The Money Market in May

A steadily firm tone was evident in the money market in May. Average member bank borrowing from the Federal Reserve Banks was somewhat higher than in April, although it remained within the range of other recent months. The reserve positions of the major money market banks—which had been relatively comfortable around the end of April following large Treasury redeposits of tax receipts in Class C bank Tax and Loan Accounts—came under increased pressure during much of the month, as Treasury balances at these banks were drawn down. Toward the close of the month, however, these pressures diminished. Almost all trading in Federal funds was at 3½ per cent, while rates posted by the major New York City banks on new and renewal call loans to Government securities dealers were predominantly in a 3¾ to 4 per cent range. Offering rates for new time certificates of deposit issued by the leading New York City banks generally changed little, although some banks at times raised their rates temporarily to add to, or retain, their deposits. The range of rates within which such certificates traded in the secondary market rose somewhat during the month. Rates on other leading short-term money market instruments were largely unchanged until the closing days of the month, when rates on various maturities of directly placed finance company paper and commercial paper were increased by ⅛ of a per cent. Treasury bill rates moved narrowly in May, with rates on shorter maturities tending to rise and those on longer maturities tending to decline.

In the market for Treasury notes and bonds, prices moved higher during the first half of May as the success of the Treasury's May refunding and statements of officials strengthened market confidence in the likelihood of near-term stability of interest rates. Around midmonth, prices of intermediate-term issues declined slightly while longer term obligations edged upward irregularly; in the latter part of the month, prices rose once again in most maturity areas. Prices of seasoned corporate and tax-exempt bonds held steady at the beginning of May, and then rose modestly before steadying again toward the end of the month.

BANK RESERVES

Market factors absorbed excess reserves on balance from the last statement period in April through the final statement week in May. Member banks lost reserves, primarily as a result of a seasonal expansion in currency outside banks and through the effects of a routine Treasury interest payment to System Account.

System open market operations provided reserves over the period as a whole, partly offsetting reserves absorbed by market factors. System outright holdings of Government securities rose on average by $834 million from the last statement period in April through the final statement week in May, while System holdings of Government securities under repurchase agreements fell by $81 million. System net holdings of bankers' acceptances declined by $31 million. From Wednesday, April 29, through Wednesday, May 27, System holdings of Government securities maturing in less than one year contracted by $1,302 million, while holdings maturing in more than one year expanded by $2,185 million; this shift largely reflected the effects of the Treasury's May refunding operation and the passage of time.

CHANGES IN FACTORS TENDING TO INCREASE OR DECREASE MEMBER BANK RESERVES, MAY 1964

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

Factor	Daily averages—week ended May 6	May 13	May 20	May 27	Net changes
Operating transactions					
Treasury operations*	+ 41	— 108	— 29	+ 88	— 2
Federal Reserve float	— 119	— 13	+ 424	— 326	— 33
Currency in circulation	— 95	— 242	— 4	+ 31	— 310
Gold and foreign account	— 15	— 4	+ 16	+ 12	+ 9
Other deposits, and other Federal Reserve accounts (net)†	+ 10	+ 24	— 255	— 51	— 272
Total	— 179	— 339	+ 154	— 245	— 609
Direct Federal Reserve credit transactions					
Open market operations					
Purchases or sales‡					
Government securities	+ 595	+ 324	— 159	+ 104	+ 834
Bankers' acceptances	—	— 2	— 1	— 1	— 4
Repurchase agreements					
Government securities	+ 82	— 100	— 49	— 14	— 81
Bankers' acceptances	+ 7	— 14	— 9	— 11	— 27
Member bank borrowings	+ 76	+ 103	— 16	— 90	+ 73
Other loans, discounts, and advances	—	— 2	—	+ 1	— 1
Total	+ 759	+ 310	— 285	— 10	+ 794
Member bank reserves					
With Federal Reserve Banks	+ 590	— 29	— 111	— 255	+ 185
Cash allowed as reserves§	— 260	+ 45	+ 121	+ 65	— 35
Total reserves§	+ 311	+ 16	+ 10	— 187	+ 150
Effect of change in required reserves§	— 290	+ 96	— 4	+ 114	— 84
Excess reserves§	+ 21	+ 112	+ 6	— 73	+ 66
Daily average level of member bank:					
Borrowings from Reserve Banks	211	314	298	208	258‖
Excess reserves§	289	401	407	334	358‖
Free reserves§	78	87	109	126	100‖

Note: Because of rounding, figures do not necessarily add to totals.
* Includes changes in Treasury currency and cash.
† Includes assets denominated in foreign currencies.
‡ May also include redemptions.
§ These figures are estimated.
‖ Average for four weeks ended May 27, 1964.

THE GOVERNMENT SECURITIES MARKET

The market for Treasury notes and bonds was bolstered in May by the favorable reception accorded the Treasury's refunding operation[1] and by optimism regarding the prospects for the short-run stability of interest rates. During the early part of the month, trading activity in the May refunding issues strongly favored the newly offered 4¼ per cent bonds of 1974, which attracted a good demand from investors. Offerings of "rights"—the maturing issues eligible for exchange—were modest and were readily absorbed by investor and professional demand. On May 15, the settlement date for the refunding, approximately $10.1 billion of the $10.6 billion of the maturing notes and certificates eligible for conversion was exchanged for the two issues which had been offered by the Treasury. Subscriptions for the new 4 per cent notes of November 1965 and for the new 4¼ per cent bonds of May 1974 totaled $8.6 billion and $1.5 billion, respectively. Approximately $0.5 billion of the three maturing issues (or about 12.6 per cent of the $4.2 billion held by the public) was redeemed for cash. Since the maturing securities were unusually widely dispersed among many types of holders, the rate of attrition was not considered high and actually fell somewhat short of earlier market expectations.

Prices of outstanding notes and bonds rose irregularly in fairly active trading during the first half of May. Growing confidence in current interest rate levels—following statements by officials that, in view of prevailing supply and demand factors, there seemed to be no immediate prospect for higher interest rates—prompted an increase in professional short-covering operations and stimulated investment demand as well. Buying favored the 2½ per cent wartime issues and the new 4¼ per cent bonds but moderate offerings of other outstanding issues, which arose partly on swaps into the new bonds, were also quickly absorbed. In the longer term sector, offerings were light, and prices continued to move irregularly higher in response to a continuing demand from investors and a limited market supply. Around midmonth, some hesitancy developed and prices of intermediate issues receded a bit, as demand tapered off and higher price levels prompted professional offerings. This reaction was short-lived, however, and during the latter part of May the market tone once again strengthened, in part because of increased public fund interest in intermediate maturities. At the close of the month, prices of short- and intermediate-term Treasury notes and bonds

[1] The terms of this refunding, announced late in April, were discussed in last month's *Review*, p. 86.

were generally $\frac{6}{32}$ to $\frac{13}{32}$ above end-of-April levels, while longer term obligations were $\frac{10}{32}$ to $\frac{20}{32}$ higher.

In the market for Treasury bills, rates fluctuated narrowly over much of the month in a range slightly above the lower rate levels prevailing toward the end of April. At the beginning of May, reinvestment demand for bills from sellers of rights to the Treasury's refunding fell short of market expectations, and bill rates edged higher since demand from other sources was also relatively limited. As confidence in the current structure of interest rates became more widespread, however, both investor and professional demand increased considerably. Scarcities began to develop in some maturity areas, and bill rates generally receded from May 6 through midmonth. In the latter part of the month, activity contracted somewhat and only small mixed changes in rates on outstanding bills occurred. The Treasury's decision to add $100 million to the six-month bills sold in each of the last two regular weekly auctions of the month had little impact on the market. Rates on most outstanding bills were 1 basis point higher to 9 basis points lower on balance during the month, while the yield spread between three- and six-month bills declined to 12 basis points.

At the last regular weekly auction of the month held on May 25, average issuing rates were 3.475 per cent for the new three-month issue and 3.595 per cent for the new six-month bill—3 basis points higher and 2 basis points lower, respectively, than the rates of the final auction in April. The May 27 auction of $1 billion of new one-year bills resulted in an average issuing rate of 3.719 per cent, compared with an average issuing rate of 3.705 per cent on the comparable issue sold in April. The newest outstanding three-month bill closed the month at 3.47 per cent (bid), as against 3.45 per cent at the end of April, while the newest outstanding six-month bill was quoted at 3.59 per cent (bid) on May 28 (the final business day of the period), unchanged from April 30.

OTHER SECURITIES MARKETS

A confident tone emerged in the markets for corporate and tax-exempt bonds in early May, largely in reaction to the same factors that strengthened the Government securities market during this period. Prices of seasoned corporate and tax-exempt bonds held generally steady, although heavy previously accumulated dealer inventories of new bonds prompted several syndicate terminations. The price concessions that resulted on several recent issues rekindled investor interest, thus facilitating the placement of unsold balances. At the same time, the tax-exempt sector was encouraged by the contracting calendar of scheduled state and local flotations. In the latter part of May, a number of new corporate bond offerings moved slowly, as investors resisted the lower reoffering yields resulting from aggressive underwriter bidding. The tax-exempt market closed with prices firm, partly because of the moderate near-term calendar. Over the month as a whole, the average yield on Moody's seasoned Aaa-rated corporate bonds was unchanged at 4.41 per cent, while the average yield on similarly rated tax-exempt bonds declined by 4 basis points to 3.08 per cent. (These indexes are based on only a limited number of issues.)

The volume of new corporate bonds floated in May amounted to approximately $470 million, compared with $375 million in the preceding month and $535 million in May 1963. The largest new corporate bond issue marketed during the month consisted of $100 million A-rated (Standard and Poor's) 4⅝ per cent finance company debentures maturing in 1989 and not redeemable for eight years. Offered to yield 4.675 per cent, the debentures were accorded a good investor reception. New tax-exempt flotations in May totaled approximately $625 million, as against $1,125 million in April 1964 and $830 million in May 1963. The Blue List of tax-exempt securities advertised for sale declined slightly by $3 million during the month to $594 million on May 28, the final business day of the period. The largest new tax-exempt bond issue during the period was a $100 million state flotation, consisting of $50 million of school building bonds reoffered to yield from 2.25 per cent in 1966 to 3.40 per cent in 1988 and $50 million of water development bonds reoffered to yield from 2.95 per cent in 1974 to 3.625 per cent in 2013. Both offerings were Aa-rated (Moody's) and were well received by investors. Other new corporate and tax-exempt issues marketed in May were accorded mixed receptions by investors.