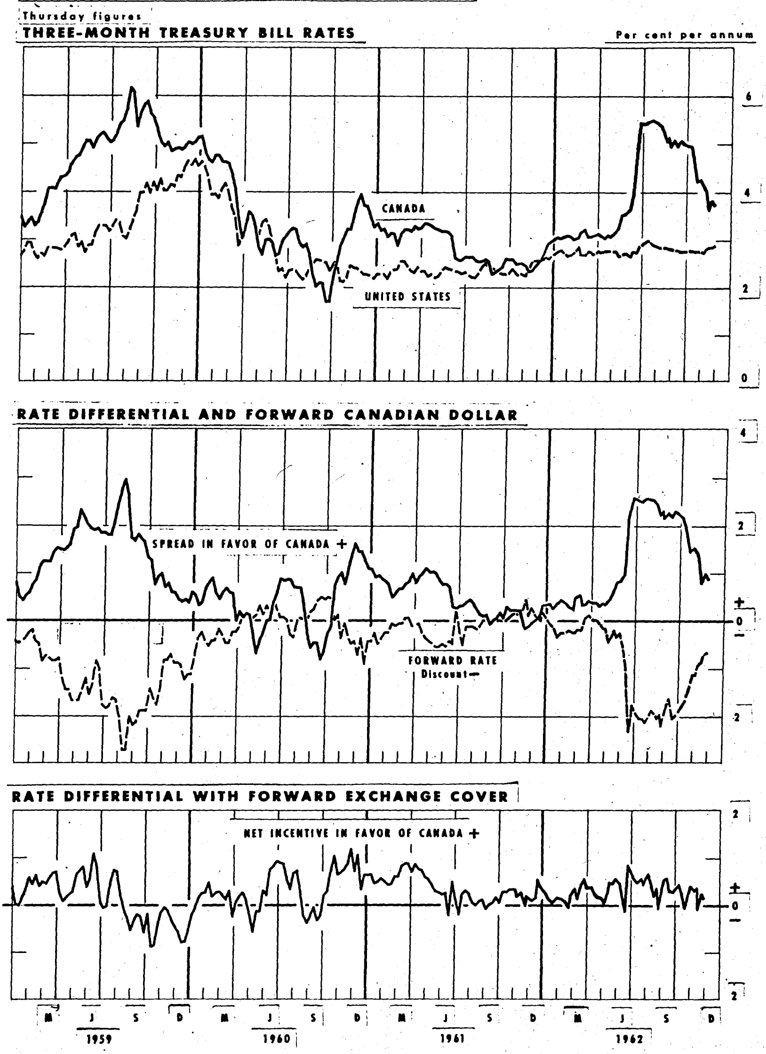

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Chart 2

INTEREST ARBITRAGE, NEW YORK/LONDON

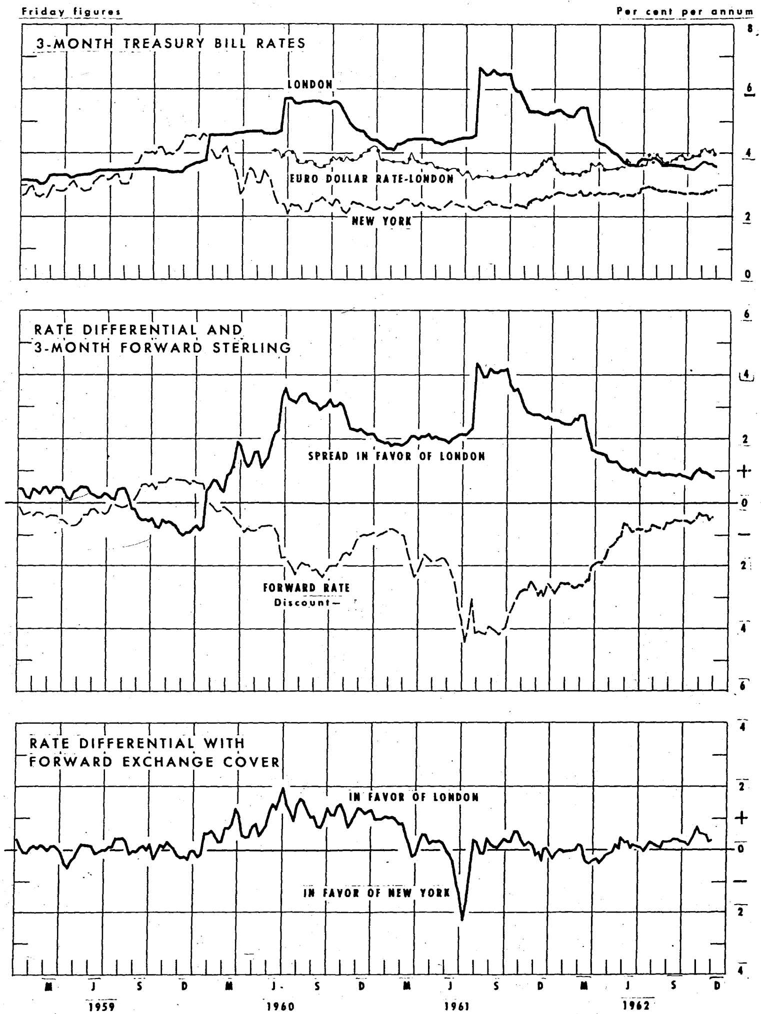
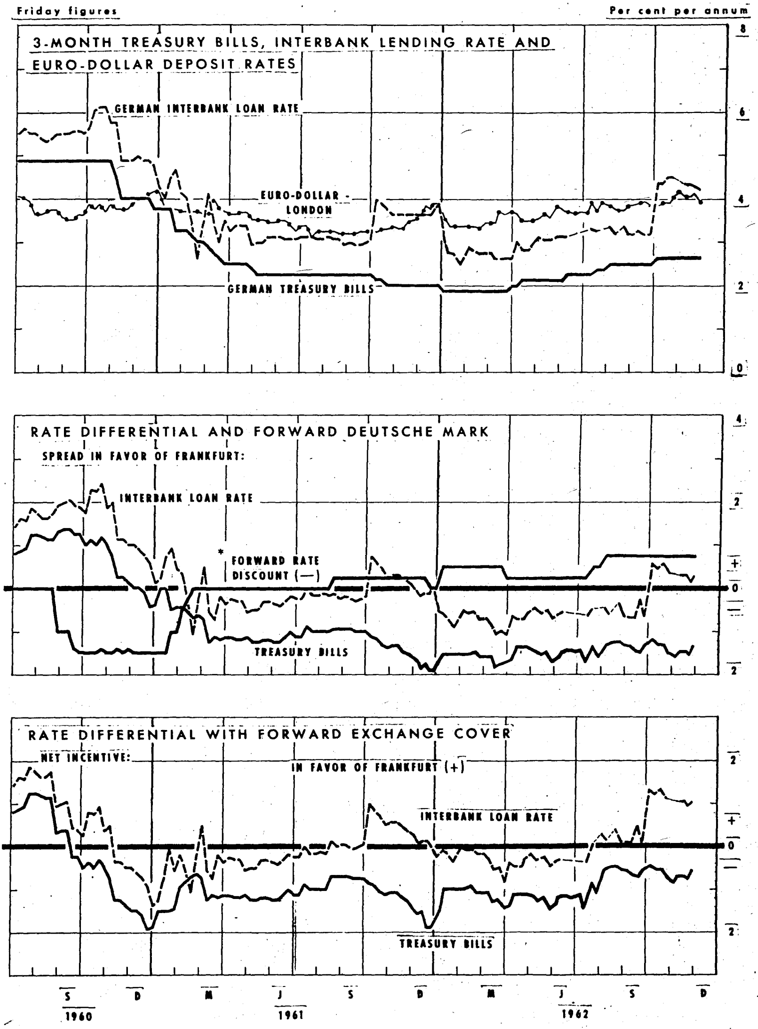


Chart 3

INTEREST ARBITRAGE FOR GERMAN COMMERCIAL BANKS



Note: Special forward rate available to German commercial banks.

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Chart 4

INTEREST ARBITRAGE, FRANKFURT / LONDON

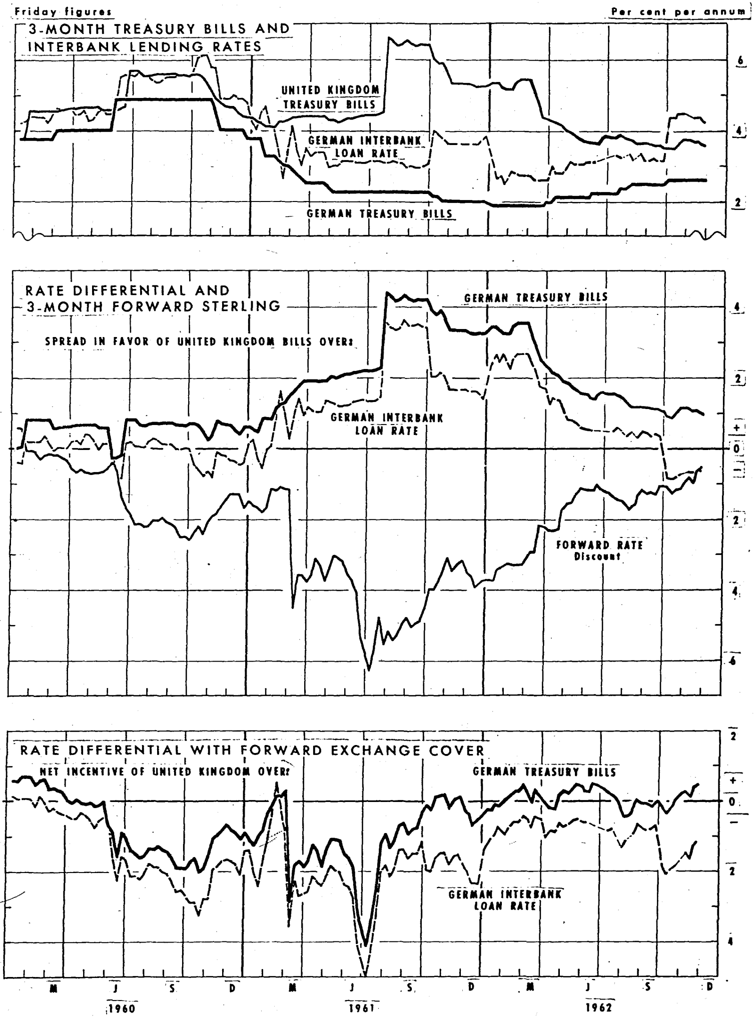
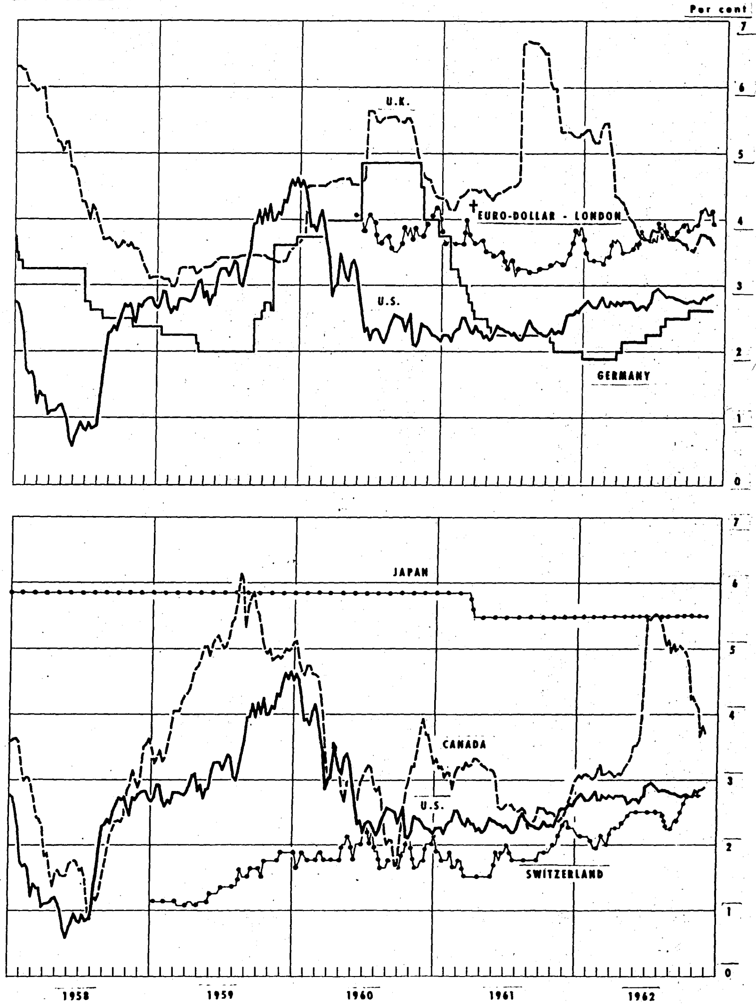


Chart 5

SHORT-TERM INTEREST RATES *



* 3-month treasury bill rates for all countries except Japan (3-month interbank deposit rate) 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

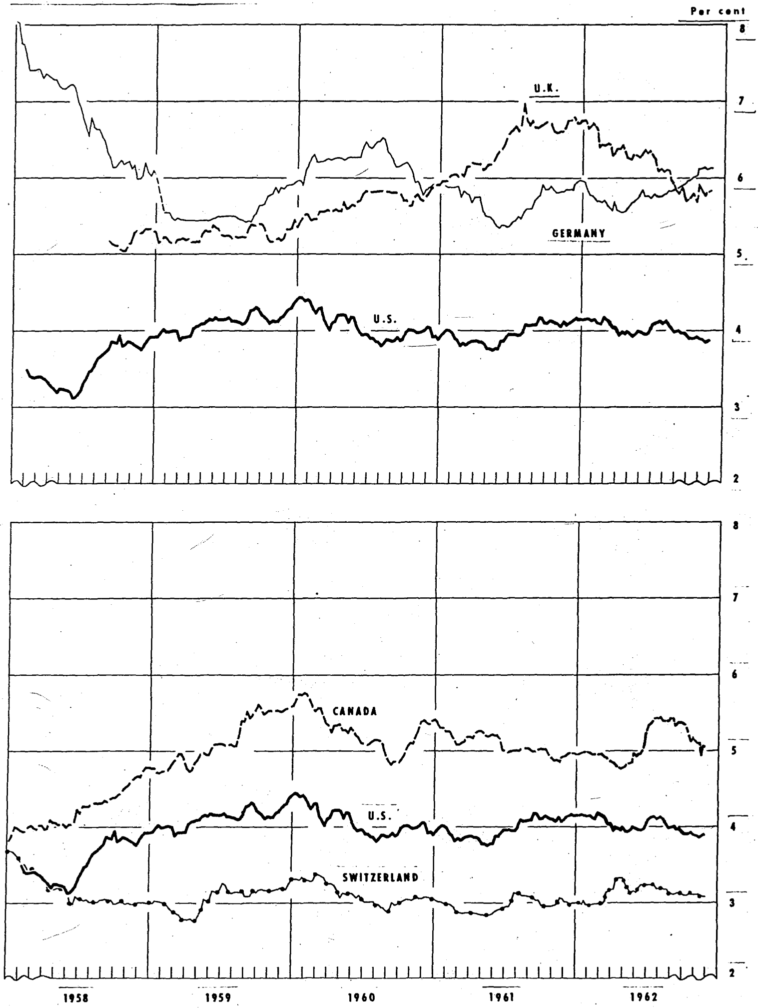
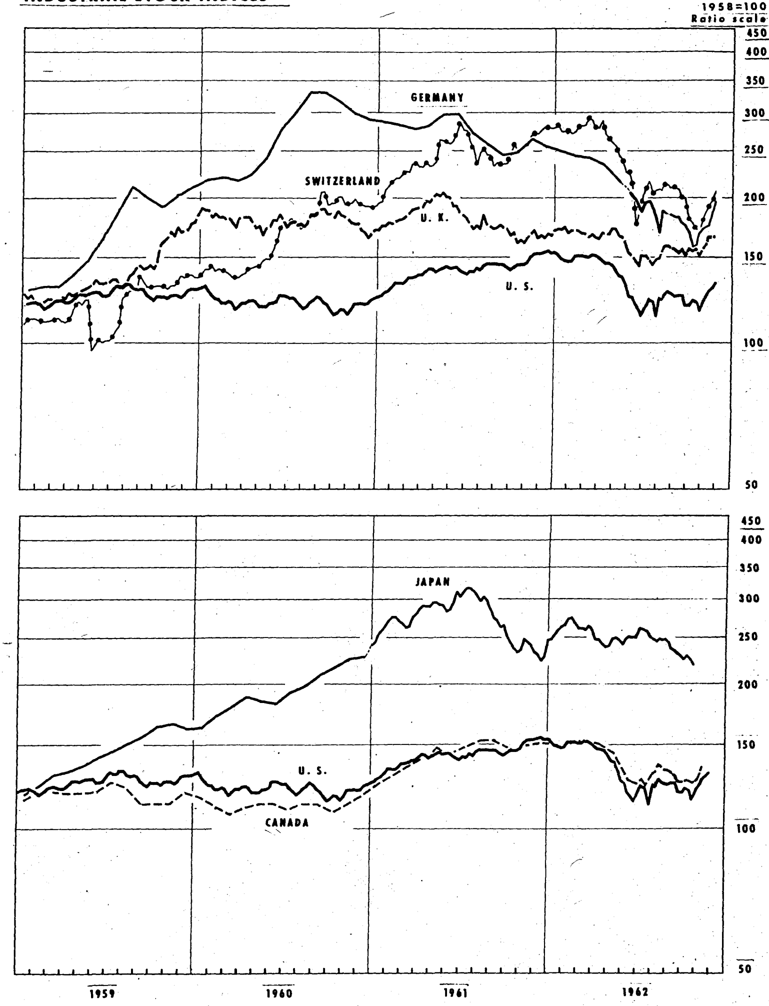


Chart 7

INDUSTRIAL STOCK INDICES*



* Note: Japan: Index of all stocks traded on Tokyo exchange.

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Chart 8

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

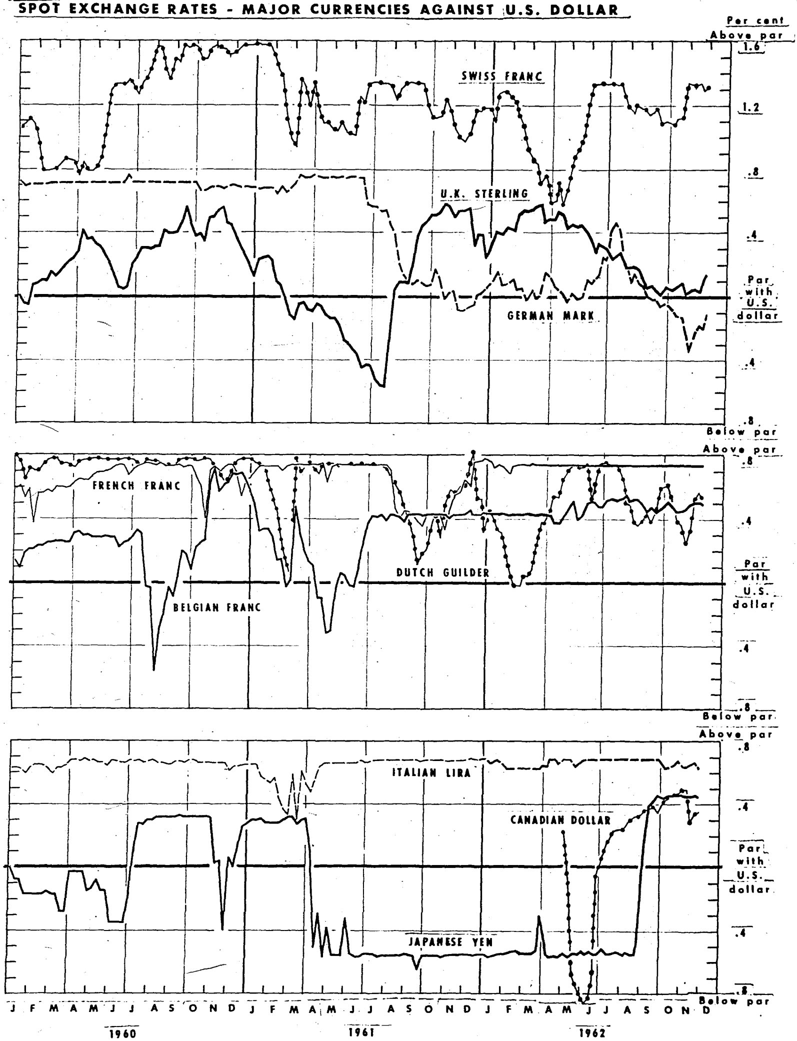

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Chart 9

3-MONTH FORWARD EXCHANGE RATES