The Money and Bond Markets in June

Interest rates in the money and bond markets declined somewhat in June, after increasing in the previous month. With Federal funds trading in a narrow range, rates on money market instruments halted their upward movement and edged slightly back toward lower levels. Bond yields also retraced part of the increases that were registered in May.

The United States Treasury auctioned 24-, 49-, and 61-month notes during June, raising $5.0 billion in new cash. Conversely, at the regular weekly auctions of Treasury bills, net redemptions reduced the amount of short-term debt outstanding. New bond financing in the corporate market was heavy, as firms continued to use bond sales as a major source of financing. Most new issues sold well, although some aggressively priced issues met investor resistance at the month end.

Preliminary data indicate that the narrowly defined money stock (M_1) declined slightly in June after the temporary spurt of late April and early May. Meanwhile, the broadly defined money stock (M_2) grew at a modest pace. In addition, for the first time in 1976, banks increased the volume of outstanding large negotiable certificates of deposit (CDs) during June. This contributed to substantial expansion in the bank credit proxy—total member bank deposits subject to reserve requirements plus certain nondeposit sources of funds—following rather slow growth earlier in the year.

THE MONEY MARKET AND THE MONETARY AGGREGATES

Interest rates on money market instruments declined slightly in June, after having risen sharply since mid-April. Yields on 90- to 119-day commercial paper ended the month at 5.75 percent, nearly unchanged from rates quoted at the opening of the period. Rates on ninety-day bankers' acceptances fell by 23 basis points in June to close the month at 5.68 percent. The average yield in the secondary market on ninety-day CDs declined sharply during the first week of the month but traded at a nearly constant level thereafter to end June at 5.73 percent, down 18 basis points from the rate at the end of May.

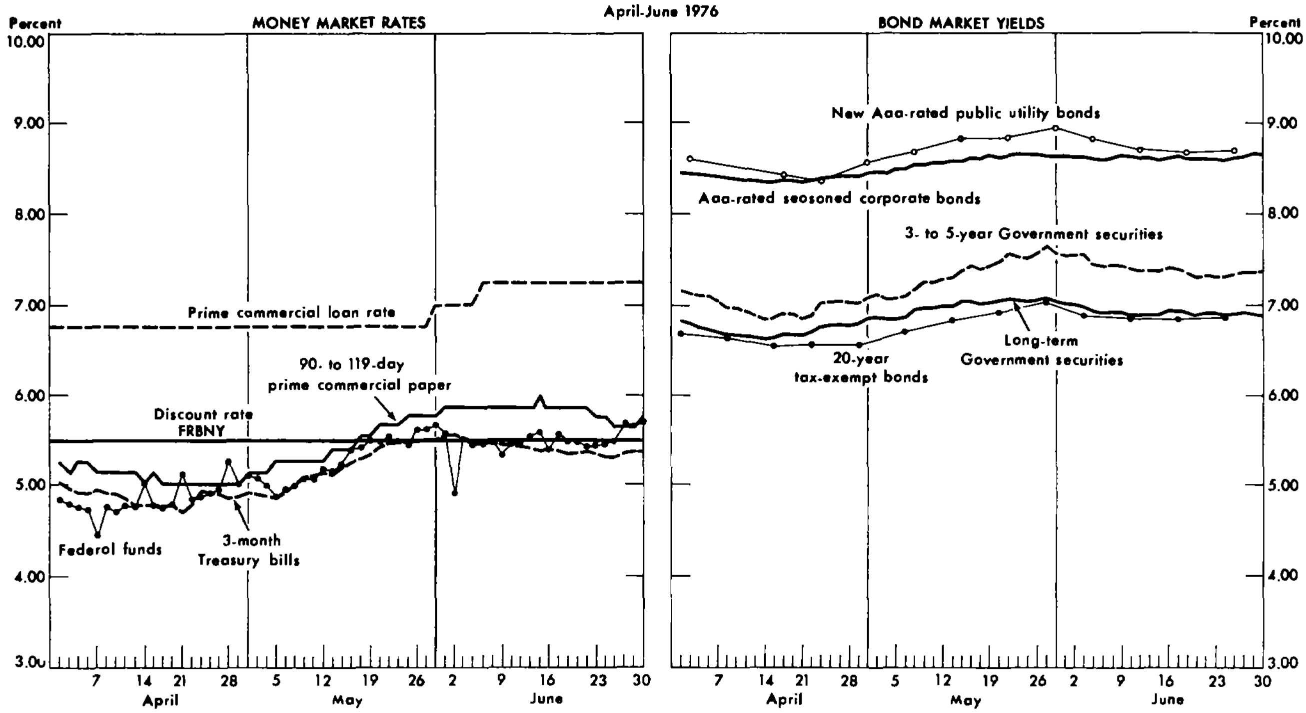
The effective rate on Federal funds averaged 5.48 percent in June (see Chart I), an increase of 19 basis points over the average for May but roughly unchanged from the levels of the final week of that month. During June, Federal Reserve open market operations were primarily aimed at offsetting massive shifts in Treasury balances between commercial banks and Federal Reserve Banks. In recent years, the Treasury has been acting to minimize the cash holdings in its Tax and Loan Accounts at commercial banks. The Treasury typically transfers the receipts which flow into these deposits to its accounts at Federal Reserve Banks. These transfers—Treasury calls—drain reserves from the banking system. Conversely, when Treasury expenditures exceed receipts and Treasury balances at Federal Reserve Banks decline, reserves are released to the banking system. The amplitude of fluctuations in Treasury balances at Federal Reserve Banks has increased sharply since 1974, leading to the large impact of Treasury operations on bank reserves reported in Table I. The average absolute weekly impact of Treasury operations on commercial bank reserves was $2.09 billion, computed on a daily average basis, in the first half of this year as compared with only $0.45 billion in the first half of 1973. The effect of these fluctuations on bank reserves can be offset through Federal Reserve open market operations, and Federal Reserve transactions for the System Account have generally mirrored these swings. This activity was particularly heavy in June. The Treasury borrowed funds during the month, which will not be needed until later in the year. In addition, Treasury deposits at Federal Reserve Banks typically rise after midmonth tax dates, such as that of June 15.

In response to the increase in money market rates in May, most banks raised their lending rate to prime customers by ½ percentage point to 7¼ percent during the first half of June. Business loan demand appeared to be starting its long-awaited revival, as loans at weekly reporting banks rose in late May and early June. Data in subsequent weeks did not confirm the stronger loan activity, however. Commercial and industrial loans at all weekly reporting banks, including loans sold to affiliates, declined on a seasonally adjusted basis by $275 million over

Chart I

SELECTED INTEREST RATES

April-June 1976



Note: Data are shown for business days only.

MONEY MARKET RATES QUOTED: Prime commercial loan rate at most major banks; 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.

the five statement weeks ended June 30.

Following the temporarily rapid growth rates of the monetary aggregates observed in late April and early May, M_1 declined slightly in June while M_2 posted a modest increase. The pace of monetary growth over longer horizons remained moderate, however. Averaged over the four-week period ended June 30, seasonally adjusted M_1—private demand deposits adjusted plus currency outside banks—increased at an annual rate of 6.3 percent over its four-week average in the period ended thirteen weeks earlier (see Chart II). This brought the M_1 growth rate of 4.0 percent over the four-week average ended fifty-two weeks earlier. Averaged over the four-week period ended June 30, M_2—M_1 plus commercial bank time and savings deposits other than large negotiable CDs—grew at an annual rate of 9.9 percent over its four-week average ended thirteen weeks earlier and at 9.0 percent over its four-week average ended fifty-two weeks earlier. Combined with member bank deposit growth, the recent increase in CDs pulled the bank credit proxy average to 5.2 percent and 3.2 percent at annual rates over average levels thirteen and fifty-two weeks earlier, respectively.

THE GOVERNMENT SECURITIES MARKET

The Treasury redeemed part of its maturing bills and borrowed new cash through coupon securities during June. This reflected a continuation of its efforts to reduce its short-term debt and to increase its longer term debt. For example, at auctions held between April 1 and June 30, the Treasury permitted a net $4.4 billion decline in three- and six-month bills while its outstanding debt rose by $0.6 billion.

Treasury bill rates declined somewhat during June, as investors came to believe that further firming in short-term credit markets was unlikely in the near future. At the regular weekly auction on June 28, three- and six-month bills were issued at average rates of 5.37 percent and 5.75 percent, respectively (see Table II), down about 20 basis points below the final auction of the previous month. On June 23, 52-week bills were sold at an average return of 6.08 percent, 23 basis points below the average issuing rate on May 26. Rates on most bill issues ended the month about 10 to 25 basis points below levels prevailing at the end of May.

In the market for coupon-bearing Government obligations, the Treasury borrowed additional funds, totaling $5 billion in three separate note auctions. On June 3, $2 billion of new cash was obtained through 49-month notes at an average issuing yield of 7.71 percent. On June 21, two-year notes with an average return of 6.99 percent were sold to refund $2 billion of maturing notes and to borrow $500 million of new cash. On June 29, an average issuing rate of 7.63 percent resulted from the auction of $2.5 billion of five-year notes for new money.

Some price improvements on seasoned issues were recorded in the Federal agency market, where new issue activity was light. On June 8, the Government National Mortgage Association auctioned $285.5 million of 7¼ percent and 7½ percent mortgage-backed securities for new cash. The thirty-year issues were aggressively priced to yield 8.43 percent and 8.48 percent, respectively, on a corporate bond equivalent basis. On June 23, the Federal National Mortgage Association issued $300 million of ten-year debentures priced at par to yield 7.95 percent. The Farm Credit System placed $1.4 billion of securities on June 17 to raise $292 million in new cash. The issue was composed of $615 million of 6.15 percent Banks for Cooperatives bonds due January 1977 and $789 million of 6.50 percent Federal Intermediate Credit Bank bonds due April 1977. Government-backed tax-exempt urban renewal and public housing notes totaling $580 million were sold through the Department of Housing and Urban Development on June 16. These short-term notes of eighty-six local public housing agencies were placed at an average yield of 3.28 percent, compared with a 3.47 percent rate in a similar offering on May 18.

Table 1

FACTORS TENDING TO INCREASE OR DECREASE MEMBER BANK RESERVES, JUNE 1976

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

Factors	Changes in daily averages—week ended					Net changes
	June 2	June 9	June 16	June 23	June 30	
"Market" factors						
Member bank required reserves	+ 151	+ 165	— 199	— 365	— 562	— 810
Operating transactions (subtotal)	+1,003	+4,859	—2,419	—4,058	—3,214	—3,829
Federal Reserve float	+ 40	+1,040	— 409	+ 8	— 283	+ 396
Treasury operations*	+1,287	+3,845	—1,092	—4,280	—3,434	—3,674
Gold and foreign account	— 44	+ 20	— 6	+ 32	+ 92	+ 94
Currency outside banks	— 162	— 450	— 422	+ 21	+ 586	— 427
Other Federal Reserve liabilities and capital	— 121	+ 407	— 491	+ 162	— 175	— 218
Total "market" factors	+1,154	+5,024	—2,618	—4,423	—3,776	—4,639
Direct Federal Reserve credit transactions						
Open market operations (subtotal)	—1,077	—5,334	+2,865	+3,700	+4,335	+4,489
Outright holdings:						
Treasury securities	— 881	—2,941	+2,580	+2,132	+1,844	+2,734
Bankers' acceptances	— 13	— 12	— 17	— 18	— 17	— 77
Federal agency obligations	— 14	—	— 22	—	—	— 36
Repurchase agreements:						
Treasury securities	— 68	—1,995	+ 276	+1,093	+2,242	+1,548
Bankers' acceptances	— 72	— 292	+ 40	+ 370	+ 210	+ 256
Federal agency obligations	— 29	— 94	+ 8	+ 123	+ 56	+ 64
Member bank borrowings	+ 107	— 149	— 45	+ 116	+ 2	+ 31
Seasonal borrowings†	+ 6	— 5	+ 4	+ 6	+ 7	+ 18
Other Federal Reserve assets‡	+ 55	+ 4	+ 451	— 159	+ 56	+ 407
Total	— 915	—5,479	+3,271	+3,657	+4,393	+4,927
Excess reserves‡§	+ 239	— 455	+ 653	— 766	+ 617	+ 288

	Daily average levels					Monthly averages‖
Member bank:						
Total reserves, including vault cash‡§	33,777	33,155	34,011	33,610	34,789	33,868
Required reserves	33,363	33,198	33,397	33,762	34,324	33,609
Excess reserves§	414	— 43	614	— 152	465	260
Total borrowings	242	93	48	164	166	143
Seasonal borrowings†	17	12	16	22	29	19
Nonborrowed reserves	33,535	33,062	33,963	33,446	34,623	33,726
Net carry-over, excess or deficit (—)¶	56	197	36	220	— 12	99

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 waivers of penalties for reserve deficiencies in accordance with the Regulation D change effective November 19, 1975.
‖ Average for five weeks ended June 30, 1976.
¶ Not reflected in data above.

OTHER SECURITIES MARKETS

Yields in the corporate and municipal bond markets also halted the upward movement of the previous month and partly retraced their earlier increases. Sentiment was buoyed by the stabilization in short-term money market conditions. While a substantial volume of new corporate issues, including obligations of many finance companies, was distributed easily during June, aggressive pricing on large issues late in the month met strong investor resistance. After a relatively heavy schedule of new state and local issues through the first half of June, the calendar of tax-exempt financings diminished considerably, taking some pressure off that sector.

In corporate underwriting, the largest industrial offering was $125 million of thirty-year debentures at midmonth. The Aa-rated debt was well received at a yield of 8.57 percent. Mixed receptions were accorded to a number of new utility issues during the month. Investors quickly purchased $200 million of Aaa-rated telephone debentures due in forty years at an 8.68 percent yield. However, an Aaa/AA-rated (Moody's/Standard & Poor's) telephone issue met stiff resistance when the $300 million 39-year debentures were priced to return 8.85 percent, a somewhat lower rate than had been expected. The return required on electric utility bonds was indicated by two thirty-year financings during the month. An Aa-rated $80 million issue carried a 9.00 percent yield, while an A-rated $125 million offering provided investors with a 9.22 percent return. In recent months, yield differentials on utilities with different ratings have continued to narrow.

At the beginning of June, the result of increases in municipal rates over the previous month required the State of Maryland to provide yields of from 4.25 percent in 1979 to 6.00 percent in 1991 on $175 million of Aaa-rated securities, 25 to 40 basis points higher than those attached to a comparably rated issue sold a month earlier. Later in June, the State of Wisconsin offered $120 million of Aaa-rated bonds, returning from 3.20 percent in 1977 to 6.00 percent in 2006. These bonds, offered at considerably lower yields on comparable maturities, were successfully distributed after some initial investor resistance. Rate declines over the month were similarly indicated by The Bond Buyer index of twenty bond yields on twenty-year tax-exempt bonds, which closed the month at 6.87 percent, down 16 basis points over the period. The Blue List of dealers' advertised inventories rose by $35 million to close the month at $860 million, reflecting the heavy volume of municipal financing.

Table II

AVERAGE ISSUING RATES AT REGULAR TREASURY BILL AUCTIONS*

In percent

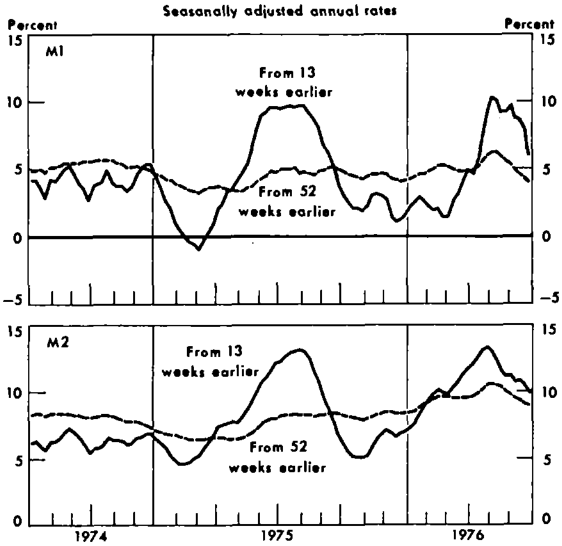
Maturity	Weekly auction dates—June 1976			
	June 7	June 14	June 21	June 28
Three-month	5.459	5.380	5.356	5.368
Six-month	5.768	5.695	5.722	5.754
	Monthly auction dates—April-June 1976			
	April 29	May 26	June 23	
Fifty-two weeks	5.645	6.309	6.081	

* 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

GROWTH OF SELECTED MONEY STOCK MEASURES

Seasonally adjusted annual rates



Note: Growth rates are computed on the basis of four-week averages of daily figures for periods ended in the statement week plotted, 13 weeks earlier and 52 weeks earlier. The latest statement week plotted is June 30, 1976.

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

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

Source: Board of Governors of the Federal Reserve System.