The Money and Bond Markets in April

Short-term interest rates continued to climb during April, under the impact of sustained pressure on member bank reserve positions and further moves by the Federal Reserve System to restrain inflationary forces in the economy and to strengthen the position of the dollar. On April 18, the Board of Governors of the Federal Reserve System announced that it had approved increases in the discount rates of the Federal Reserve Banks of New York, Philadelphia, and Minneapolis to 5½ per cent from 5 per cent, effective the following day. At the same time, the Board announced the adoption of a liberalized schedule of maximum interest rates payable by member banks on large-denomination negotiable certificates of deposit (C/D's), with ceiling rates scaled upward from 5½ per cent on the shortest maturity category to 6¼ per cent on the longest. In the next week, similar discount rate action was taken by the other nine Reserve Banks.[1] Immediately following the initial moves by the System, large commercial banks across the country raised their prime lending rate—the minimum rate charged on loans to the largest and best-rated business borrowers—to 6½ per cent, and major money market banks in New York City and outside

[1] The discount rate increase became effective on April 19 at the San Francisco Reserve Bank, on April 22 at the Atlanta Reserve Bank, on April 23 at the Boston and St. Louis Reserve Banks, and on April 26 at the remaining five.

Table I

FACTORS TENDING TO INCREASE OR DECREASE MEMBER BANK RESERVES, APRIL 1968

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

Factors	Changes in daily averages—week ended on April 3	April 10	April 17	April 24	Net changes
"Market" factors					
Member bank required reserves*	+ 32	+ 118	— 539	+ 169	— 220
Operating transactions (subtotal)	— 196	— 274	+ 471	— 154	— 153
Federal Reserve float	— 85	+ 188	+ 167	+ 37	+ 307
Treasury operations†	+ 303	+ 22	+ 94	— 616	— 198
Gold and foreign account	+ 23	+ 14	+ 20	— 12	+ 45
Currency outside banks*	— 236	— 544	+ 29	+ 462	— 289
Other Federal Reserve accounts (net)‡	— 200	+ 47	+ 100	— 26	— 25
Total "market" factors	— 164	— 156	— 68	+ 15	— 373
Direct Federal Reserve credit transactions					
Open market instruments					
Outright holdings:					
Government securities	+ 13	+ 316	+ 2	— 25	+ 306
Bankers' acceptances	— 1	—	—	—	— 1
Repurchase agreements:					
Government securities	+ 164	+ 30	+ 66	— 260	—
Bankers' acceptances	— 3	+ 20	— 49	— 14	— 46
Federal agency obligations	+ 45	— 36	— 2	— 7	—
Member bank borrowings	+ 114	— 60	+ 117	— 112	+ 69
Other loans, discounts, and advances	—	—	—	—	—
Total	+ 333	+ 270	+ 134	— 418	+ 328
Excess reserves*	+ 169	+ 128	+ 66	— 403	— 45

	Daily average levels				
Member bank:					
Total reserves, including vault cash*	25,463	25,408	26,073	25,501	25,626§
Required reserves*	25,133	25,015	25,554	25,385	25,273§
Excess reserves*	330	463	519	116	355§
Borrowings	696	646	763	651	689§
Free reserves*	— 366	— 183	— 244	— 535	— 334§
Nonborrowed reserves*	24,767	24,822	25,310	24,850	24,937§

	Changes in Wednesday levels				
System Account holdings of Government securities maturing in:					
Less than one year	+ 676	— 424	+ 331	— 905	— 322
More than one year	+ 128	—	—	+ 9	+ 137
Total	+ 804	— 424	+ 331	— 896	— 185

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 of four weeks ended on April 24.

Table II

RESERVE POSITIONS OF MAJOR RESERVE CITY BANKS APRIL 1968

In millions of dollars

Factors affecting basic reserve positions	Daily averages—week ended on April 3	April 10	April 17	April 24*	Averages of four weeks ended on April 24*
Eight banks in New York City					
Reserve excess or deficiency(—)†	18	121	— 2	— 7	33
Less borrowings from Reserve Banks	—	127	46	49	56
Less net interbank Federal funds purchases or sales(—)	436	1,131	1,211	672	863
Gross purchases	*950*	*1,479*	*1,726*	*1,466*	*1,405*
Gross sales	*514*	*348*	*515*	*793*	*543*
Equals net basic reserve surplus or deficit(—)	— 418	—1,137	—1,259	— 729	— 886
Net loans to Government securities dealers	758	729	736	513	684
Thirty-eight banks outside New York City					
Reserve excess or deficiency(—)†	12	44	33	31	30
Less borrowings from Reserve Banks	278	71	407	293	262
Less net interbank Federal funds purchases or sales(—)	356	624	884	1,191	764
Gross purchases	*1,603*	*1,910*	*2,018*	*2,298*	*1,957*
Gross sales	*1,247*	*1,287*	*1,134*	*1,107*	*1,194*
Equals net basic reserve surplus or deficit(—)	— 622	— 650	—1,258	—1,453	— 996
Net loans to Government securities dealers	232	406	635	371	411

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—April 1968: April 1	April 8	April 15	April 22	April 29
Three-month	5.146	5.309	5.463	5.542	5.499
Six-month	5.265	5.400	5.568	5.689	5.612

Maturities	Monthly auction dates—February-April 1968: February 21	March 26	April 23
Nine-month	5.239	5.424	5.665
One-year	5.281	5.475	5.663

* 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.

posted higher offering rates on new C/D's.

While nationwide net reserve availability averaged about the same in April as in March, the reserve positions of the major money market banks in New York City deteriorated sharply, and most Federal funds trading took place at 5¾ or 5⅞ per cent, compared with 5¼ to 5½ per cent in the latter half of March. During the three statement weeks ended on April 17, covering the income tax date and preceding the increase in the Regulation Q ceiling, the city banks experienced a C/D attrition of $503 million, substantially greater than the $186 million attrition in the comparable period of March which also included a tax date. After the March 31 quarterly statement date, banks liquidated Treasury bills in volume, so that bill rates came under strong upward pressure early in April. They were marked up further after an announcement by the Treasury of an addition to its weekly auction of six-month bills, and still further after the discount rate increase. The latter action also prompted increases in rates on bankers' acceptances, finance company paper, prime commercial paper, and Euro-dollars.

In contrast to the pronounced upward trend of short-term interest rates, yields rose only slightly on intermediate-term issues and declined moderately on long-term Treasury securities during April. Prices of Treasury coupon issues rose sharply at the beginning of the month after President Johnson announced on March 31 that he had ordered a limitation of the bombing of North Vietnam and was seeking early peace negotiations. However, price gains were limited by increasing disappointment in the market over the delay in reaching agreement on a site for peace talks and over the failure of the Congress to act affirmatively on a tax increase. The announcement of increases in the discount rate and in the Regulation Q ceiling on April 18 caused a sharp markdown of prices, but revived hope of peace negotiations and tax action served to steady the market later. However, the approach of the Treasury's May financing was a restraining influence on prices. Similarly, in the markets for corporate and tax-exempt bonds, an atmosphere of buoyancy early in the period was later replaced by one of hesitancy and caution, and yields established on new offerings rose.

BANK RESERVES AND THE MONEY MARKET

Average net borrowed reserves of member banks amounted to $334 million during the four statement weeks ended in April (see Table I), only moderately higher than the $311 million average (revised) in the four statement weeks of March. Net reserve availability varied widely within the period, however, with average net borrowed reserves easing to the $200 million level in the second and third statement weeks and deepening to $535 million in the final week of the month.

The money market was continuously firm during April, and Federal funds were generally quoted at a substantial premium over the prevailing discount rate. This premium rose as high as ⅞ percentage point at the start of the month, when the major money market banks in New York City began to feel the effects of a marked deterioration in their basic reserve position. The average basic reserve deficit of the forty-six reporting money market banks mounted to more than $2.5 billion in the week of April 17 (see Table II) from $0.7 billion in the final week of March, reflecting the continuing heavy financing needs of dealers in United States Government securities and an increased demand for business and sales finance company loans. In the statement week of April 17, moreover, the city banks, along with banks elsewhere in the country, sustained a sharp loss of C/D's as maturities around the income tax date were not renewed. Prior to the increase in the discount rate, rates charged by the city banks on new call loans to Government securities dealers were quoted at about 6 to 6½ per cent, compared with 5½ to 5¾ per cent in late March (see chart). Money market rates moved generally higher following the increase in the discount rate. Later in the statement week ended on April 24, however, conditions tended to ease temporarily, mainly because of the release of accumulated excess reserves by the "country" banks. In that week, moreover, the basic reserve position of the money market banks improved, largely because of a rapid repayment of business loans and a sharp decline in the financing needs of dealers in United States Government securities. At the end of the month, however, pressures in the money market intensified; the effective rate for Federal funds rose to 6¼ per cent, the highest since November 1966, and new call loans to dealers were quoted at 6⅝ to 6¾ per cent.

Under the new schedule of maximum rates of interest payable on C/D's, rates of 5¾ per cent may be offered on 60- to 89-day maturities, 6 per cent on 90- to 179-day maturities, and 6¼ per cent on maturities of 180 days or more. The 5½ per cent ceiling, which had previously applied to all maturities, continues in effect for maturities of 30 to 59 days. Immediately after the ceilings were lifted, the money market banks in New York City raised their posted offering rates on new C/D's maturing in 90 days or more to 5⅞ per cent, and a rate of 6 per cent was posted by the end of the month. The new C/D offering rates posted at the end of April compared with dealer offering rates of 5⅞ per cent on 90-day unendorsed bankers' acceptances and 6 per cent on prime four- to six-month commercial paper, with a published offering rate of 5⅞ per cent on directly placed finance company paper maturing in 30 to 270 days and with a bond equivalent yield of 5.88 per cent on six-month Treasury bills.

During the statement week ended on April 24, the weekly reporting banks in New York City gained $184 million through an increase in large C/D's, after having lost $359 million through C/D runoffs in the preceding week. At large commercial banks throughout the country, the net contraction of C/D's in the April 17 statement week amounted to $697 million, a substantial proportion of the $1,243 million that had been scheduled to mature on the April 15 tax date. In the following statement week, however, C/D liabilities of these institutions rose by $286 million, in response to the higher issuing rates posted subsequent to the increase in the Regulation Q ceiling.

THE GOVERNMENT SECURITIES MARKET

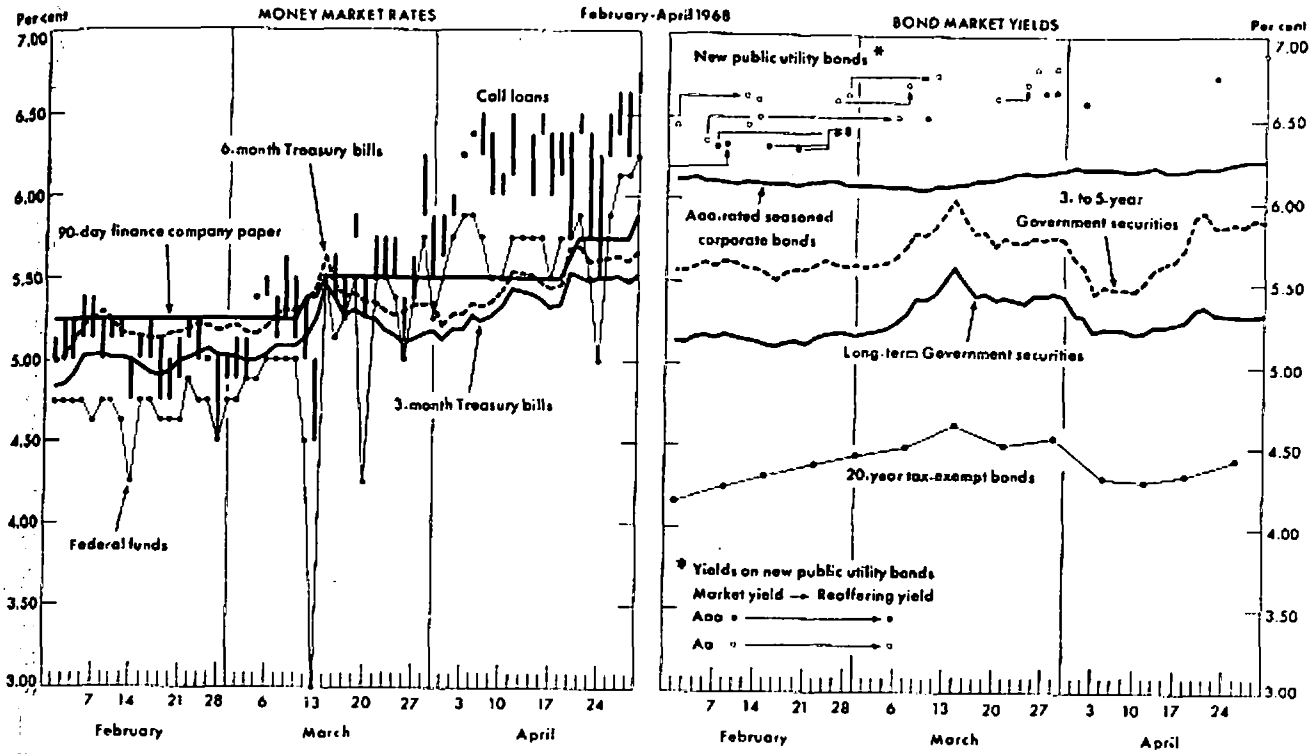
Prices of Treasury notes and bonds rose sharply during the first three days of April, in reaction to the speech by President Johnson on March 31 announcing a halt in the bombing of much of North Vietnam and calling for peace negotiations, and to subsequent indications that this de-escalation move had met with a favorable response from the Hanoi government. The coupon market was further strengthened by news that the United States Senate, on April 2, had approved legislation providing for a 10 per cent income tax surcharge and a $6 billion reduction in Federal Government spending. Optimism in the market soon faded, however, as progress toward peace negotiations was stalled by the failure of the Washington and Hanoi governments to reach agreement on a site for the talks, and as further consideration of income tax legislation by the Congress was postponed until after the Easter recess. Moreover, market participants began to reflect that the Vietnam negotiations might be quite lengthy and that even a total cessation of hostilities in Vietnam would not bring about an immediate sizable reduction in defense spending. They saw further cause for concern over the outlook for intermediate- and long-term yields in the recent resurgence in the demand for business loans at commercial banks, in the sizable calendar of new corporate financing, and in increasing evidence of strong monetary restraint. As midmonth approached, in fact, there was growing speculation about an increase in the commercial bank prime lending rate.

After the announcement of the discount rate increase on April 18, prices of Treasury coupon issues were marked down sharply. Over the remainder of the period, however, prices fluctuated irregularly, mainly in response to varied news reports regarding the outlook for peace negotiations and for enactment of income tax legislation. Activity was limited, as participants awaited an announcement of the terms of the Treasury's refunding of May maturities expected near the month end. (The Treasury announced on May 1 that it was offering at par a 6 per cent seven-year note in exchange for the 4¾ per cent note and 3⅞ per cent bond maturing on May 15. The maturing issues total $8 billion, approximately $3.9 billion of which is publicly held. Additionally, the Treasury announced a concurrent offering for cash of about $3 billion of a fifteen-month note, priced at par to yield 6 per cent. The payment and delivery date for both of the new issues is May 15.)

Rates on Treasury bills rose substantially during April, attaining their highest levels since the fall of 1966. The news of a reduction in hostilities in Vietnam produced only a limited markdown in bill yields on the opening day of the period. Over the first half of the month, rates tended to rise in response to aggressive selling by commercial banks meeting increased pressure on their reserve positions and by dealers attempting to reduce inventories in the face of substantially higher financing costs. On April 11, rates were marked up sharply after an announcement by the Treasury that the size of the regular weekly offering of six-month bills would be increased by $100 million. Around midmonth, however, the market firmed in response to the reappearance of investment buying. Demand was strong from public funds and other investors, including holders of April tax anticipation bills who redeemed for cash bills not tendered in payment of income taxes. Frequently such demand encountered a thin supply of offerings. Bill rates were adjusted roughly 20 to 30 basis points higher on April 19, when increases in the discount rates of four Reserve Banks and in the Regulation Q ceilings on C/D's became effective.

Bidding in the regular weekly auctions of three- and six-month bills was unenthusiastic in the first two auctions held during the month, but was quite aggressive in later auctions at the higher rate levels after investment buying reappeared. In the auction held on April 15, the first in which the additional $100 million of six-month maturities was offered, bidding resulted in average issuing rates of 5.46 per cent and 5.57 per cent for the three- and six-month issues, respectively, 15 and 17 basis points higher than corresponding rates established in the preceding weekly auction (see Table III). Issuing rates rose further in the next auction, but tapered off in the final weekly auction of April. In the regular monthly auction of longer bill maturities held at the end of April, the nine-month and one-year bills were awarded at average issuing rates of 5.67 per cent and 5.66 per cent, respectively, 24 and 19 basis

SELECTED INTEREST RATES



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.

points above rates established on comparable offerings in the March auction.

In the market for Federal agency securities, a $445 million issue of nine-month debentures of the Federal intermediate credit banks, originally intended to be offered just before the discount rate increase, was postponed until April 24, when it received an excellent market reception at a yield of 6.10 per cent. On April 17, the Export-Import Bank of the United States, for the first time, began selling short-term discount notes in order to obtain supplemental funds for its various export programs. Maturities of the notes, ranging from 30 to 360 days, are selected by investors with the approval of the agency. The Attorney General has ruled that contractual obligations of the Export-Import Bank are general obligations of the United States.

OTHER SECURITIES MARKETS

Prices of corporate and tax-exempt bonds moved sharply higher at the beginning of April in the wake of the announcement of new attempts by the Administration to seek a negotiated settlement of the Vietnam war. Dealers' inventories of both corporate and tax-exempt debt issues were reduced substantially: unsold balances of recent offerings were quickly taken from dealers, and new issues being marketed at higher prices met a favorable response from investors. As the month progressed, however, signs of investor resistance to the higher price levels became apparent. A few issues were postponed, and one prospective corporate borrower canceled an offering after obtaining financing through a commercial-bank term loan.

After the discount rate increase, prices in the corporate and tax-exempt markets weakened considerably. Illustrating the sharp change of sentiment in the corporate market, a large issue of Aaa-rated long-term telephone bonds was sold late in the month at a reoffering yield of 6.75 per cent, whereas a comparable offering at the start of the period had been successfully marketed at a yield of 6.60 per cent. Although many participants in the tax-exempt market were hopeful that the increase in the Regulation Q ceiling would provide some assurance of continued bank buying, more apparently felt that the increase in monetary restraint taking place did not augur well for the market over the months ahead. Thus, *The Weekly Bond Buyer's* average yield series of twenty seasoned tax-exempt issues, which had declined sharply from 4.54 per cent at the start of April to 4.29 per cent just prior to the discount rate and Regulation Q actions, rose to close the month at 4.43 per cent. Over the latter part of April, inventories of both corporate and tax-exempt issues tended to accumulate in dealers' hands. The Blue List of dealers' advertised inventories of tax-exempt bonds climbed to $585 million at the month end, substantially higher than the $454 million at the end of March.