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Article

Price Fluctuations of Japanese Foreign Bonds in the New York Stock Exchange during the 1930s

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Abstract

In the study of Japanese economic history, foreign bond issuance in the 1920s has been linked to the trends of specie holdings abroad. Furthermore, In the study of Japanese political and diplomatic history, the issuance of the series of US dollar–denominated bonds has been regarded as one of the economic factors leading to the stability of US–Japan relations under the Washington System. The above–mentioned research focuses on the process of Japanese foreign bond issuance. However, both the primary and secondary markets exist in capital markets. In this study, we review the trends in Japanese foreign bond prices at the New York Stock Exchange from 1931 to 1939, and analyze economic and political factors of these trends. Previous studies have discussed the relationship between Wall Street and the Far East mainly up to 1931 as they focused on the process of Japanese foreign bond issuance. However, this study aims at discussing the materials up to 1939, focusing on the secondary market of Japanese foreign bonds. Even after 1932 when Japanese foreign bonds lost support in Wall Street's primary market, they were still traded in the secondary market. Prices rebounded despite a temporary dip. From the discussion in this study, we can conclude that it was around August 1937, with the outbreak of the Battle of Shanghai, that Japanese foreign bonds lost support in the secondary market and completely lost credibility in Wall Street.

Introduction

Ceased to issue in 1913, Japanese foreign currency–denominated bond (foreign bond) issuance was rebooted in 1923 with the US dollar–denominated bonds of the Oriental Development Company (ODC). By 1931, there were four sovereign bond issuances ($221M, £37.5M); three municipal bond issuances ($40.38M, £6M); and 20 corporate bond issuances

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($274.2M, £13.9M). The 27 issuances totaled $535.58M, £57.4M.[1] Foreign bonds were exclusively issued by the electric power companies, semi-governmental special companies and banks. Among the 16 foreign bonds issuances of the electric power companies, 11 were in the US dollar. In the US of the 1920s, it was apparent that foreign bonds were increasingly popularizing among buyers. Overall speaking, Japan's US dollar-denominated bonds were equally well received by the public, and sales were said to have been good.[2]

In the study of Japanese economic history, foreign bond issuance in the 1920s as described above has been linked to the trends of specie holdings abroad. In other words, Japan had continually adopted a policy of selling specie holdings abroad for balancing the current account deficit and neutralizing the domestic economy from the rest of the world. Consequently, the Japanese economy developed a framework, in which foreign bond issuance was decided in relation to the residual overseas specie holdings.[3] The negotiations of South Manchuria Railway Co.'s and ODC's US dollar-denominated bond issuance were embedded with political and diplomatic opportunities for Japan, to maintain special interests in Manchuria and Inner Mongolia while falling in line with the new Four-Power Consortium. In the study of Japanese political and diplomatic history, the issuance of the series of US dollar-denominated bonds has been regarded as one of the economic factors leading to the stability of US-Japan relations under the Washington System, albeit the US State Department's objections to the issuance.[4] In particular, focus has been put upon Thomas W. Lamont, the partner of J. P. Morgan & Co., who underwrote the issuances of Japanese dollar-denominated bonds, such as Japanese Government Bonds (JGB) 6.5% ($150M) issued in 1924, Yokohama Municipal Bonds 6% ($19.74M) issued in 1926, Tokyo Municipal Bonds 5.5% ($20.64M) issued in 1927, and JGB 5.5% ($71M) issued in 1930. During the period between January–March 1932, events such as the Shanghai Incident, and the assassinations of Junnosuke Inoue and Takuma Dan, led to the loss of Lamont's confidence in Japan, causing Wall Street to "exit

1) Industrial Bank of Japan, Foreign Affairs Dept. *Nihon Gaisai Shōshi* (*Short History of Japanese Foreign Bonds*), 1948, pp.59–62.

2) Takeo Kikkawa, *Nihon denryokugyō no hatten to Matsunaga Yasuzaemon* (*The Role of Matsunaga Yasuzaemon in the Development of Japan's Electric Power Industry*), Nagoya Daigaku Shuppankai, 1995, pp.140–142.

3) Masanao Itō, *Nihon no Taigai Kinyū to Kinyū Seisaku* (*External finance and financial policy of Japan*), Nagoya Daigaku Shuppankai, 1989, p.157.

4) Taichirō Mitani, *Wall Street to Manmō* (*Wall Street, Manchuria and Mongolia*). Hosoya Chihiro and Saitō Makoto (eds.), *Washington Taisei to Nichi-Bei Kankei* (*Washington System and Japan-US Relations*), University of Tokyo Press, 1978 (Later included as Chapter 5 in Taichirō Mitani, *Wall Street to Kyokutō* (*Wall Street and the Far East*), University of Tokyo Press, 2009).

from the Far East."[5] Indeed, the Japanese issuance of US dollar-denominated bonds became impossible after 1932.[6]

The above-mentioned research focuses on the process of foreign bond issuance. However, both the primary and secondary markets exist in capital markets. There were 14 foreign bond issuances by the five bic electric power companies (Tokyo Electric Light Co. Great Consolidated Electric Power Co., Tōhō Electric Power Co., Nippon Electric Power Co. and Ujigawa Electric Power Co.).[7] The five companies used the funds obtained through foreign bond issuance for capital investment, redemption of domestic bonds, and repayment of debts during the period 1923-26, and redemption of foreign bonds and repayment of debts during the period 1927-31.[8] After the 1931 renewal on gold export embargo, the respective companies actively repurchased and redeemed their own foreign bonds as a measure against foreign exchange loss.[9] The electric power companies conducted the repurchase and redemption of their own foreign bonds in the secondary market for Japanese foreign bonds, which operated throughout the 1930s. In this study, we review the trends in Japanese foreign bond prices at the New York Stock Exchange (NYSE) from 1931 to 1939, and analyze economic and political factors of these trends. Clearly, the environment surrounding Wall Street varied greatly between the 1920s and 1930s. The Banking Act of 1933 (Glass-Steagall Act) prohibited the joint operation of commercial and investment banking,[10] while the Securities Exchange Act of 1934 added restrictions on trading in the secondary securities market. In search of new fund management schemes, major commercial banks launched medium-term lending called term loans, and among the commercial banks a coordinated system of funding was developed.[11] Consequently, the secondary securities market was "narrowed

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5) Taichirō Mitani, "*Wall Street to Kyokutō* (*Wall Street and the Far East*)," Chūō Kōron September 1975. (Later included as Chapter 4 in Mitani, *Wall Street to Kyokutō*).

6) Susie J. Pak, *Gentlemen Bankers: the World of J. P. Morgan,* Harvard University Press, 2013, pp.188-189.

7) Kikkawa, *Nihon denryokugyō no hatten to Matsunaga Yasuzaemon,* pp.104-105.

8) *Ibid.,* p.109.

9) *Ibid.*, pp.130-134, 329-334.

10) J. P. Morgan & Co. decided to focus on commercial banking operations, and as a result, its three partners, and two partners from Drexel & Co. quit their respective firms to start the investment bank, Morgan Stanley & Co. (Junko Nishikawa and Kazuo Matsui, *America Kinyūshi: Kenkoku kara* 1980 *Nendai Made* (*Financial history of US : from Founding Nation era to 1980's*), Yūhikaku Publishing, 1989, pp.186-187).

11) Nishikawa and Matsui, *America Kinyūshi: Kenkoku kara 1980 Nendai Made*, pp.202-218.

down".[12] And so was the secondary market for Japanese foreign bonds. It was said that a small number of transactions triggered intense price movements.[13] Previous studies have discussed the relationship between Wall Street and the Far East mainly up to 1931 as they focused on the process of foreign bond issuance. However, this study aims at discussing the materials up to 1939, focusing on the secondary market of foreign bonds.

This study analyzes the Japanese foreign bonds as follows: Tokyo Municipal Bonds issued in 1927 ($20.64M, issue price $89.5, yield-to-maturity 6.49%, maturity 34 years), ODC series 57 corporate bonds issued in 1928 ($19.9M, issue price $90, yield-to-maturity 6.63%, maturity 30 years), JGBs issued in 1930 ($71M, issue price $90, yield-to-maturity 6.20%, maturity 35 years), and Taiwan Electric Power Company (TEP) corporate bonds issued in 1931 ($22.8M, issue price $93.5, yield-to-maturity 5.92%, maturity 25 years).[14] All of these bonds had a face value of $100 and a coupon rate of 5.5%. The Tokyo Municipal Bonds, ODC corporate bonds, and TEP corporate bonds were guaranteed by the Japanese government. The underwriters of the bonds included: J. P. Morgan & Co., Kuhn Loeb & Co., National City & Co., First National Bank of N.Y., and Yokohama Specie Bank for the JGBs and Tokyo Municipal Bonds. The same underwriting group excluded the Yokohama Specie Bank for the TEP corporate bonds. For the ODC corporate bonds, National City & Co. and National City Bank of N.Y. underwrote.

1. Abandonment of the Gold Standard in the UK and Japan and the Sharp Decline in Yen Exchange Rate

The British abandonment of the gold standard on September 21, 1931 brought about a sharp fall in bond prices at the NYSE.[15] Triggered by the German bank crisis, the withdraw-

12) Merwin H. Waterman, *Investment Banking Functions: Their Evolution and Adaptation to Business Finance*, University of Michigan, 1958 (Kaichi Shimura (trans.), *America no Shihon Shijō: Sono Rekishi to Toushi Ginkō-gyō* (*Capital Markets in America: Its History and Investment Banking Business*), Tōyō Keizai, 1965, p.90).

13) "Waga Gaikō Kankei no Barometer (Barometer of Our Diplomatic Relations)," *Chūgai Shōgyō Shinpō*, October 14, 1941.

14) For the citation in this paragraph, see Itō, *Nihon no Taigai Kinyū to Kinyū Seisaku*, Table 214 on pp.148-149, Table 215 on pp.152-153. Mark Metzler, *Lever of Empire: The International Gold Standard and the Crisis of Liberalism in Prewar Japan*, University of California Press, 2006, Table 4 on pp.150-152.

15) For the citation in this paragraph, see Mitsuhiko Takumi, *Sekai Daikyōkō: 1929 Kyōkō no Katei to Genin* (*The Great Global Crisis: Stages and Causes of the 1929 Depression*), Ochanomizushobō, 1994, pp.642-649, 659-673. Charles P. Kindleberger, *The world in depression 1929-1939*, University

Table 1 The Official Discount Rate of the Federal Reserve Bank of New York

1930/12/23	2.0
1931/5/8	1.5
1931/10/9	2.5
1931/10/16	3.5
1932/2/25	3.0
1932/6/23	2.5
1933/3/2	3.5
1933/4/2	3.0
1933/5/25	2.5
1933/10/19	2.0
1934/2/1	1.5
1937/8/26	1.0

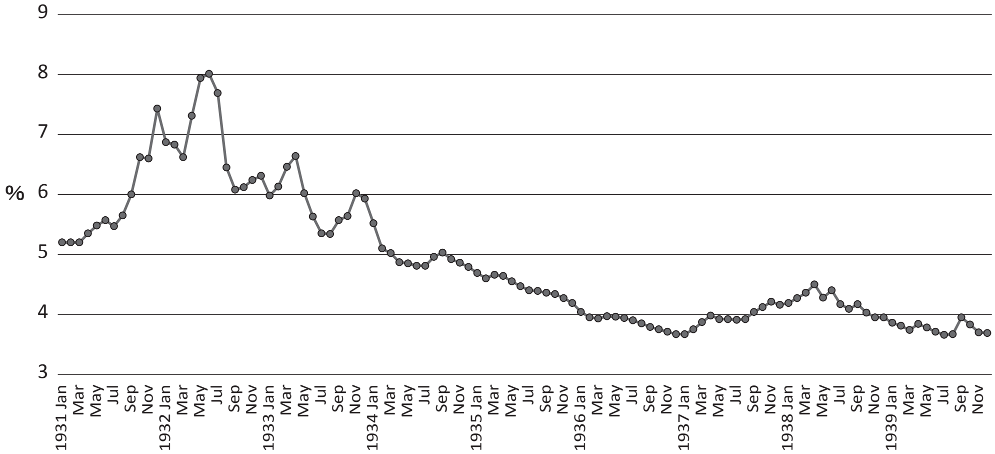
Source: *Keizai Nenkan* (*Economic Yearbook*), vol. 21, Tōyō Keizai, 1937, p.91.

al of enormous short-term capital (a run on the sterling) and intensification of outflow of gold caused Britain to abandon the gold standard, and resulted in a sharp decline in the sterling's exchange rate. Moreover, this sparked a large withdrawal of short-term capital in the United States and various European countries with the fear that a dollar plunge may occur next. This caused a large outflow of gold from the United States through October. As shown in **Table 1**, the US Federal Reserve Board raised interest rates twice in October to deal with the situation, leading to an increase in corporate bond yields (i. e., fall in bond prices) as can be seen in **Figure 1**. The decline in foreign bond prices was particularly intense. As banks saw their assets greatly depreciated, they sold large quantities of securities to guarantee liquidity, spurring a further decline in bond prices.

After the first-rate companies and banks mentioned above had underwritten Japanese foreign bonds, they then sold the bonds through securities firms on the premise that the buyers would possess them for the long term.[16] However, the Mukden Incident of September

of California Press, 1973 (Akihiko Ishizaki and Ichirō Kimura (trans.), *Daifukyōka no sekai 1929–1939 revised and enlarged edition*, Iwanami Shoten, 2009, Chapter 7).

16) *Daiikkai Gaika Shori Iinkai Kaigi Gijiroku* (*Minutes of the 1st Meeting of the Foreign Currency Processing Committee*), May 26, 1943, remarks by Takeo Haraguchi, committee member and Director of Foreign Capital Div, Ministry of Finance (Japan Center for Asian Historical Records, Ref. B08060373800, Matters Related to Influences from the Economy, Trade, and Industry during the Greater East Asia War, Matters related to the economy and finance, domestic and foreign bonds in



Source: *Keizai Nenkan* (*Economic Yearbook*), Tōyō keizai, 1939, p.462, 1940, p.422.

Figure 1 Trends of US's bond yields (120 brands average, investigation by the Moody's)

18, 1931 shook up the prices of Japanese foreign bonds. JGB prices in September 1931 fell from a high of $97 to a low of $86, while ODC corporate bonds fell from $93.5 to $79, and the TEP corporate bonds fell from $94 to $78.[17] Subsequently, Japanese foreign bond prices plummeted in October and November as shown in **Figure 2**. In response to this plunge, US banks initially had hopeful views that Japan's external credibility would be maintained as long as Japan continued with the gold standard.[18] However, in November, the Seiyūkai started to pressure the Wakatsuki Cabinet (Constitutional Democratic Party) to immediately renew the embargo on gold export. In the foreign exchange market, there was speculative "dollar purchase," anticipating Japan's renewed prohibition of gold export. In the context of this "dollar purchase" that anticipated the yen's decline, it was believed that investors targeted at Japanese foreign bonds for investment as the drop in prices made yields attractive.[19] The contemporary newspapers reported that the amount of domestic investment in Japanese foreign bonds reached 300 million yen during the period between Britain's abandonment of the gold standard and Japan's renewal on gold export embargo. They also reported that the bondholders included no small number of retail investors.[20]

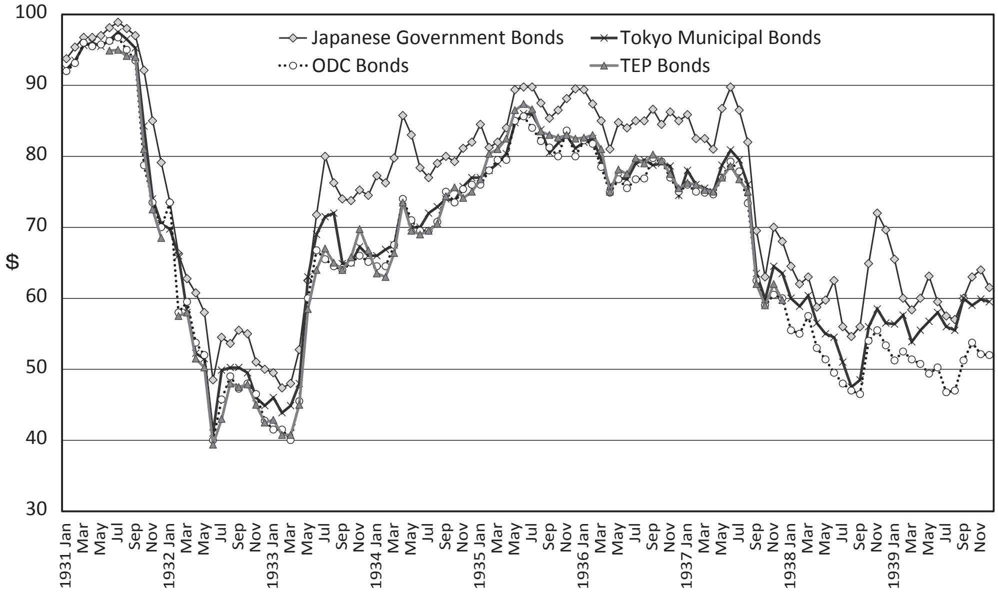
the Period Including the Second Sino-Japanese War and World War II, vol. 1, E-0-0-0-3_1_8_001, Diplomatic Archives of the Ministry of Foreign Affairs of Japan).

17) *Keizai Nenkan* (*Economic Yearbook*), vol. 16, Tōyō Keizai, 1932, p.139.

18) "Honpousai geraku wo beiginkouka ha keishi (US Bankers Disregard Price Declines in Japanese Bonds)," *Ōsaka Mainichi Shinbun,* October 21, 1931.

19) "Dollar temochisuji (Holders of the US Dollar)," *Ōsaka Mainichi Shinbun,* February 10, 1932.

20) "Gaikahousai no rikui uri ousei (Vigorous Profit Taking in Japanese Foreign Currency-Denomi-



Source: *Keizai Nenkan* (*Economic Yearbook*), Tōyō keizai, vol. 16–22, 1932–1938.

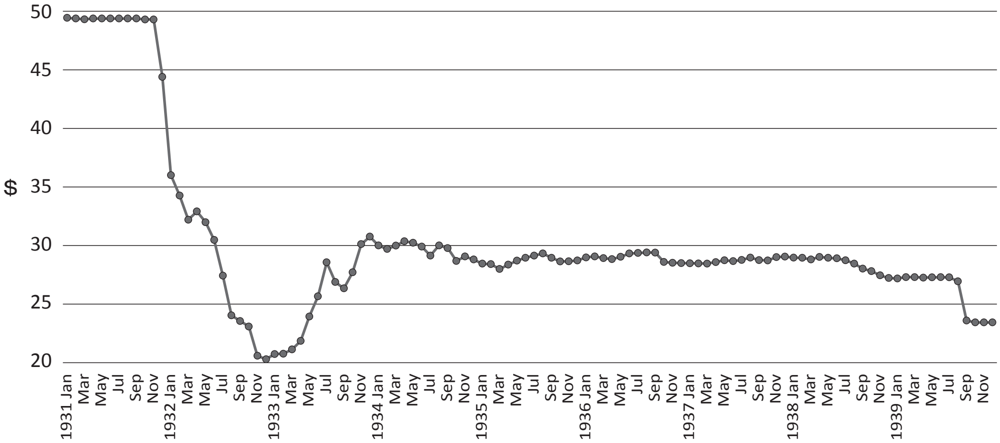
Figure 2 Fructuation in Japanese foreign bond price on the NYSE (monthly highest price)

In December 1931, the Wakatsuki Cabinet of the Constitutional Democratic Party was forced to step down, being replaced by the Seiyūkai's Inukai Cabinet. The Minister of Finance, Korekiyo Takahashi, immediately took measures to renew the prohibition of gold export. The so-called Takahashi financial policy, an aggressive approach entailing the reduction of interest rates accompanied by an expansion of the military, triggered a recovery in the economy. The decline in the yen caused by the renewed gold export embargo brought about a stalling of imports and accelerated exports. Thus, from late 1932, the Japanese economy headed towards recovery.

Finance Minister Takahashi took a laissez-faire approach to the fall in the yen. As a result, the yen's exchange rate crashed as shown in Figure 3. We can categorize the fall in the yen's exchange rate into five stages during the period from the renewal of gold export embargo to the end of 1932.[21] The first stage (renewal of gold export embargo – January

nated Bonds)," *Chūgai Shōgyō Shinpō*, February 4, 1932.

21) Ryōichi Miwa, "*Takahashi zaiseiki no keizai seisaku* (*Economic Policy in the Takahashi Era*)," University of Tokyo, Institute of Social Science (ed.), *Fascism-ki no Kokka to Shakai 2: Senji Nihon Keizai* (*State and Scoiety during Periods of Fascism Part 2: Japanese Wartime Economy*), University of Tokyo Press, 1979 (Later included as Chapter 9 in Ryōichi Miwa, *Senkan-ki Nihon no Keizai Seisakushi-teki Kenkyū* (*Historical Study on Japanese Economic Policy in the Interwar Period*), University of Tokyo Press, 2003).



Source: *Keizai Nenkan* (*Economic Yearbook*), Tōyō keizai, 1932, 1933, 1938, 1940.

Figure 3 The Dollar-Yen Exchang Rate (The Forward Sales Price on the Tokyo Market for ¥100)

1932) is the fall to the $35 level vs. 100 yen. The second stage (February–May) is the drop to the $32–33 level, triggered by the Shanghai Incident. The third stage (June–July) is the further decrease to the $27 level, triggered by the supplementary budget and cutting of interest rates. The fourth stage (August–mid–October) is the fall to the $23 level due to the additional cutting of interest rates and the budget for temporary relief works. The fifth stage (late October–December) is the shrinkage to the $20–21 level, triggered by reports that the budget size was informally decided.

The intensification of the yen's depreciation against the dollar spurred by the renewal of gold export embargo generated foreign exchange losses for bond issuers at the payment of principal and interest. This further depressed the prices of Japanese foreign bonds, which had already been in a downward trend since September 1931. In December of the year, the prices of JGBs plunged from a high of $79.125 to a low of $68.125. Similarly, ODC corporate bonds fell sharply from $70 to $54, and TEP corporate bonds from $68.5 to $54.[22] As shown in **Figure 1**, US corporate bond yields was in a downward trend (i. e., corporate bond prices was moving upward) since January 1932. This trend continued through March, caused by an interest rate cut in February 1932 (**Table 1**). However, as shown in **Figure 2**, the prices of Japanese foreign bonds entered a further downward trend. This shrinkage was affected by the loss of Japan's external credibility due to the Shanghai Incident and the further decline in the yen's exchange rate. Contemporary newspapers reported that foreign investors were

22) *Keizai Nenkan* (*Economic Yearbook*), vol. 16, Tōyō Keizai, 1932, p.139.

selling Japanese foreign bonds because of the Shanghai Incident, while domestic retail investors started reaping profit on bonds that they had purchased during the speculative "dollar purchase" phase.[23] From February 1932, the decline in the yen's exchange rate entered the above-mentioned second stage, augmenting the foreign exchange gains of Japanese foreign bonds purchased prior to the renewal of gold export embargo. Therefore, it was believed that many investors who had purchased Japanese foreign bonds during the "dollar purchase" turned to sell their holdings. In addition, a large-scale purchase operation was conducted by the Federal Reserve Board from April to June of the year. Thus, the prices of the "first-rate bonds" (such as US sovereign bonds) rose and stabilized, while those of the "second-rate bonds" continued to drop.[24] The US corporate bond yields rebounded after April (**Figure 1**), while prices of the Japanese foreign bonds continued to be weak, including ODC corporate bonds and TEP corporate bonds, which had temporarily halted their slide in April (**Figure 2**).

2. Loss of External Trust and Inflow of Japanese Foreign Bonds

It has been said that the May 15 Incident of 1932 caused further depression of the prices of Japanese foreign bonds. In fact, in May of the year, JGB prices plummeted from a high of $58 to a low of $45.5, ODC corporate bonds from $52 to $41, TEP corporate bonds from $50.25 to $37.[25] However, when we view the prices of Japanese foreign bonds before and after the incident (May 14 and 16) in **Table 2**, there are relatively sharp declines in Tokyo Municipal Bonds and TEP corporate bonds, plunging 5.4% and 5.5% respectively. Meanwhile, the JGB and ODC corporate bonds only had relatively small declines, at 3.4% and 3.5% respectively. In addition, the prices of JGB and TEP corporate bonds recovered on the 17th. Indeed, the May 15 Incident had depressed prices of Japanese foreign bonds, but it is hard to conclude that the incident had a decisive influence on the downward trend of bond prices. In fact, declines in Japanese foreign bonds were enlarged when the Cabinet under PM Makoto Saitō was formed around May 26.[26] Contemporary newspapers pointed out that this was possibly resulted from the selling by foreign investors who were concerned with the

23) "Gaikahousai no rikui uri ousei (Vigorous Profit Taking in Japanese Foreign Currency-Denominated Bonds)," *Chūgai Shōgyō Shinpō*, February 4, 1932.

24) Takumi, *Sekai Daikyōkō: 1929 Kyōkō no Katei to Genin,* p.712.

25) *Keizai Nenkan* (*Economic Yearbook*), vol. 17, Tōyō Keizai, 1933, p.143.

26) "Taigaikou kenen de nage uri (Foreigners Cut Losses on Fears of Rising Nationalism)," *Ōsaka Asahi Shimbun,* May 28, 1932.

Table 2 Prices of Japanese Foreign Bonds in 1932 May ($)

	JGBs	Tokyo Municipal Bonds	ODC Bonds	TEP Bonds
14-May	58	51	50	50 1/4
16-May	56	48 1/4	48 1/4	47 1/2
17-May	57	48	—	48 1/4

Source: *Tōyō Keizai Shinpō*, May 21, 1932, p.1722.

new cabinet's hard line foreign policy regarding the Manchurian problem.[27] In addition, the newspapers indicated that the volume of selling was likely large enough to cause the large plunge in price, as the secondary markets for Japanese foreign bonds was narrow in nature.[28] However, this reveals the decline in Japan's external creditability. For these reasons, we can say that the May 15 Incident marked the end of the political party participation in the cabinet and strongly depressed Japanese foreign bond prices.

In addition, the US economy in May and June 1932 encountered a financial crisis as had been similarly seen in September and October 1931, the intensification of outflow of gold and a sharp rise in bank failures, albeit the adoption of large-scale monetary easing measures.[29] As shown in **Figure 1**, yields of US corporate bonds, which had been moving upward since April, maintained this trend until June. The plunge in Japanese foreign bonds through June was influenced by not only general trends in the US securities market. It was also resulted from the May 15 Incident and the fact that the decline in the yen's exchange rate had entered into the above-mentioned third stage in June.

The US corporate bond yields declined rapidly in August (**Figure 1**), resulted from the lowering of US interest rates in June (**Table 1**). The Japanese foreign bond prices also started to rise in July, and the downward trend appeared to be lessened, despite the decline in the yen's exchange rate entering into the above-mentioned fourth stage. After July 1932, there was a reduction in the US bank failures and halting of gold outflow. The economy was temporarily revived through October.[30] From January to February 1933, bank withdrawals increased (bank run), and several banks were temporarily closed in February.[31] Although the US corporate bond yields rose from September to December 1932, fluctuations were

27) *Ibid*.
28) *Ibid*.
29) Takumi, *Sekai Daikyōkō: 1929 Kyōkō no Katei to Genin*, p.706.
30) *Ibid*., p.718.
31) *Ibid*., pp.733-738.

more stable than the previous period and hovered over the 6% range through March 1933 (**Figure 1**). However, the prices of Japanese foreign bonds continued to decline significantly, hitting the bottom in March 1933, which had been seen in June 1932 (**Figure 2**). We should regard the plunge in Japanese foreign bond prices during this period as being related to the weakening of Japan's external creditability. According to contemporary newspapers, the prices of Japanese foreign bonds declined as Japan announced its withdrawal from the League of Nations in mid-February 1933.[32)]

Clearly, the decline in the yen's exchange rate to the above-mentioned fifth stage in late October 1932 would have influenced the drop in Japanese foreign bond prices. Foreign bond issuers constantly suffered increased exchange rate losses during the period of decline in the yen's exchange rate since the end of 1931. In response, they were forced to take measures, such as repurchase and redemption. Japanese foreign bonds, which had been flowing into Japan since the "dollar purchase" trend, became more appealing due to the high yields during the low-interest rate policies of the (Minister of Finance) Takahashi era. It is inferred that this helped the increase of capital inflow even before the enforcement of the Capital Flight Prevention Laws. To begin with, Japanese foreign bond prices were lower in the domestic market than overseas. Despite increases in buyers of Japanese foreign bonds in the domestic market, their trade volume was small. It appears that securities firms tried to import Japanese foreign bonds in large volumes ahead of the enforcement of the Capital Flight Prevention Laws.[33)] Contemporary media reported that at the end of March 1932, foreign currency-denominated securities in Japan amounted to 793M yen, of which 593M yen were Japanese foreign bonds.[34)] It was also said that the buyers of Japanese foreign bonds in Japan were mainly individual investors,[35)] while foreign banks organized foreign exchange remittances for these purchases.[36)] It was said that about 60% of foreign bonds issued by electric power companies had flowed into Japan by the end of the first half of 1932,[37)] and it

32) "Naigai tomo gaikasai sanraku (Plunge in Foreign Currency-Denominated Bonds, Domestic and Foreign)," *Ōsaka Asahi Shimbun,* February 16, 1933.

33) "Kawase kanri no hamon (Ripple Effects from Forex Controls)," *Ōsaka Asahi Shimbun,* May 14, 1932.

34) "Kikaitsuke no gaikashouken ni nichigin ga stamp wo osu (BOJ Signs Off on Purchased Foreign-Denominated Securities)," *Kōbe Yūshin Nippō,* June 23, 1932.

35) "Kojintoushika no gaikasaigai gekizousu (Sharp Rise in Purchases of Foreign-Denominated Bonds by Individual Investors)," *Ōsaka Mainichi Shinbun,* May 14, 1932.

36) "Kaigaitouhishikin no toriatsukai wo kyohi suru (Denying Overseas Capital Flight Transactions)," *Chūgai Shōgyō Shinpō,* May 20, 1932.

37) *Tōhō Denryoku-shi* (*History of Tōhō Electric Power Co.*), 1962, p.175.

was estimated that by October of the same year, half of the Japanese foreign bonds in circulation had flowed into Japan.[38] Electric power companies at first started to repurchase their own foreign bonds that flowed into Japan. However, the domestic market prices of Japanese foreign bonds escalated with the enforcement of the Capital Flight Prevention Laws in July 1932. For example, the prices of US dollar-denominated 6.5% JGBs between June to November 1932 moved from $58.25 to $63.25 in New York, while in the Tokyo market, it rallied from 215 yen (June), 233.50 yen (July), 254.50 yen (August), 265 yen (September), 280.25 yen (October), to 309.50 yen (November).[39] Likewise, foreign bonds issued by electric power companies saw increases in price in the domestic market. The electric power companies repurchased their own foreign bonds abroad after receiving permission from the government in accordance with the Capital Flight Prevention Laws.[40]

3. US Abandonment of the Gold Standard and Stabilization of the Yen Exchange Rate

The situation changed drastically when the United States also abandoned the gold standard in April 1933. The US Federal Reserve Board cut interest rates in April and May of that year (**Table 1**), and corporate bond yields declined (bond prices increased) from May to August (**Figure 1**). In addition, the rise in the dollar-yen exchange rate (**Figure 3**) and abolishment of gold clause mitigated the Japanese foreign bond's default risk, and thus the prices of these bonds rose sharply through July (**Figure 2**). The monthly highs in JGB prices reversed losses rapidly in 1933, from $48 (March) to $52.75 (April), $62.50 (May), $71.75 (June), and $80 (July). The prices of ODC corporate bonds also rose sharply in 1933, from $40 (March) to $45.50 (April), $60 (May), and $66.75 (June), as did TEP corporate bonds, from $40.75 (March) and $45 (April), $58.50 (May), to $64 (June).

Although the dollar depreciation continued until late July, the trend temporarily turned upward, which led to the announcement of the gold purchase plan in late October. The announcement of this program caused the dollar to drop once again.[41] The rise in the yen exchange rate also halted in July 1933 (**Figure 3**), and the rise in monthly high prices for

38) Comments by Takeo Kurusu of the Industrial Bank of Japan (IBJ) at the discussion forum on countermeasures for foreign bonds issued by electric power companies at Tōyō Keizai on October 1932 (*Tokyo Keizai Shinpō,* October 29, 1932, p.397).

39) *Keizai Nenkan* (*Economic Yearbook*), vol. 17, Tōyō Keizai, FY 1933, p.143.

40) Kikkawa, *Nihon denryokugyō no hatten to Matsunaga Yasuzaemon*, p.131.

41) Takumi, *Sekai Daikyōkō: 1929 Kyōkō no Katei to Genin,* pp.770–774.

Japanese foreign bonds peaked in July (**Figure 2**). Subsequently, the United States enacted the Gold Reserve Act of 1934 at the end of January,[42] and the yen exchange rate rose slightly and stabilized. The yen exchange rate traded in the $26–$28 range after August 1933, resulted from the Foreign Exchange Control Law enacted in May 1933. The rate stabilized at the $30 level after November 1933 (**Figure 3**). This move in the yen exchange rate signified the diminishing effects from foreign bond repurchases for electric power companies. The foreign bonds repurchased by TEP with government approval reached $2.68M by the end of the first half of 1933 and $4.88M by the end of the second half of 1933 out of the total issuance face value of $22.8M. However, the buyback slowed down since the beginning of 1934.[43]

Having been stagnant since April 1933, the US economy started to boom from October 1934 on. It continued through May 1937. Prices of Japanese foreign bonds, which had been stabilized since the summer of 1933, also turned to a continuous upward trend. The prices of Tokyo Municipal bonds, ODC corporate bonds, and TEP corporate bond prices rose rapidly through the summer of 1935, narrowing their gap with JGB prices (**Figure 2**). From the fall of 1935, prices of Japanese foreign bonds began to decrease but without sharp fall. Even though the February 26 Incident broke out, prices of the Japanese foreign bonds plunged for several days but there was no significant collapse in price.[44] In the United States, the reserve ratio was raised in March and May 1937, elevating corporate bond yields,[45] but the prices of Japanese foreign bonds remained stable. It was presumed that an influential buyer existed behind the stability of the Japanese foreign bond prices. The contemporary media speculated that foreign investors were buying up Japanese foreign bonds, as Japanese investors had difficulty in purchasing these bonds in overseas markets under the Foreign Exchange Control Law.[46]

After the enactment of the Capital Flight Prevention Laws in July 1932, there appears to be a decrease in the volume of Japanese foreign bonds that flowed into Japan. However, in the Japanese domestic market, there was active buying of these high-yielding bonds from financial institutions struggling in their fund management strategies due to declining interest

42) *Ibid.,* pp.774–775.

43) Teruhiro Minato, *Kindai Taiwan no Denryoku Sangyō* (*Power Industry in Modern Taiwan*), Ochanomizushobō, 2011, pp.100–101.

44) Nomura Securities, *Gaika Housai Narabini Gaikoku Kawase Sōba Nichibetsu Zuhyō: Shōwa 11 nen-chū* (*Daily Chart of Foreign Bonds, JGB, and Foreign Exchange Markets in 1936*), 1937.

45) Takumi, *Sekai Daikyōkō: 1929 Kyōkō no Katei to Genin,* pp.802–803.

46) "Kousai no minshūka ni tourokuseido wo katsuyou (Utilizing the Registration System for the Popularization of Public Debt)," *Ōsaka Mainichi Shinbun,* 1935, June 22.

Table 3 Domestic Holders for the Outstanding Japanese US Dollar-denominated Bonds ($)

	Government bond	Municipal bond	Corporate bond	Total
Location in Japanese empire				
Issuers	—	2,372,000	21,380,000	23,752,000
Banks	62,505,600	7,776,000	18,815,000	89,096,600
Foreign exchange bank	34,950,300	4,912,000	11,400,000	51,262,300
Government	25,241,500	3,874,000	2,476,500	31,592,000
Deposit Department of MOF	22,005,600	2,685,600	—	24,691,200
Manchuria securities investment company	12,878,000	2,369,000	5,566,500	20,813,500
Public corporations	10,155,800	204,000	883,000	11,242,800
Life insurance companies	2,557,000	400,000	5,569,000	8,526,000
Non life insurance companies	2,162,000	—	25,000	2,187,000
Shipping companies	175,000	—	—	175,000
Trusts	6,593,300	561,000	1,369,500	8,523,800
Ordinaly companies	2,083,300	185,000	1,354,500	3,622,800
Securities companies	1,533,100	149,000	400,500	2,082,600
Personal	4,435,000	649,500	5,041,500	10,126,000
Colonial residents	203,000	2,000	62,000	267,000
Location abroad				
Japanese foreign companies	375,300	40,000	61,000	476,300
Personal	60,000	15,000	939,000	1,014,000
Total	130,957,900	18,596,500	63,943,000	213,497,400

Source: Same as Footnote 16, 49.

rates. Table 3 shows a survey taken after the beginning of war against Britain and the US. From this survey, we can see the breakdown of domestic holders of the outstanding Japanese dollar-denominated bonds: 42% banks, 5% trusts, 4% life insurance companies, and 1% non-life insurance companies, while more than half were financial institutions. We can see that life insurance companies had a large share of corporate bond holdings, and that financial institutions primarily purchased Japanese foreign bonds, mostly sovereign bonds. It was believed that financial institutions seeking high-yield assets helped to stabilize the domestic market prices of Japanese foreign bonds.[47)]

47) The prices of USD-denominated sovereign bonds were stable in the domestic market through September 1936 (Nomura Securities, *Gaika Housai Narabini Gaikoku Kawase Sōba Nichibetsu Zuhyō: Shōwa 11 nen-chū,* 1937).

4. Outbreak of the War

While the US economy entered a phase of recession in May 1937, which started to manifest in September, the prices of Japanese foreign bonds tended to move upward until June 1937, being unrelated to the US economic recession. However, despite the lowering of interest rates in August as shown in Table 1, and stable US corporate bond yields (Figure 2), the prices of Japanese foreign bonds dropped once again. Disturbed by the Marco Polo Bridge Incident in July 1937 and Shanghai's involvement in the war, investors likely deemed increased risk in Japanese foreign bonds. The bond prices decrease in August was steeper than in July: in the case of JGBs. The high was $86.5 and the low was $78 in July, while August saw a high of $82 and a low of $68. ODC corporate bonds marked a high of $77.875 and a low of $72.75 in July, and a high of $73.375 and a low of $55.25 in August. TEP corporate bonds witnessed a similar downtrend: July marked a high of $76.75 and a low of $71.625, while the margin of decrease widened in August, from a high of $75 to a low of $57. Subsequently, Japanese foreign bonds prices on the NYSE remained sluggish in 1938 and 1939, never recovering to the 1935–36 level. It is likely that most bondholders moved to sell amid the sharp fall of prices, while buyers were sidelined.

Based on the above analysis, we can say that the liquidity of Japanese foreign bonds on the NYSE diminished greatly due to the outbreak of the Second Sino-Japanese War, and dried up almost completely with the prolonging of war and intensifying conflict between Japan and the US. However, bond issuers continued to retire bonds through the secondary market. For example, ODC remitted funds to New York to partially redeem their debt, and the National City Bank purchased the ODC bonds in the secondary market. While the purchase was interrupted due to the freezing of Japanese assets in July, the repurchase was completed in October at a face value of $393,000. Shortly before the outbreak of war between Japan and the US, ODC received a telegram from the National City Bank, indicating that they would retire the bonds based on the November agreement.[48]

Even at the beginning of war against Great Britain and the US, roughly half of the

48) Addressed to the Ministry of Finance, Foreign Exchange Authority from the Oriental Development Company: "High certificate subpetition request for Redemption of 5.5% USD-denominated Series 57 bonds," December 15, 1941 (Japan Center for Asian Historical Records, Ref. B06050283500, Japanese Corporation-Related Matters, Oriental Development Company, Official document related to accounting, E97, Diplomatic Archives of the Ministry of Foreign Affairs of Japan).

Table 4　Holders for the Outstanding Japanese US Dollar-denominated Bonds ($)

	JGBs	Tokyo Municipal Bonds	ODC Bonds	TEP Bonds	Others 11	Total
Japanese	48,419,000	9,426,500	6,666,000	15,702,000	133,283,900	213,497,400
Location in Japanese empire	45,215,000	8,838,500	6,648,000	15,692,000	122,132,800	198,526,300
Issuers	—	—	—	6,528,000	14,876,000	21,404,000
Others	45,215,000	8,838,500	6,648,000	9,164,000	107,256,800	177,122,300
Location abroad	3,204,000	588,000	18,000	10,000	11,151,100	14,971,100
Foreigner	10,321,000	3,011,500	4,391,000	4,056,000	48,362,000	70,141,500
Total	58,740,000	12,438,000	11,057,000	19,758,000	181,645,900	283,638,900

Source: Same as Table 3.

Japanese foreign bonds were owned by the Japanese. For domestic bondholders and bondholders from “friendly nations,” such as Germany and Italy, interest payments were made in yen as decreed by the Foreign Exchange Control Law, at a conversion rate of $1 = 4 yen 25 sen, £1 = 16 yen 84 sen. On the other hand, for bondholders in “enemy nations,” such as the US and Britain, interest was paid into a controlled account for special assets at the aforementioned conversion rate, on the basis of the Enemy’s Property Administration Act.[49] It became impossible for the issuers to retire bonds through the operation of a sinking fund, which could ease the burden of high interest payments. However, due to the Act on Treatment of Foreign Currency-Denominated Bond enacted in March 1943, domestic-owned bonds were swapped into yen-denominated bonds, while the government assumed the debt owned by holders in “enemy nations” who were not able to re-finance. As seen in Table 4, there was large domestic ownership of Japanese dollar-denominated bonds.[50] About three-fourths were swapped into yen-denominated bonds, and a quarter was assumed by the gov-

49) *Daiikkai Gaika Shori Iinkai Kaigi Gijiroku* (*Minutes of the 1st Meeting of the Foreign Currency Processing Committee*), May 26, 1943, Explanation by Minister of Finance Okinori Kaya (Japan Center for Asian Historical Records, Ref. B08060373800, Matters Related to Influences from the Economy, Trade, and Industry during the Greater East Asia War, Matters related to the economy and finance, domestic and foreign bonds in the Period Including the Second Sino-Japanese War and World War II, vol. 1, E-0-0-0-3_1_8_001, Diplomatic Archives of the Ministry of Foreign Affairs of Japan).

50) The ownership of the outstanding Japanese GBP-denominated bonds after the outbreak of the war was about 30% Japanese, and about 70% foreigners (*Ibid*). This was directly contrasting with the ownership profile of Japanese USD-denominated bonds.

ernment. Of the Japanese foreign bonds discussed in this study, the respective outstanding portions in domestic ownership were as follows: about 82% of JGBs, about 76% of Tokyo Municipal Bonds, about 60% of ODC corporate bonds, and about 79% of TEP corporate bonds. We can infer that these were all switched into yen-denominated bonds.

Conclusion

It has been said that the political party cabinet system during Japan's inter-war period was organically tied to the international monetary system represented by the gold standard. Thus, the issuance of US dollar-denominated bonds in Japan has been regarded as a stabilizing factor in the US-Japan relations under the Washington System. In this study, we have examined the price fluctuations in the secondary market for Japanese foreign bonds.

The price fluctuation of Japanese foreign bonds on the NYSE can be classified into the following five phases. These include the period of (1) sharp decline (September 1931-June 1932), (2) bottoming (July 1932-March 1933), (3) recovery (April-July 1933), (4) stability (August 1933-June 1937), and (5) renewed contraction (July 1937-). In Phase 1, Britain's abandonment of the gold standard had a strong impact on the international monetary system, and the prices of Japanese foreign bonds were dragged down with the collapse of the US corporate bond prices. The fall in Japanese foreign bond prices were exacerbated by not only a general downtrend in the US markets due to the collapse in corporate bonds but also the depreciation in the yen's exchange rate on the back of the renewal of gold export embargo, and the May 15 Incident which caused an end to the political party cabinet system. There was a subsequent increase in the sensitivity of the dollar-yen exchange rates. Despite the stabilization of US corporate bond yields in Phase 2, Japanese foreign bond prices marked further lows in March 1933, due to a loss in Japan's external creditability during its withdrawal from the League of Nations and further decline in the yen exchange market. However, prices of Japanese foreign bonds rallied in Phase 3 with the rise in the yen's exchange rate during the US abandonment of the gold standard. In Phase 4, there was a high level of stability in the prices of Japanese foreign bonds, and minimal impact was seen from the February 26 Incident. While we cannot identify the influential buyers of Japanese foreign bonds during this period, it was believed that the main buyers were Japanese financial institutions and investors until June 1932, and foreign investors after July 1932. In the domestic market, financial institutions bought up these high-yielding bonds, primarily in the form of sovereign bonds. In the end, the prices of Japanese foreign bonds entered the fifth phase during the outbreak of the Marco Polo Bridge Incident and the Battle of Shanghai. This phase was marked by an apparent rise in foreign investors looking for unloading their bond holdings. Prices plunged, never returning to the previous levels.

Even after January 1932 when Japanese foreign bonds lost support in Wall Street's primary market, they were still traded in the secondary market. Prices rebounded despite a temporary dip. From the discussion in this study, we can conclude that it was around August 1937, with the outbreak of the Battle of Shanghai, that Japanese foreign bonds lost support in the secondary market and completely lost credibility in Wall Street.