The Money and Bond Markets in June

The money market remained very firm in June. Bank credit expanded strongly over the mid-June corporate tax period and also in the latter part of the month, while nationwide reserve availability held steady on average at the reduced May volume. As both credit demand and reserve supply pressures converged upon the money market in June, interest rates came under general upward pressure. This pressure was highlighted by a rise on June 29 and June 30 in the prime lending rate of most commercial banks from 5½ per cent to 5¾ per cent. In addition, rates on bankers' acceptances, commercial paper, and sales finance company paper were increased by ⅛ of a per cent in late June. Federal funds traded at generally high rates throughout the month; toward the end of the period the effective rate climbed for the first time to 5½ per cent, 1 percentage point above the discount rate, while some funds even traded at 5⅝ per cent.

In sharp contrast to the firmness of most other money market rates, yields on Treasury bills continued to edge lower during most of the month in response to a broadly based demand from public funds and other sources which pressed upon scarce market supplies. Even over the June 10 and June 15 corporate dividend and tax payment dates, bill offerings were not heavy and market pressures were minimal. The technical position of the bill sector subsequently improved further when $4.5 billion of tax anticipation bills matured on June 22. A hesitant tone developed in the bill market late in the month, however, when offerings increased and rates rose.

Bond yields continued to move higher in early June, but capital market sentiment improved markedly during the second third of the month, when many traders began to feel that interest rates might be near their peaks. In part, this feeling reflected the better receptions then being accorded new corporate, tax-exempt, and Government agency offerings, all of which carried near-record yields. An additional factor was the feeling on the part of some traders that the pace of economic expansion was slackening.

As bond market sentiment strengthened, a good investment and dealer demand developed for Treasury notes and bonds, and prices of these securities rebounded sharply around midmonth. Later in June, prices of coupon issues first drifted below their highs of the month in profit-taking activity, and then fell sharply when renewed concern developed over the viability of prevailing interest rate levels. Contributing to the reemergence of a cautious atmosphere throughout the bond markets was the increase from 4 per cent to 5 per cent in reserve requirements against certain time deposits of member banks announced by the Board of Governors of the Federal Reserve System on June 27. The increase will apply to each member bank's time deposits—other than passbook savings accounts—in excess of $5 million. (The first $5 million of time deposit accounts will continue to be subject to a 4 per cent reserve requirement.)

In the markets for corporate and tax-exempt bonds, new issue yields continued to rise through midmonth. Prices then generally edged slightly higher for almost two weeks when many offerings attracted fairly good investor interest. In the closing days of June, interest in new issues became more selective at the higher price levels and, as dealer inventories increased, a heavier tone reemerged.

THE MONEY MARKET AND BANK RESERVES

The money market was quite firm in June, especially in the week following the midmonth quarterly corporate tax payment date when accelerated payment schedules for withheld personal income and social security taxes went into effect for large- and medium-sized firms. Net borrowed reserves fluctuated in a somewhat wider range in June than in other recent months, although the average for the month as a whole was about the same as in May. Member bank borrowings from the Federal Reserve Banks also fluctuated widely in June, increasing moderately on a monthly average basis (see Table I). Most transactions in Federal funds occurred in a 5 to 5⅜ per cent range, ⅛ to ¼ of a per cent higher than the range predominating in May, and some trading even took place for the first time at rates as high as 5½ per cent and 5⅝ per cent, 1 to 1⅛ of a per cent above the discount rate. Rates posted by the major New York City banks on call loans to Government securities dealers generally rose from ⅛ to ⅜ of a percentage point from their May peaks, ranging as high as 5⅞ per cent on several days and climbing to 6⅛ per

Table I

FACTORS TENDING TO INCREASE OR DECREASE MEMBER BANK RESERVES, JUNE 1966

In millions of dollars; (+) denotes increase, (−) decrease in excess reserves

Factors	Changes in daily averages— week ended					Net changes
	June 1	June 8	June 15	June 22	June 29	
"Market" factors						
Member bank required reserves*	− 5	− 65	+ 136	− 571	− 53	− 558
Operating transactions (subtotal)	− 498	− 161	− 56	+ 627	− 207	− 295
Federal Reserve float	− 313	+ 95	+ 44	+ 445	− 275	− 4
Treasury operations†	+ 17	+ 125	− 175	+ 96	− 78	− 15
Gold and foreign account	− 17	+ 2	+ 10	− 47	− 70	− 122
Currency outside banks*	− 174	− 401	+ 14	+ 68	+ 186	− 307
Other Federal Reserve accounts (net)‡	− 11	+ 17	+ 54	+ 62	+ 31	+ 153
Total "market" factors	− 503	− 226	+ 80	+ 56	− 260	− 853
Direct Federal Reserve credit transactions						
Open market instruments						
Outright holdings:						
Government securities	+ 442	+ 204	− 60	− 73	+ 267	+ 780
Bankers' acceptances	+ 1	—	+ 1	—	− 2	—
Repurchase agreements:						
Government securities	—	+ 21	+ 37	− 58	—	—
Bankers' acceptances	+ 25	+ 34	− 34	+ 4	+ 48	+ 77
Member bank borrowings	+ 159	− 265	+ 241	− 97	+ 80	+ 118
Other loans, discounts, and advances	− 1	—	− 8	− 6	− 1	− 16
Total	+ 625	− 4	+ 176	− 230	+ 393	+ 960
Excess reserves*	+ 122	− 230	+ 256	− 174	+ 133	+ 107
	Daily average levels					
Member bank:						
Total reserves, including vault cash*	22,368	22,203	22,323	22,720	22,906	22,504§
Required reserves*	21,932	21,997	21,861	22,432	22,485	22,141§
Excess reserves*	436	206	462	288	421	363§
Borrowings	812	547	788	691	771	722§
Free reserves*	− 376	− 341	− 326	− 403	− 350	− 359§
Nonborrowed reserves*	21,556	21,656	21,535	22,029	22,135	21,782§
	Changes in Wednesday levels					
System Account holdings of Government securities maturing in:						
Less than one year	+ 255	+ 156	+ 1	+ 34	+ 288	+ 734
More than one year	+ 33	+ 47	− 108	—	+ 49	+ 21
Total	+ 288	+ 203	− 107	+ 34	+ 337	+ 755

Note: Because of rounding, figures do not necessarily add to totals.

* These figures are estimated.

† Includes changes in Treasury currency and cash.

‡ Includes assets denominated in foreign currencies.

§ Average for five weeks ended June 29.

Table II

RESERVE POSITIONS OF MAJOR RESERVE CITY BANKS JUNE 1966

In millions of dollars

Factors affecting basic reserve positions	Daily averages—week ended					Average of five weeks ended June 29*
	June 1	June 8	June 15	June 22	June 29*	
Eight banks in New York City						
Reserve excess or deficiency(−)†	68	− 2	16	44	15	28
Less borrowings from Reserve Banks	80	14	103	185	147	106
Less net interbank Federal funds purchases or sales(−)	− 161	128	161	676	569	275
Gross purchases	*626*	*811*	*911*	*1,245*	*1,078*	*934*
Gross sales	*788*	*683*	*750*	*569*	*509*	*660*
Equals net basic reserve surplus or deficit(−)	150	− 143	− 247	− 816	− 701	− 351
Net loans to Government securities dealers	632	503	568	524	543	554
Thirty-eight banks outside New York City						
Reserve excess or deficiency(−)†	− 2	53	32	26	15	25
Less borrowings from Reserve Banks	63	72	113	45	150	89
Less net interbank Federal funds purchases or sales(−)	199	571	547	744	495	511
Gross purchases	*1,038*	*1,308*	*1,242*	*1,603*	*1,351*	*1,308*
Gross sales	*840*	*738*	*695*	*859*	*858*	*798*
Equals net basic reserve surplus or deficit(−)	− 264	− 590	− 628	− 763	− 630	− 575
Net loans to Government securities dealers	341	275	232	337	227	282

Note: Because of rounding, figures do not necessarily add to totals.

* Estimated reserve figures have not been adjusted for so-called "as of" debits and credits. These items are taken into account in final data.

† Reserves held after all adjustments applicable to the reporting period less required reserves and carry-over reserve deficiencies.

Table III

AVERAGE ISSUING RATES* AT REGULAR TREASURY BILL AUCTIONS

In per cent

Maturities	Weekly auction dates—June 1966			
	June 6	June 13	June 20	June 27
Three-month	4.573	4.575	4.470	4.435
Six-month	4.744	4.707	4.591	4.610
	Monthly auction dates—April-June 1966			
	April 26	May 25	June 23	
One-year	4.773	4.966	4.697	

* Interest rates on bills are quoted in terms of a 360-day year, with the discounts from par as the return on the face amount of the bills payable at maturity. Bond yield equivalents, related to the amount actually invested, would be slightly higher.

cent at the end of June. Late in the month, rates on bankers' acceptances, commercial paper placed by dealers, and directly placed finance company paper were adjusted upward by ⅛ of a per cent. Moreover, most large commercial banks raised the prime loan rate from 5½ per cent to 5¾ per cent on June 29 and June 30. Offering rates posted by the leading money market banks on time certificates of deposit continued to increase in June when the ceiling rate of 5½ per cent was reportedly paid by prime banks on new certificates maturing in as little as thirty days. The weekly reporting member banks were able to replace a considerable portion of the substantial $3.9 billion of certificates maturing during the quarterly corporate dividend and tax month.

As the banking system helped to service the substantial June credit demands of the economy, the reserve positions of commercial banks remained under considerable pressure. The rate of growth of bank credit, after having slowed in May, expanded more rapidly in June as credit requirements showed more than seasonal strength. During the midmonth corporate dividend and tax payment period, banks extended a large volume of loans to accommodate the seasonal credit demands of businesses and nonbank financial intermediaries. As usual, the New York City banks bore the brunt of the pressures over this period. At the New York City weekly reporting member banks, bank credit rose by approximately $1.5 billion during the statement period ended June 15 which included the dividend and tax payment dates, as against a $1.1 billion increase in the comparable week of 1965. These banks also experienced a net decline of $428 million in their negotiable time certificates of deposit outstanding during the June 15 statement week, compared with only about a $168 million drop during the comparable period a year earlier. Total demand deposits (including checks in process of collection) at weekly reporting member banks in New York expanded by a substantial $3.4 billion, however, as corporations accumulated deposits with which to pay dividends and Federal taxes. Even after the midmonth tax date had passed, loans and investments extended by city banks continued to rise. Associated increases also occurred in their deposit liabilities as they filled the strong supplementary loan demands from businesses making accelerated payments of withholding taxes. During the June 22 statement period, bank credit outstanding at the New York City banks rose by approximately $84 million, as against a decline of $232 million in the comparable week last year. By the last Wednesday of the month, bank credit extended by the New York weekly reporting banks had grown by $2.4 billion from the May 25 level, while total demand deposits had increased by $1.8 billion.

As a result of this sizable deposit and credit expansion, member bank required reserves expanded by an estimated $622 million from the last Wednesday in May through the last Wednesday in June, in contrast with the decline in required reserves which had taken place in May. The rise in required reserves absorbed a particularly large volume of member bank total reserves in the week ended June 22, when net borrowed reserves increased to an average of $403 million.

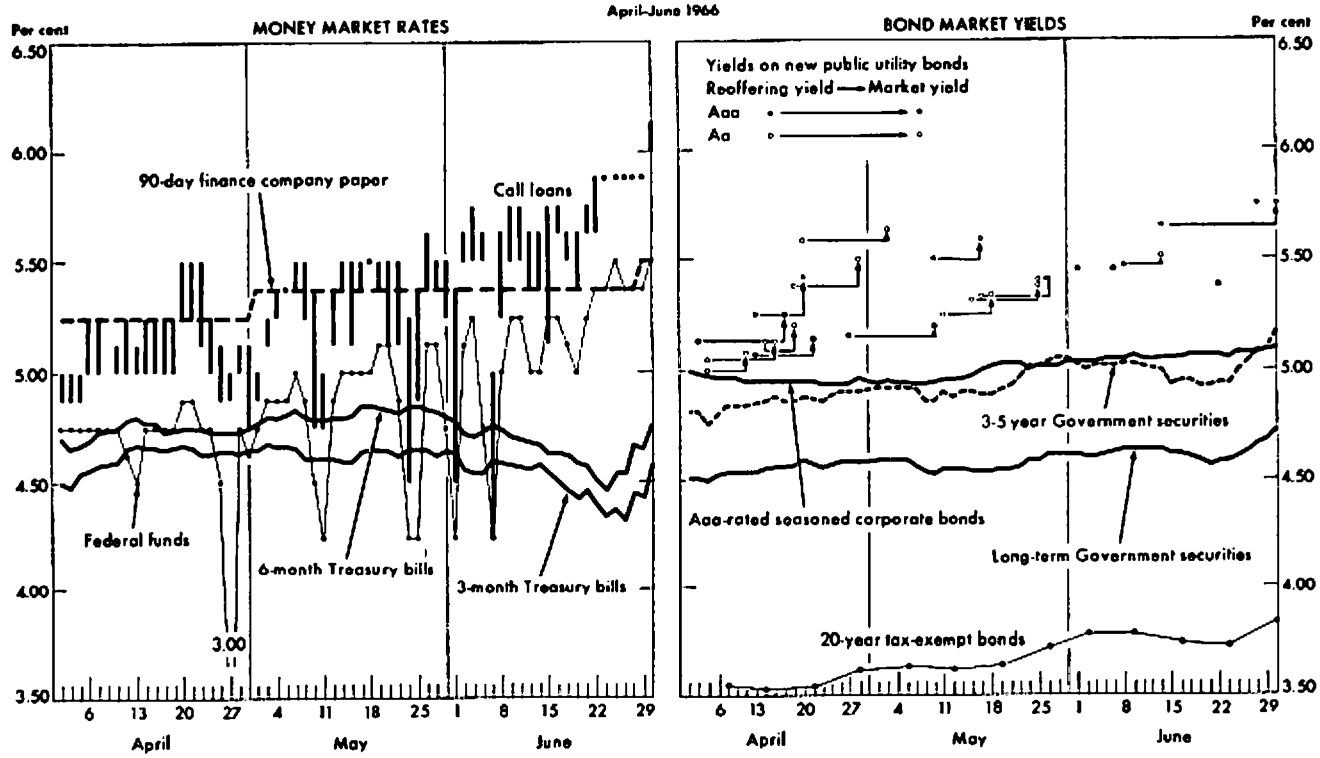
Against this background of an expanded demand for bank credit in June and the persisting limited supply of available reserves, the money market banks accumulated increasingly large reserve deficits as the month progressed (see Table II). The reserve position of the eight major New York banks swung from an average surplus in the June 1 statement week to a deficit which reached as high as an average of $816 million in the June 22 statement period. At thirty-eight large banks outside New York, the basic reserve deficit also grew substantially during the month, rising by $242 million on average in June. The reserve needs of the money market banks were satisfied both through purchases of Federal funds at rising rates and through a continuing heavy volume of borrowings at the Federal Reserve "discount window".

THE GOVERNMENT SECURITIES MARKET

Prices of Treasury notes and bonds fluctuated within a fairly wide range during June. In the opening days of the month, the Treasury coupon sector was buoyed by news from the corporate bond market where a fairly large new Aaa-rated utility issue offered at the highest yield in several decades was accorded an enthusiastic investor reception. At the same time investment demand for Treasury coupon issues, both outright and in switching transactions, expanded and sparked professional demand as well. As a result, prices of coupon issues rose fairly sharply as the month began, with the largest gains recorded by intermediate-term maturities. The rally was of short duration, however, and in the following week a cautious atmosphere reappeared in the coupon sector. During the latter period, the market was affected by the reported weakness of the pound sterling in the foreign exchange market, by the continuing buildup in offerings scheduled in other sectors of the capital market, by renewed heaviness in the corporate bond market, and by developments in Vietnam. Against this background, dealer offerings of coupon issues expanded considerably, investor selling also increased—particularly in the five- to ten-year maturity area, and prices of intermediate- and long-term Treasury issues again edged downward from June 3 through June 9. (The

SELECTED INTEREST RATES *

April–June 1966



Note: Data are shown for business days only.

* MONEY MARKET RATES QUOTED: Daily range of rates posted by major New York City banks on new call loans (in Federal funds) secured by United States Government securities (a point indicates the absence of any range); offering rates for directly placed finance company paper; the effective rate on Federal funds (the rate most representative of the transactions executed); closing bid rates (quoted in terms of rate of discount) on newest outstanding three- and six-month Treasury bills.

BOND MARKET YIELDS QUOTED: Yields on new Aaa- and Aa-rated public utility bonds are plotted around a line showing daily average yields on seasoned Aaa-rated corporate bonds (arrows point from underwriting syndicate reoffering yield on a given issue to market yield on the same issue immediately after it has been released from syndicate restrictions); daily averages of yields on long-term Government securities (bonds due or callable in ten years or more) and of Government securities due in three to five years, computed on the basis of closing bid prices; Thursday averages of yields on twenty seasoned twenty-year tax-exempt bonds (carrying Moody's ratings of Aaa, Aa, A, and Baa).

Sources: Federal Reserve Bank of New York, Board of Governors of the Federal Reserve System, Moody's Investors Service, and The Weekly Bond Buyer.

right-hand panel of the chart on this page illustrates the rise in yields which accompanied this decline in prices.) Subsequently, selling pressures subsided, demand expanded modestly, and prices of coupon issues started to inch higher. The price recovery gained momentum at midmonth, when market participants began to feel that the growth rate of the domestic economy might be moderating and that, if this proved to be the case, prices of debt obligations might soon rise from their relatively low levels. At the same time, the improved tone emerging in the markets for corporate, tax-exempt, and Government agency issues, as well as the intermittent rumors of peace moves in Vietnam, also buoyed the Treasury bond market. These developments triggered further investor and professional demand for coupon issues and, against this background, prices of Treasury notes and bonds generally moved higher from June 10 through June 21. Subsequently, offerings expanded as some traders realized profits, demand contracted, and prices generally receded from June 22 through June 24. In the closing days of the month, prices of coupon issues moved sharply lower in response to the revival of uncertainty over the future course of interest rates.

Demand for Treasury bills was quite strong during most of June, as the increasingly firm tone taking shape in many parts of the money market again failed to influence the bill sector. In recent months, Treasury bills have been in especially heavy demand from investor groups who for various reasons tend to have a strong preference for these bills even at times when rates on competing money market instruments may be considerably higher.

Continuing this trend, a broadly based demand for bills prevailed in June. Public funds made substantial bill purchases, and holders of maturing June 22 tax anticipation bills who did not turn in these bills for taxes reinvested part of their proceeds in other issues. In addition, commercial banks built up bill positions in preparation for their June 30 statement-publishing date. Late in the month the Federal Reserve System bought bills in order to supply reserves to the banking system prior to the long July 4 holiday weekend. In the face of the persisting widespread demand for bills through much of June, dealers' overall bill positions held steady at very low levels, and there were pronounced scarcities of many individual issues. In this setting, the popular June 10 corporate dividend payment date, the midmonth corporate tax date, and the June 20 accelerated withholding-tax payment date passed without giving rise to any real pressure in the bill sector. The moderate bill offerings that did arise, including bills supplied through maturing corporate repurchase agreements with dealers, were readily absorbed. Reflecting the strength of the bill market, rates generally receded during most of June (see the left-hand panel of the chart). At the end of the month, however, offerings expanded and bill rates moved higher when traders began to weigh the possibility that the recent period of strong bill demand might be drawing to a close.

In the market for United States Government agency obligations, new flotations continued to be issued at a rapid pace in June. However, as yields rose, investor interest expanded considerably, and this contributed to the improvement in sentiment throughout the bond markets during the second third of the month. Agency offerings totaled approximately $1.7 billion, of which $1.2 billion represented new money. Early in the month, a $125 million flotation by the Federal Land Banks, consisting of eight-month 5.60 per cent bonds offered at par, encountered investor resistance. Subsequently, investors responded quite enthusiastically to a $530 million June 9 offering of new loan participation certificates. These obligations were offered under the auspices of the Federal National Mortgage Association and were initially priced at par to yield from 5.70 per cent up to 5.75 per cent on one- to five-year issues and from 5.40 per cent down to 5⅜ per cent on thirteen- to fifteen-year issues. Around midmonth, the Federal Home Loan Banks marketed $750 million of short-term securities priced at par to yield from 5.65 per cent on seven-month obligations to 5.75 per cent on one-year securities. This offering was smaller than the market had generally expected, and its high yields again attracted a very good interest on the part of investors. In the wake of this experience, investors began to feel that pressure in the agency market might be abating for a while, and a better feeling emerged throughout the capital markets. On June 21, a flotation by the Federal Intermediate Credit Banks of $283 million of nine-month debentures was fairly well received at an offering yield of 5.60 per cent, the same rate that had been placed on a comparable Credit Bank issue in May.

OTHER SECURITIES MARKETS

The markets for corporate and tax-exempt bonds generally remained under pressure during the early part of June, when sizable additions were made to an already large volume of current and prospective new offerings. At the beginning of the month, a new $50 million Aaa-rated issue of utility debentures, carrying five-year call protection and priced to yield a near-record 5.45 per cent, was accorded an excellent investor reception. This development temporarily buoyed sentiment in various sectors of the bond market. A more restrained atmosphere quickly reappeared, however, as the weight of current and planned June corporate and tax-exempt offerings prompted dealers to make further price concessions on slow-moving accounts (see the right-hand panel of the chart). A better atmosphere took shape in the corporate and tax-exempt sectors for almost two weeks after midmonth, when the higher prevailing yields generated greater investor demand and traders also began to focus upon the lighter July financing calendar and the strengthening tone of the Government agency market. During this period, several new corporate and tax-exempt issues were reoffered at yields as much as 10 basis points below those set on comparable flotations in early June and were accorded good investor receptions. Late in June, however, a more hesitant tone again developed in both sectors. Many new issues encountered investor resistance, and prices moved lower once more.

Over the month as a whole, the average yield on Moody's seasoned Aaa-rated corporate bonds rose by 6 basis points to 5.10 per cent, while *The Weekly Bond Buyer's* series for twenty seasoned tax-exempt issues (carrying ratings ranging from Aaa to Baa) increased by 11 basis points to 3.83 per cent (see the right-hand panel of the chart). These indexes are, however, based on a limited number of seasoned issues and do not necessarily reflect market movements fully, particularly in regard to new and recent issues.