The Money and Bond Markets in November

Interest rate movements were mixed during November. The yields on three-month Treasury bills and on intermediate- and long-term securities fell during the month. The rates on Treasury bills of six months or longer and on several money market instruments moved higher. A combination of selling pressure resulting from the improved international position of the dollar and a growing concern among market participants that monetary policy might not loosen significantly in the coming months caused many rates to rise sharply in the first half of November. However, rates declined noticeably in the second half of the month, when investors began anticipating slower business activity in the months ahead as a consequence of the energy shortage. For the month as a whole, the rate on bankers' acceptances rose ¼ percentage point, while secondary market rates on negotiable certificates of deposit (CDs) increased 81 basis points. The effective rate on Federal funds during the statement week ended December 5 was 10.17 percent, 27 basis points higher than during the final week of October.

Higher inventories acquired in the November financing, expectations that foreign central banks would be selling securities, and an increase in dealer financing costs exerted steady upward pressure on yields in the Government securities market early in November. In addition, Governor Brimmer's statement that inflation would continue in 1974 reinforced the already cautious atmosphere in the market, and yields on all maturities rose sharply. A much firmer tone developed toward the end of the month's second week, and rates generally receded over the remainder of the period. New issue activity in the market for Federal agency securities was moderately heavy, but interest rates on agency securities recorded only small changes. There was a substantial volume of new issues in the corporate and municipal bond markets, and yields were essentially unchanged.

The narrow money supply (M_1)—demand deposits adjusted plus currency outside banks—grew much more rapidly in November than in October. The broad money supply (M_2), which includes time and savings deposits other than large-denomination CDs, expanded only slightly faster than in October. The seasonally adjusted volume of CDs outstanding declined again as it did in October and September. Partially as a result of this and partly in response to a change in the composition of business borrowing, the adjusted bank credit proxy declined from its October level.

BANK RESERVES AND THE MONEY MARKET

Interest rates on money market instruments edged upward during November (see Chart I). Yields on nonbank-related, dealer-placed commercial paper registered increases of ⅝ to ⅞ percentage point and closed the month ranging from 9⅛ percent to 9½ percent. The effective rate on Federal funds averaged 10.03 percent, 2 basis points above October's average level. The volume of nonborrowed reserves declined in November; however, total reserves fell by an even larger amount. As a result, both seasonal and nonseasonal member bank borrowings declined, for the third successive month (see Table I).

The market for CDs continued to show the effects of the higher marginal reserve requirement that was imposed in September as well as the lighter demand for bank loans. The volume of CDs outstanding declined in November for the third consecutive month. However, there was a modest increase during the final week of the month. In the secondary market, the interest yield on CDs increased to 9.34 percent.

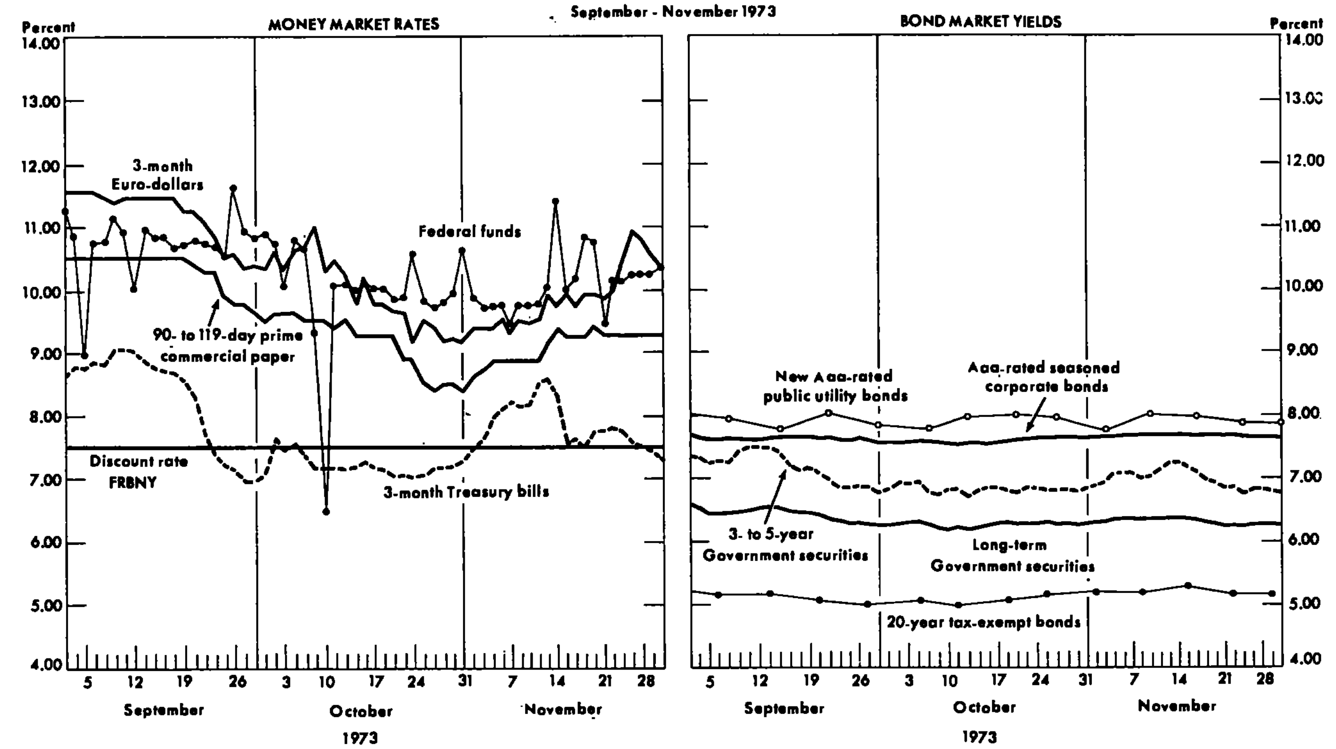
The 9½ percent prime lending rate that was set by several major banks in late October spread to a few additional banks during the first week of November. However, the 9½ percent rate did not become universal, and on the last day of the month a few of the banks that had been quoting 9½ percent returned their rates to 9¾ percent.

The narrow money supply grew considerably faster in November than it had in recent months. Preliminary data indicate that for the three months ended in November, M_1 expanded at a seasonally adjusted annual rate of 4 percent, up from 0.2 percent for the three months ended in October (see Chart II).

Chart I

SELECTED INTEREST RATES

September - November 1973



Note: Data are shown for business days only.

MONEY MARKET RATES QUOTED: Bid rates for three-month Euro-dollars in London; offering rates (quoted in terms of rate of discount) on 90- to 119-day prime commercial paper quoted by three of the five dealers that report their rates, or the midpoint of the range quoted if no consensus is available; 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-month Treasury bills.

BOND MARKET YIELDS QUOTED: Yields on new Aaa-rated public utility bonds are based on prices asked by underwriting syndicates, adjusted to make them equivalent to a standard Aaa-rated bond of at least twenty years' maturity; daily averages of yields on seasoned Aaa-rated corporate bonds; daily averages of yields on long-term Government securities (bonds due or callable in ten years or more) and on 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, Inc., and The Bond Buyer.

In November, M_2 expanded at about an 11 percent rate, approximately the same rate that prevailed in October. The three-month growth rate of M_2 through November is 8½ percent, and for the year so far it is 7¾ percent. The interest rate ceilings that were imposed on four-or-more-year consumer-type time deposits last month accompanied by higher short-term interest rates caused the growth of other time deposits to diminish somewhat in November. Despite this slowdown, other time deposits still expanded at a healthy 12 percent rate.

Contrary to the behavior of the other monetary aggregates, the adjusted bank credit proxy—which consists of daily average member bank deposits subject to reserve requirements plus certain nondeposit liabilities—grew in November at only a 0.5 percent annual rate. The slow growth has been partly a reflection of the higher costs to banks of raising funds in the CD market since the reserve requirement on CDs was increased. It is also caused by the fact that, during the last week of September, the rate on commercial paper fell below the prime rate and business credit demand shifted to the commercial paper market. This reduced the banks' need for funds and tempered their CD sales effort. Since late September, the volume of commercial paper outstanding has increased noticeably while the credit proxy has shown virtually no growth.

The fall in the volume of CDs is, in some measure,

Table I

FACTORS TENDING TO INCREASE OR DECREASE MEMBER BANK RESERVES, NOVEMBER 1973

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

Factors	Changes in daily averages— week ended Nov. 7	Nov. 14	Nov. 21	Nov. 28	Net changes
"Market" factors					
Member bank required reserves	+ 457	— 347	— 11	+ 369	+ 468
Operating transactions (subtotal)	+ 198	+ 503	—1,726	+ 376	— 649
Federal Reserve float	— 57	+ 332	+ 300	+ 444	+1,019
Treasury operations*	+ 343	+ 996	— 800	+ 106	+ 645
Gold and foreign account	— 53	— 248	+ 23	— 94	— 372
Currency outside banks	— 289	— 532	—1,051	— 44	—1,916
Other Federal Reserve liabilities and capital	+ 256	— 46	— 198	— 35	— 23
Total "market" factors	+ 655	+ 156	—1,737	+ 745	— 181
Direct Federal Reserve credit transactions					
Open market operations (subtotal)	— 325	— 848	+2,561	— 827	+ 561
Outright holdings:					
Treasury securities	— 65	—1,140	+1,484	— 3	+ 276
Bankers' acceptances	+ 1	— 5	— 2	+ 1	— 5
Federal agency obligations	—	—	+ 14	+ 42	+ 59
Repurchase agreements:					
Treasury securities	— 232	+ 259	+ 893	— 727	+ 193
Bankers' acceptances	— 8	+ 10	+ 25	— 22	+ 5
Federal agency obligations	— 21	+ 28	+ 147	— 118	+ 36
Member bank borrowings	— 285	+ 351	+ 48	— 281	— 167
Seasonal borrowings†	— 26	— 13	+ 5	— 1	— 35
Other Federal Reserve assets‡	+ 89	+ 97	— 557	+ 45	— 326
Total§	— 521	— 400	+2,052	—1,064	+ 67
Excess reserves‡	+ 134	— 244	+ 315	— 319	— 114

	Daily average levels				Monthly averages
Member bank:					
Total reserves, including vault cash‡	34,625	34,728	35,054	34,366	34,693‖
Required reserves	34,360	34,707	34,718	34,349	34,534‖
Excess reserves§	265	21	336	17	160‖
Total borrowings	1,170	1,521	1,569	1,288	1,387‖
Seasonal borrowings†	93	80	85	84	86‖
Nonborrowed reserves	33,455	33,207	33,485	33,078	33,306‖
Net carry-over, excess or deficit (—)#	120	186	58	212	144‖

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

* Includes changes in Treasury currency and cash.

† Included in total member bank borrowings.

‡ Includes assets denominated in foreign currencies.

§ Adjusted to include $84 million of certain reserve deficiencies on which penalties can be waived for a transition period in connection with bank adaptation to Regulation J as amended effective November 9, 1972. The adjustment amounted to $450 million from November 9 through December 27, 1972, $279 million from December 28, 1972 through March 28, 1973, $172 million from March 29 through June 27, 1973, and $112 million from June 28 through September 26, 1973.

‖ Average for four weeks ended November 28, 1973.

Not reflected in data above.

responsible for the decline in reserves available to support private nonbank deposits (RPD) during November. After showing no growth during October, RPD contracted at an 11 percent rate during November.

THE GOVERNMENT SECURITIES MARKET

The interest rate on three-month Treasury bills fell slightly in November, while the rates on six-month and 52-week bills advanced modestly. Throughout the month, the market's tone was affected by several competing factors. Among these was concern over the short-run implications of the international strength of the dollar relative to certain foreign currencies. The strong demand for the dollar created a situation in which foreign central banks needed funds to support their own currencies. To obtain the required funds, the central banks sold some of their holdings of United States Treasury securities. In addition, the spreading consensus that monetary policy was unlikely to promote ease in coming months and the continued high costs of financing dealers' inventories both exerted upward pressure on short-term rates early in November. Against these accumulating concerns, the Treasury's announcement that it would auction a strip of bills totaling $1.1 billion to raise cash because of foreign central bank redemptions of special Treasury certificates contributed to the sharp climb in rates early in the month. The "strip" consisted of a $100 million addition to each regular weekly bill issue maturing between November 23 and January 31. Bidding for the strip when it was sold on November 9 was indifferent, and the average issuing rate was set at 8.67 percent.

At the regular weekly auction of November 12, the rates on newly issued three- and six-month bills were 8.64 and 8.38 percent, respectively (see Table II), 144 and 112 basis points above the rates set at the last regular auction in October. At these yields, however, substantial investor demand materialized. The market received additional support, as information and opinion concerning the energy shortage became more abundant. The market interpreted this information to indicate that the pace of economic activity in the near future would be more restrained than was initially expected. Consequently, bill rates reversed field and declined abruptly. Issuing rates on three- and six-month bills at the auction of November 19 were down 93 and 58 basis points from the previous week. However, continued selling pressure was sufficient to prevent the rates on six-month and 52-week bills from completely retracing their earlier gains. For the month as a whole, rates on three-month bills were 6 basis points lower while rates on six-month bills were up 35 basis points. During November, the yield on 52-week securities rose 29 basis points.

On November 28 the Treasury sold $3 billion of tax anticipation bills, of which $1 billion will mature next April 19 and $2 billion on June 21. The bills can be used at face value to pay Federal income tax due in April and June. Both maturities were well received. The average issuing rate on the April 19 bills was 7.83 percent, and on the June 21 issue it was 7.79 percent.

After fluctuating within a relatively narrow range, the prices of Treasury coupon securities finished November very near their end-of-October levels. The prices of intermediate-term securities registered moderate declines early in the month, as participants noted that the Federal funds rate had stopped falling and that further declines appeared unlikely. The market's technical position was somewhat weak because of large dealer inventories remaining from the Treasury refunding late in October. Governor Brimmer's statement that inflation would keep interest rates high in 1974 added another pessimistic note, and the yields on coupon securities followed bill rates upward. In the second half of the month, investors began weighing the possibility that the energy shortage could curtail economic activity and lead to an easier monetary policy next year. At the same time, yields on corporate and municipal bonds, which had been exerting a depressing influence on prices of coupon securities, began to move downward. As a result, the prices of Treasury coupon securities reversed their earlier losses and finished the month essentially unchanged.

The prices of Federal agency securities changed very little, as new issue activity declined a bit from its pace of the preceding few months. The Federal Home Loan Banks offered a $600 million refinancing, $300 million maturing in May 1976 and $300 million coming due in November 1977. The rate on both maturities was 7.45 percent. They were well received and soon traded at premium prices. Late in the month, the Federal National Mortgage Association offered a $1.3 billion package of debentures maturing between June 10, 1977 and December 10, 1982. The offering rates were set between 7.20 percent and 7.35 percent, and the financing attracted a lively pre-sale interest.

Table II

AVERAGE ISSUING RATES*
AT REGULAR TREASURY BILL AUCTIONS

In percent

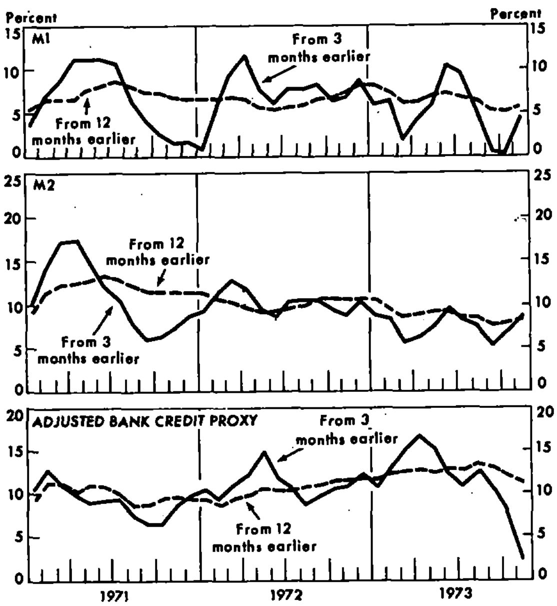
Maturities	Weekly auction dates—November 1973			
	Nov. 5	Nov. 12	Nov. 19	Nov. 26
Three-month	8.098	8.636	7.704	7.695
Six-month	7.987	8.381	7.805	7.679
	Monthly auction dates—September-November 1973			
	Sept. 19	Oct. 17	Nov. 14	
Fifty-two weeks	8.057	7.132	7.708	

* 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.

Chart II

CHANGES IN MONETARY AND CREDIT AGGREGATES

Seasonally adjusted annual rates



Note: Data for November 1973 are preliminary.

M1 = Currency plus adjusted demand deposits held by the public.

M2 = M1 plus commercial bank savings and time deposits held by the public, less negotiable certificates of deposit issued in denominations of $100,000 or more.

Adjusted bank credit proxy = Total member bank deposits subject to reserve requirements plus nondeposit sources of funds, such as Euro-dollar borrowings and the proceeds of commercial paper issued by bank holding companies or other affiliates.

Sources: Board of Governors of the Federal Reserve System and the Federal Reserve Bank of New York.

OTHER SECURITIES MARKETS

Prices of corporate and municipal bonds changed marginally during November. Prices were under steady pressure during the first half of the month. Anticipations of a large volume of new issues, general concern over the troubled state of affairs in the Mideast, and the possibility that the oil embargo could cut into utility company earnings all operated to force prices downward. However, forecasts of an economic slowdown in 1974 stimulated the market during the latter part of the month. Prices regained most of their earlier losses and finished the month slightly above their opening levels.

After starting slowly, the new issue market in corporate debt was quite active in November. One of the key new issues was a $170 million offering of Aaa-rated thirty-year debentures. These were sold to yield 8.07 percent, 12 basis points higher than the yield on a similar issue sold late in October. Later in the month the American Telephone & Telegraph Company sold $500 million worth of preferred stock. The stock was priced to yield 7.48 percent, some portion of which is exempt from Federal corporate income tax. The issue met a fair reception.

The new issue market in tax-exempt securities was quite active for the second consecutive month. Most of the offerings sold at yields above those on comparable securities marketed at the end of October. One offering of Aaa-rated bonds was priced to yield from 4.20 percent in 1979 to 4.94 percent in 1991. The yield on the short maturity was 15 basis points higher than a similar bond marketed October 30. Another large issue of bonds with an A-1 rating that was sold later in November was priced to yield from 4.50 percent in 1975 to 5.97 percent in 2016. It received a good initial reception, but demand subsequently tapered off. The Bond Buyer index of twenty tax-exempt bond yields closed the month at 5.15 percent, 3 basis points above its level at the end of October. The Blue List of dealers' advertised inventories rose in November by $47 million to $978 million.