The Money and Bond Markets in September

The money market was generally comfortable during September, with no significant pressures evident around the midmonth tax and dividend payment dates. Free reserves fluctuated in a range slightly higher than in August, and Federal funds traded at about 4 per cent throughout the month. The basic reserve positions of banks in leading money centers deteriorated sharply during the first half of the month. These banks, however, had little difficulty covering their reserve needs through the Federal funds market, and borrowings from the Federal Reserve System were relatively light. A large volume of negotiable certificates of deposit (C/D's) matured during September. In order to limit attrition of these funds, a number of banks increased offering rates for C/D's.

Continuing the pattern of recent months, the comfortable tone of the money market during September coincided with further increases in yields on capital market instruments. The month opened with prices of Treasury coupon issues buoyed by prospects of possible new peace feelers following the election in South Vietnam. However, the price situation quickly deteriorated after the Labor Day holiday (September 4), as apprehension grew that Treasury financing needs in the months ahead would be considerably larger than previously anticipated even with passage of the Administration's proposed surtax. Also, hopes faded for a near-term solution in Vietnam, and it appeared likely that a long automobile strike might create additional difficulty for the Administration's tax proposals. Treasury bill rates declined briefly early in the month, but then rose almost steadily until September 25, after which rates again declined. During the month, rates on some bills climbed to new 1967 peaks, while yields on long-term Treasury bonds exceeded last year's highs.

The market for corporate securities also began the month with an improved tone. The calendar of new offerings scheduled for September was lighter than in August, and there was good investment demand. Early in the month prices increased from their lows for the year, although receptions were mixed when dealers attempted to price new offerings more than slightly above previously accepted levels. During the last half of the month, corporate bond prices declined moderately as dealer inventories and the calendar of prospective new offerings mounted. Tax-exempt securities were under pressure throughout September, and underwriters generally had difficulty reducing inventories without deep price concessions. The prevailing caution was enhanced by a growing calendar of future issues.

BANK RESERVES AND THE MONEY MARKET

The money market remained generally comfortable in September: average nationwide free reserves were $274

Table I

FACTORS TENDING TO INCREASE OR DECREASE MEMBER BANK RESERVES, SEPTEMBER 1967

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

Factors	Changes in daily averages— week ended on Sept. 6	Sept. 13	Sept. 20	Sept. 27	Net changes
"Market" factors					
Member bank required reserves*	— 363	— 62	— 253	— 58	— 736
Operating transactions (subtotal)	— 7	+ 583	+ 400	— 543	+ 433
Federal Reserve float	+ 120	+ 134	+ 210	— 253	+ 206
Treasury operations†	+ 399	+ 520	— 151	— 560	+ 208
Gold and foreign account	— 48	+ 6	—	— 4	— 46
Currency outside banks*	— 524	— 64	+ 245	+ 272	— 71
Other Federal Reserve accounts (net)‡	+ 45	— 13	+ 97	+ 6	+ 135
Total "market" factors	— 370	+ 521	+ 147	— 601	— 303
Direct Federal Reserve credit transactions					
Open market instruments					
Outright holdings:					
Government securities	+ 351	— 459	— 86	+ 397	+ 203
Bankers' acceptances	— 2	— 6	— 3	— 5	— 16
Special certificates	—	+ 66	— 66	—	—
Repurchase agreements:					
Government securities	+ 87	— 87	—	—	—
Bankers' acceptances	—	—	—	+ 86	+ 86
Federal agency obligations	+ 6	— 6	—	—	—
Member bank borrowings	+ 33	— 9	+ 36	— 32	+ 28
Other loans, discounts, and advances	—	—	—	—	—
Total	+ 476	— 501	— 119	+ 446	+ 303
Excess reserves*	+ 106	+ 20	+ 28	— 155	— 1

	Daily average levels				
Member bank:					
Total reserves, including vault cash*	23,944	24,026	24,307	24,210	24,122§
Required reserves*	23,578	23,640	23,893	23,951	23,766§
Excess reserves*	366	386	414	259	356§
Borrowings	79	70	106	74	82§
Free reserves*	287	316	308	185	274§
Nonborrowed reserves*	23,865	23,956	24,201	24,136	24,040§

	Changes in Wednesday levels				
System Account holdings of Government securities maturing in:					
Less than one year	+ 840	—1,176	+ 170	+ 591	+ 425
More than one year	+ 52	—	—	+ 56	+ 108
Total	+ 892	—1,176	+ 170	+ 647	+ 533

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 September 27.

Table II

RESERVE POSITIONS OF MAJOR RESERVE CITY BANKS SEPTEMBER 1967

In millions of dollars

Factors affecting basic reserve positions	Daily averages—week ended on Sept. 6	Sept. 13	Sept. 20	Sept. 27*	Averages of four weeks ended on Sept. 27*
Eight banks in New York City					
Reserve excess or deficiency(—)†	23	16	18	2	15
Less borrowings from Reserve Banks	21	—	21	—	11
Less net interbank Federal funds purchases or sales(—)	282	876	671	70	475
Gross purchases	*1,144*	*1,360*	*1,355*	*1,008*	*1,217*
Gross sales	*862*	*485*	*684*	*938*	*742*
Equals net basic reserve surplus or deficit(—)	— 280	— 860	— 674	— 68	— 471
Net loans to Government securities dealers	1,069	1,168	1,020	776	1,008
Thirty-eight banks outside New York City					
Reserve excess or deficiency(—)†	36	27	7	— 21	12
Less borrowings from Reserve Banks	12	7	35	13	17
Less net interbank Federal funds purchases or sales(—)	397	908	1,095	1,019	855
Gross purchases	*1,792*	*2,214*	*2,241*	*2,257*	*2,126*
Gross sales	*1,395*	*1,306*	*1,146*	*1,238*	*1,271*
Equals net basic reserve surplus or deficit(—)	— 375	— 888	—1,123	—1,053	— 860
Net loans to Government securities dealers	571	794	893	803	765

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—September 1967 Sept. 1	Sept. 11	Sept. 18	Sept. 25
Three-month	4.324	4.360	4.490	4.629
Six-month	4.765	4.951	4.998	5.143

Maturities	Monthly auction dates—July-September 1967 July 25	August 24	September 26
Nine-month	5.164	5.098	5.145
One-year	5.150	5.100	5.124

* 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.

million, and average member bank borrowings from the Federal Reserve Banks were $82 million (see Table I). Federal funds continued to trade predominantly at 4 per cent, the level of the Federal Reserve discount rate. No significant pressures developed around the September 15 payment date for the quarterly instalment of corporate income taxes. Although loans extended by commercial banks rose substantially in the week ended on September 20, the advance was apparently no greater than expected, and investments also increased moderately during the week.

The basic reserve positions of the major money market banks deteriorated sharply during the first half of the month. The shift of reserves away from banks in the leading money centers reflected attrition of C/D's and Euro-dollar holdings, as well as sizable calls on Treasury Tax and Loan Accounts, at a time when loans to securities dealers were increasing. The reserve positions of the major banks in New York City improved after the September 15 corporate tax date, due largely to an inflow of Euro-dollars, an increase in Government deposits as corporate tax payments were credited to Treasury Tax and Loan Accounts, and a decline in lending to Government securities dealers. On the other hand, the basic reserve deficit of the major banks outside New York City continued to deepen through September 20 and, although there was some improvement toward the close of the month, the average deficit remained substantial (see Table II).

Approximately $5.1 billion, or one fourth, of the C/D's outstanding at weekly reporting banks matured in September. Of that total, more than $1.1 billion fell due on September 15 alone. In view of the heavy volume of maturing C/D's, several banks raised their offering rates and generally succeeded in replacing a substantial portion of their maturities. At the end of the month, the most often posted rates ranged from 4¼ per cent for the shortest maturities to 5⅜ per cent for certificates maturing in one year or longer. The corresponding rates a month earlier were 4⅛ per cent and 5¼ per cent, respectively. Rates on bankers' acceptances rose by ⅛ percentage point to 5 per cent during September.

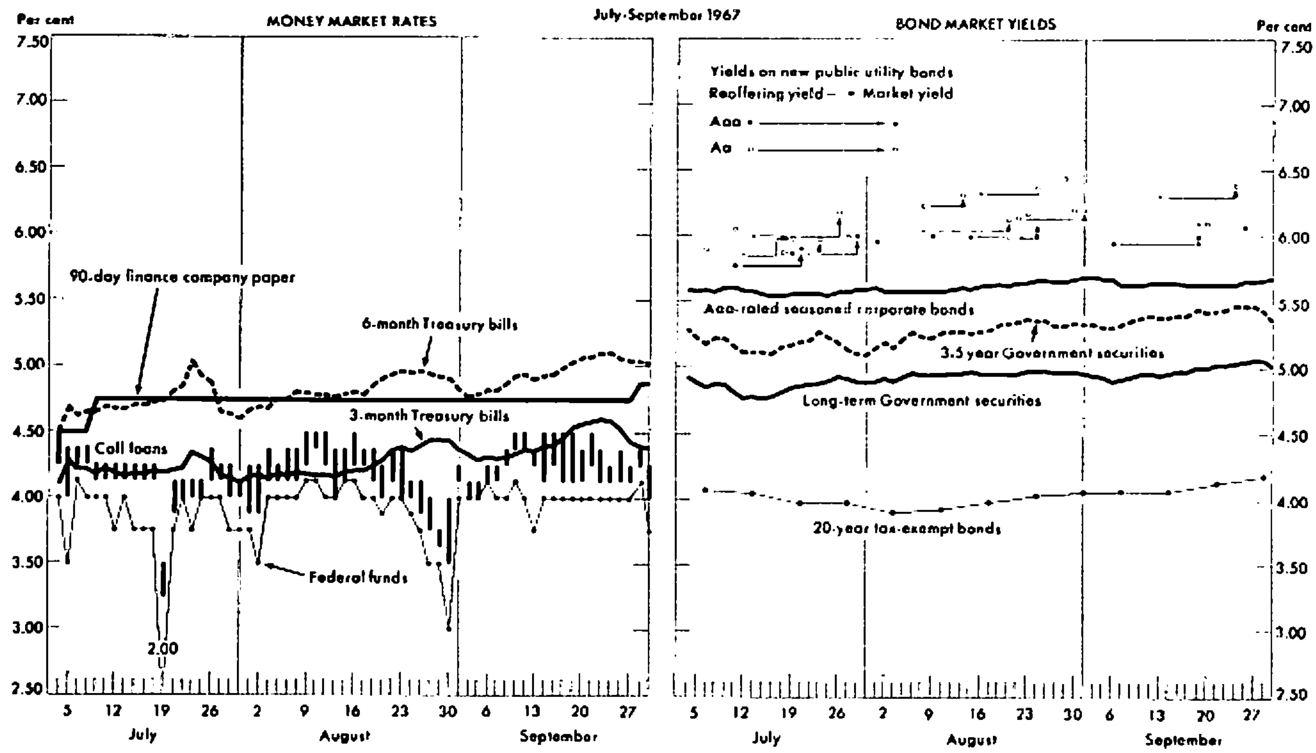
THE GOVERNMENT SECURITIES MARKET

A cautious atmosphere continued to pervade the Government securities market during September, and prices generally declined. Prior to the Labor Day holiday, however, prices of fixed income securities increased slightly as professional traders covered short positions and rebuilt inventories. Moreover, underlying investment sentiment was buoyed by an improved tone in the corporate bond market, the possibility of new peace efforts following the election in South Vietnam, and the prospect that a strike in the automobile industry might temporarily dampen economic activity. Reports of lagging loan demand also appeared to have a favorable impact on the market.

Market sentiment deteriorated after the holiday, however, and price declines during the second week wiped out almost all the increases of the preceding two weeks. The underlying tone became cautious and indecisive, as opinions differed concerning the probable length and economic impact of the automobile strike and its possible effect on passage of the Administration's tax proposals by the Congress. In addition, hopes faded for near-term peace in Vietnam and there was some discussion of the likelihood of a shift from ease in monetary policy, although most participants felt that no such change was imminent. In this environment, professional traders began to lighten inventories accumulated over the preceding two weeks, thereby further depressing prices. Prices of Treasury notes and bonds continued to drift lower as market participants considered the possibility that, even with the passage of the Administration's tax proposals, Treasury financing needs stemming from the expected large deficit would probably be appreciably greater than previously anticipated. By the end of the month, prices of many long-term Government bonds were below their lowest levels of last year, although prices of intermediate-term issues remained well above their 1966 lows.

The Treasury bill market began the month on a comparatively steady note, with dealers making fairly good sales at slightly lower rates. The Federal Reserve System entered the market to meet the reserve needs associated with the long holiday weekend, and there was good demand from the public and commercial banks. The market bid rate for three-month bills fell to 4.29 per cent at the end of the first week, about 10 basis points below the level in the final week of August (see chart). In subsequent days, however, the demand for bills abated, especially for shorter maturities, as dealers focused their attention on the possibility of an increased supply of bills to the market during the dividend and tax payment period. Treasury bill rates then continued to rise under investor selling and dealers' desire to prepare for the possibility that the Treasury might soon be entering the market to sell up to $5 billion of new tax anticipation bills. At the last regular weekly auction of the month on September 25, the average issuing rate for the new three-month bills was 4.629 per cent (see Table III), about 14 basis points higher than the average rate of the last regular auction in August and the highest auction rate since January 23, 1967. The average rate on the six-month issue was 5.143 per cent, about 15 basis points higher than that of the last auction in August and the highest since De-

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.

cember 5, 1966. Strong demand developed for Treasury bills at the higher rates, partly as commercial banks bought before the September 30 statement publishing date. As a consequence, bill rates fell sharply and the rates on three- and six-month bills closed the month at 4.39 per cent and 5.02 per cent, respectively.

On September 22, the Treasury announced plans to raise $4.5 billion of cash through the sale of tax anticipation bills maturing in April and June 1968. The bills were auctioned on Tuesday, October 3, for payment on Monday, October 9. Of the $4.5 billion total, $1.5 billion represented an additional offering of tax anticipation bills maturing on April 22, 1968, of which $2.0 billion was already outstanding. The remaining $3.0 billion comprised a new issue of tax anticipation bills maturing on June 24, 1968. The shorter maturities were sold at an average yield of 4.93 per cent, and the longer maturities yielded 5.11 per cent. Commercial banks were allowed to pay for 75 per cent of the bills allotted to themselves and their customers through credits to Treasury Tax and Loan Accounts. The Treasury also announced that it would continue adding $100 million each week to the weekly offerings of three-month bills through another full thirteen-week cycle. The previous cycle of $100 million weekly additions was completed with the bills paid for on October 5. Subsequent weekly offerings will consist of $1.5 billion of three-month bills and $1.0 billion of six-month bills.

Several new Government agency obligations were marketed during September. Among the larger issues, the Federal Home Loan Banks offered two $300 million issues on

Tuesday, September 12, to replace a $650 million maturity on September 27. The two issues were offered at yields of 5.45 per cent and 5.50 per cent for ten- and sixteen-month maturities, and both were trading at small premiums by the end of the week. Shortly after midmonth, the announcement by the Federal National Mortgage Association of a $400 million three-year debenture issue to be offered September 22 tended to depress the market, as it was a larger amount than the outstanding issue being refunded. However, at a yield of 5.82 per cent it was generally well received, although there were slight price declines in subsequent trading.

OTHER SECURITIES MARKETS

Many of the factors influencing the Government securities market early in the month also affected the corporate market, but perhaps of most immediate influence was the decline in the calendar of new issues scheduled for September to $860 million, still large but well below the average monthly volume floated publicly during the summer months. In this environment, Aa-rated utility issues with five years of special call protection, which had reached yields of 6.20 per cent or more during the last week of August, posted price advances during early September large enough to bring yields down to around 6.10 per cent. However, underwriters who bid aggressively for a sizable Aaa-rated telephone issue at the start of the month encountered considerable investor resistance at a reoffering yield of 5.95 per cent. This was roughly 12 basis points under the yield on a similar issue marketed the previous week and the lowest rate on this type of security since June. Only offerings which came out at yields around the levels of the preceding month tended to be well received. After midmonth, underwriters became increasingly concerned with their rather large unsold balances of recently marketed bonds; and, in view of the growing calendar of scheduled offerings, bidding turned cautious. An offering of $100 million Aaa-rated telephone debentures with five years of special call protection was priced to yield 6.06 per cent, 11 basis points higher than had been offered on the earlier telephone issue and the highest interest cost incurred by the company in over forty-five years. Nevertheless, the issue was accorded a poor reception, with lagging sales in part due to competition from sizable dealers' inventories of the earlier telephone issue. Other large corporate offerings toward the end of the month were mostly convertible issues and were generally accorded excellent receptions. The average yield on Moody's Aaa-rated seasoned corporate bonds was 5.68 per cent at the end of September, virtually unchanged from August.

The market for tax-exempt securities labored under pressure throughout most of the month, although some short-lived relief appeared during the second week as underwriters experienced a good distribution from their heaviest weekly schedule of new offerings since early in the year. To attract buyers, however, yields on new issues moved almost to the high levels reached in July, prior to the President's request for a tax surcharge. For most of the month, underwriters had difficulty reducing unsold balances of older issues without deep price concessions, and investor interest in new issues was only fair despite higher reoffering yields. The prevailing caution was further influenced by growing concern over the fate of the proposed tax surcharge. *The Weekly Bond Buyer's* average yield series for twenty seasoned tax-exempt bonds, carrying ratings from Aaa to Baa, rose to 4.19 per cent at the month end, from 4.06 per cent at the close of August (see chart). By the end of the month, the volume of tax-exempt issues advertised on the Blue List stood at $469 million, compared with $433 million at the end of August.