The Money and Bond Markets in July

The money market was generally firm throughout July, though the degree of firmness was somewhat greater in the first half of the month than in the second. Federal funds traded predominantly at 4⅛ per cent, with small amounts trading as high as 4¼ per cent in the early part of the period. At the same time, member bank borrowings from the Reserve Banks ranged around $600 million. Later, Federal funds traded as often at 4 per cent as at 4⅛ per cent, and member bank borrowings receded. Treasury bill rates rose until around midmonth, as the high cost of financing inventories led to increased professional offerings of bills. Thereafter, bill rates declined in response to a good investment demand and an increased willingness of dealers to hold inventories with the approach of the Treasury's August refinancing.

Prices of Treasury notes and bonds fluctuated in a narrow range during the month. Activity was light, and the atmosphere was cautious. Investment interest was dampened by a sizable flow of corporate offerings and by the proximity of the Treasury's refinancing of August maturies, announced after the close of business on Wednesday, July 28.

In the corporate bond market, prices were initially firm in the wake of the successful distribution of a very large volume of new issues in June. Subsequently, the sizable flow of new corporate bonds offered in July encountered mixed receptions, and reoffering yields on issues marketed late in the month were slightly above June levels. In the tax-exempt market, demand picked up and dealers were able to work down their inventories despite large offerings of new issues.

THE MONEY MARKET AND BANK RESERVES

Nationwide net reserve availability and member bank borrowings fluctuated somewhat more widely on a week-to-week basis during July than in other recent months, but the over-all tone of the money market remained generally firm. Federal funds traded mainly at 4⅛ per cent through the first half of the month, and on occasion there was some trading at 4¼ per cent. During the second half of the month, however, it was as common for Federal funds to trade at 4 per cent or below as at 4⅛ per cent (see left-hand panel of the chart on page 163). Rates quoted by major New York City banks on new call loans to Government securities dealers were predominantly in a 4⅜ to 4⅝ per cent range through the middle of July, while rates on renewal call loans were quoted most frequently in the 4⅜ to 4½ per cent range—in both cases about ⅛ of a percentage point higher than the range of such rates quoted in other recent months. After midmonth, rates dropped back to a predominant range of 4¼ to 4½ per cent on new loans and of 4¼ to 4⅜ per cent on renewals. Offering rates for new time certificates of deposit issued by leading New York City banks were essentially unchanged over the month. On July 1, the major finance companies lowered their offering rates of 30- to 89-day directly placed paper by ⅛ of a percentage point to 4⅛ per cent. Their offering rates on 90- to 270-day paper, however, were maintained at 4¼ per cent. Rates on bankers' acceptances were reduced by ⅛ of a percentage point late in the month, as dealer inventories of acceptances dropped to relatively low levels. The new rates on 90-day prime acceptances were set at 4¼ per cent bid-4⅛ per cent offered.

At the beginning of the month, banks in the central money market were under substantial reserve pressure. In part, this pressure reflected heavy demands for loans by Government securities dealers whose inventories were swollen by allotments of the June one-year bill as well as by bills which had been pressed on the market by commercial banks following the midyear bank statement date. At the same time, banks sought to avoid accumulating large reserve deficiencies over the long Independence Day weekend. While Federal Reserve open market operations offset the bulk of the reserve drain stemming from the preholiday increase in currency in the hands of the nonbank public, Federal funds were in particularly strong demand at 4⅛ per cent. A small amount, however, traded at 4¼ per cent. Member bank borrowings from the Reserve Banks rose, but net reserve availability was changed little from the preceding week.

Over the middle two statement weeks of the month, there

Table I

CHANGES IN FACTORS TENDING TO INCREASE OR DECREASE MEMBER BANK RESERVES, JULY 1965

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

Factor	Daily averages—week ended July 7	July 14	July 21	July 28	Net changes
"Market" factors					
Member bank required reserves*	− 204	+ 244	+ 108	+ 196	+ 284
Operating transactions (subtotal)	− 536	− 76	+ 478	− 266	− 400
Federal Reserve float	+ 40	+ 166	+ 323	− 532	− 4
Treasury operations†	+ 245	− 278	− 62	+ 4	− 86
Gold and foreign account	− 293	+ 10	− 33	+ 12	− 298
Currency outside banks*	− 805	+ 52	+ 148	+ 228	− 382
Other Federal Reserve accounts (net)‡	+ 277	− 36	+ 100	+ 23	+ 370
Total "market" factors	− 800	+ 168	+ 586	− 70	− 116
Direct Federal Reserve credit transactions					
Open market instruments					
Outright holdings:					
Government securities	+ 310	− 63	− 221	+ 33	+ 59
Bankers' acceptances	—	− 1	− 2	− 2	− 5
Repurchase agreements:					
Government securities	+ 408	+ 46	− 485	+ 116	+ 84
Bankers' acceptances	+ 1	− 2	− 12	—	− 13
Member bank borrowings	+ 96	+ 38	− 195	+ 54	− 7
Other loans, discounts, and advances	− 2	− 9	− 1	− 2	− 14
Total	+ 813	+ 8	− 916	+ 198	+ 103
Excess reserves*	+ 13	+ 176	− 330	+ 128	− 13
Daily average level of member bank:					
Total reserves, including vault cash*	22,171	22,103	21,665	21,597	21,884§
Required reserves*	21,822	21,578	21,470	21,274	21,536§
Excess reserves*	349	525	195	328	348§
Borrowings	582	620	425	479	527§
Free reserves*	− 233	− 95	− 230	− 150	− 179§
Nonborrowed reserves*	21,589	21,483	21,240	21,118	21,358§

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 four weeks ended July 28, 1965.

was a marked divergence between statistical reserve availability and money market conditions. In the statement week ended July 14, there was a sharp increase in nationwide net reserve availability. "Country" banks, however, built up their excess reserves to an unusual degree in the first week of their new statement period, reducing the supply of Federal funds to the market. Consequently, the money market was quite firm, and member bank borrowings from the Reserve Banks rose to $620 million for the week. In contrast, the money market was distinctly less taut in the statement week ended July 21, even though net borrowed reserves rose to $230 million. Country banks—now in the second week of their settlement period—worked down their excess reserves to $142 million from $482 million in the previous week. At the same time there was an improvement in the basic reserve positions of the money center banks, and Federal funds traded in volume at both 4 per cent and 3¾ per cent after the weekend. Thus, even with the sharp drop in over-all net reserve availability, member bank borrowings from the Reserve Banks declined to $425 million.

The money market continued free of stress in the final statement week of the month. The major New York City banks developed a substantial reserve surplus, and there was a good flow of Federal funds at both 4⅛ per cent and 4 per cent. Member bank borrowings were also moderate at $479 million.

Over the month as a whole, "market" factors absorbed $116 million of reserves, while System open market operations provided $125 million. The weekly average of System outright holdings of Government securities rose by $59 million from the final statement week in June through the last week in July, and average System holdings of Government securities under repurchase agreements increased by $84 million. Average net System holdings of bankers' acceptances, both outright and under repurchase agreements declined by $18 million during the month. From Wednesday, June 30, through Wednes-

Table II

RESERVE POSITIONS OF MAJOR RESERVE CITY BANKS JULY 1965

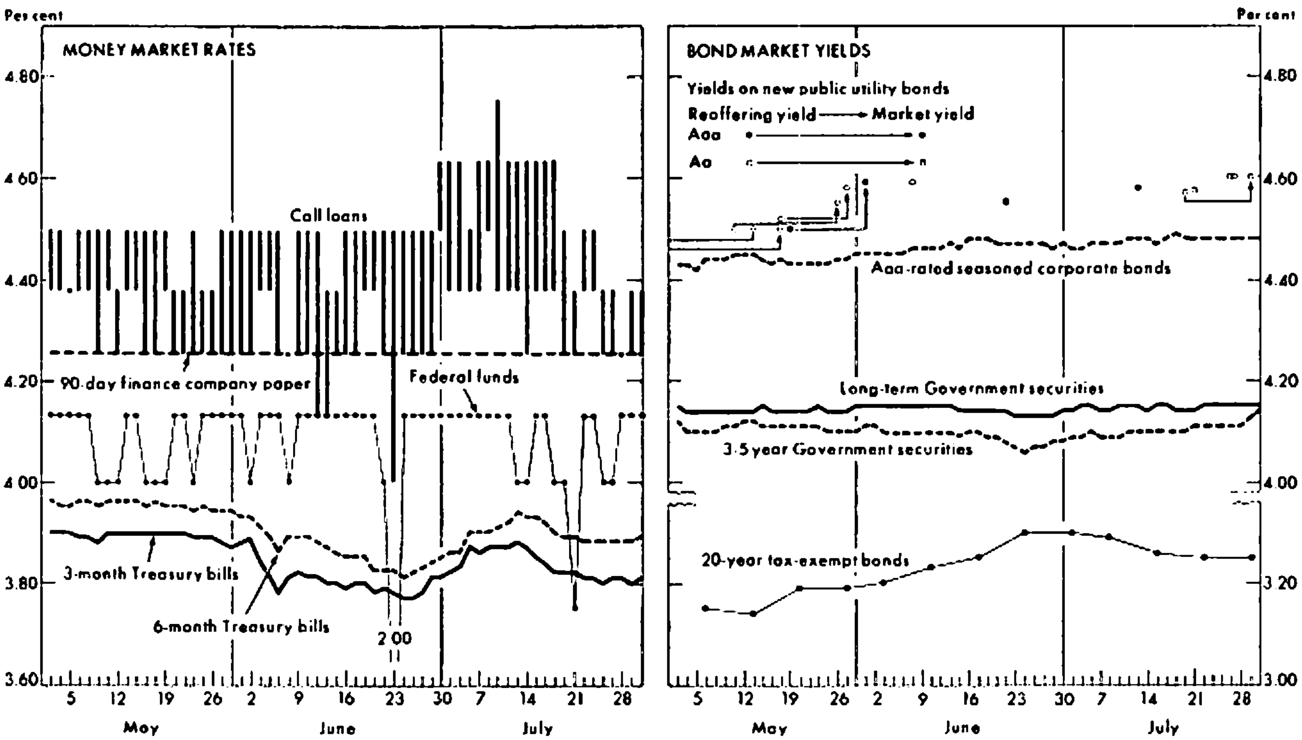
In millions of dollars

Factors affecting basic reserve positions	Daily averages—week ended July 7	July 14	July 21	July 28*	Average of four weeks ended July 28*
Eight banks in New York City					
Reserve excess or deficiency(−)†	23	6	15	13	14
Less borrowings from Reserve Banks	181	172	43	7	101
Less net interbank Federal funds purchases or sales(−)	338	481	244	− 429	159
Gross purchases	*930*	*922*	*866*	*660*	*845*
Gross sales	*592*	*441*	*622*	*1,089*	*686*
Equals net basic reserve surplus or deficit(−)	− 497	− 648	−272	435	−246
Net loans to Government securities dealers	929	654	696	479	690
Thirty-eight banks outside New York City					
Reserve excess or deficiency(−)†	18	15	13	− 3	11
Less borrowings from Reserve Banks	118	157	119	177	143
Less net interbank Federal funds purchases or sales(−)	512	670	756	581	630
Gross purchases	*1,293*	*1,227*	*1,324*	*1,240*	*1,271*
Gross sales	*781*	*556*	*568*	*658*	*641*
Equals net basic reserve surplus or deficit(−)	− 611	− 812	−862	−761	−762
Net loans to Government securities dealers	285	402	426	304	354

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.

SELECTED INTEREST RATES*

May-July 1965



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 of new Aaa- and Aa-rated public utility bonds are plotted around a line showing daily average yields of seasoned Aaa-rated corporate bonds (arrows point from underwriting syndicate reoffering yield of a given issue to market yield of the same issue immediately after it has been released from syndicate restrictions); daily averages of yields of 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 of 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.

day, July 28, System holdings of Government securities maturing in less than one year rose by $131 million, while holdings of issues maturing in more than one year remained unchanged.

THE GOVERNMENT SECURITIES MARKET

An atmosphere of caution prevailed in the market for Treasury bills during the first half of July. The taut money market conditions and associated high costs of inventory financing at the beginning of the period led to an expansion in professional offerings early in the month. The resulting upward movement in bill rates (see left-hand panel of the chart) was accelerated by sizable bill sales on the part of commercial banks following the June 30 statement date. Investment demand began to improve at the higher rate levels around midmonth, however, and as professional selling tapered off, a better atmosphere developed. At the same time, the more comfortable money market conditions after midmonth made it less expensive for dealers to finance their positions. In this environment, Treasury bill rates again moved lower—spurred in part by professional expectations that the Treasury's August financing would be likely to generate additional demand.

At the last regular weekly auction of the month, held on July 26, average issuing rates were 3.803 per cent for the new three-month issue and 3.873 per cent for the new six-month bills, about 2 and 5 basis points higher than the average issuing rates at the last weekly auction in June. The $1 billion of new one-year bills sold in the July 27 auction at an average issuing rate of 3.875 per cent, compared with 3.807 per cent for a comparable issue sold on June 24. A more hesitant tone developed in the wake of the July auction and persisted through the end of the month, as reinvestment demand from the refunding proved disappointing. The newest outstanding three- and six-month bills were bid at rates of 3.81 per cent and 3.89 per cent, respectively, at the close of the month.

In the market for Treasury notes and bonds, the downward drift in prices that had begun toward the end of June continued in early July as investor activity remained light. (The right-hand panel of the chart shows the rise in bond yields that accompanied this decline in prices.) A temporary firming in market tone appeared at the end of the first week, partly in response to press discussion regarding the tenability of the current interest rate levels and the improved atmosphere in the corporate bond market. Activity once again subsided, however, and buyers became more price conscious. A contributing factor to the renewed caution was the high volume of new corporate issues being marketed combined with the relatively wide rate differential between Government and corporate bonds. As the month progressed, market activity was further restrained by reports of a deterioration in the Vietnamese situation and by the approach of the Treasury's August refinancing. Discussion of the possibility that an intermediate issue might be offered led to declines, during July, of generally $\frac{5}{32}$ to $\frac{7}{32}$ in prices of issues maturing in two to five years. Prices of most longer issues also closed lower over the month.

After the close of business on Wednesday, July 28, the Treasury announced that holders of \$7.3 billion of 3⅞ per cent notes maturing on August 13—about \$3.2 billion of which was publicly held—would have the opportunity to exchange their holdings for either new 4 per cent 18-month notes or reopened 4 per cent 3½-year bonds. The new 4 per cent notes, which will mature on February 15, 1967, were offered at 99.85 to yield about 4.10 per cent. The reopened 4 per cent bonds of February 15, 1969 were offered at 99.45 to yield about 4.17 per cent. Subscription books were open from August 2 through August 4, with payments for and delivery of the securities scheduled for August 13. While the terms of the financing were considered attractive, the trading activity that developed was only moderate, and prices tended to ease further after their initial adjustment to the refunding terms.

OTHER SECURITIES MARKETS

Attention in the markets for both corporate and tax-exempt securities in July was dominated by the substantial volume of new issues that were offered during the month. Activity in both markets was light at the beginning of the month as investors awaited the terms of the new issues, the major portion of which was scheduled to be offered later in the month. In the corporate market, a better tone emerged at the beginning of the month as the market assessed the successful sale of the preceding month's heavy volume of offerings. Subsequently, investors became selective, resisting efforts of underwriters to price new issues aggressively. This investor resistance restrained underwriter bidding and led to slightly higher yields on offerings late in the month. A \$150 million negotiated offering of the Baa-rated debentures of a leading merchandising chain was quickly sold out at a reoffering yield of 4.90 per cent in late July.

In the tax-exempt market, an element of caution prevailed early in the period, reflecting the slow sales of older issues and still sizable dealer inventories. Around mid-month, however, the demand for new offerings and for unsold balances of old offerings picked up substantially as commercial banks began to show renewed interest in tax-exempt securities. Later, investor interest became more selective, but dealers were able to hold down their inventories, despite the substantial supply of new issues coming into the market. Over the month as a whole, the average yield on Moody's seasoned Aaa-rated corporate bonds rose by 1 basis point to 4.48 per cent. During the same period, the average yield on *The Weekly Bond Buyer's* series for twenty seasoned tax-exempt issues (carrying ratings ranging from Aaa to Baa) declined by 5 basis points to 3.25 per cent. (These yield series are shown in the right-hand panel of the chart.)

The volume of new corporate bonds publicly floated in July amounted to an estimated \$535 million, compared with \$720 million in June 1965 and \$230 million in July 1964. The largest publicly offered new corporate bond issue of the month consisted of the offering—mentioned above—by a leading merchandising chain of \$150 million of 4⅞ per cent sinking fund debentures nonrefundable for five years and maturing in 1990. New tax-exempt flotations totaled about \$980 million, as against \$885 million in June 1965 and \$835 million in July 1964. The Blue List of tax-exempt securities advertised for sale closed the month at \$756 million, compared with \$834 million at the end of June. The largest new tax-exempt bond flotation during the month was a \$175 million municipal Baa-rated offering. It consisted of \$111 million of general purpose bonds reoffered to yield from 2.80 per cent in 1967 to 3.565 per cent in 1995 which were quickly sold, and \$64 million of bonds maturing in 1966-70. The latter were awarded at a net interest cost of 3.499 per cent, but reoffering was delayed pending settlement of a legal question.