The Money and Bond Markets in February

Money market rates edged higher on balance during February, as nationwide net reserve availability contracted and member bank borrowings at the Reserve Banks increased. The effective rate for Federal funds was generally ⅛ percentage point higher than in January, and other short-term rates rebounded from late-January lows early in the month and rose irregularly thereafter. An outflow of funds from maturing certificates of deposit (C/D's) early in February was subsequently reversed, and short-term C/D rates remained below earlier ceiling levels, although some increases were posted in these maturities. The movement of yields in the Treasury bill sector was greatest in the six-month area, where rates moved up as much as 20 basis points, while three-month bills rose 14

Table I

FACTORS TENDING TO INCREASE OR DECREASE MEMBER BANK RESERVES, FEBRUARY 1968

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

Factors	Changes in daily averages—week ended on				Net changes
	Feb. 7	Feb. 14	Feb. 21	Feb. 28	
"Market" factors					
Member bank required reserves*	− 205	+ 537	+ 125	− 406	+ 61
Operating transactions (subtotal)	− 85	− 458	+ 519	+ 30	+ 12
Federal Reserve float	+ 2	− 164	+ 467	− 178	+ 107
Treasury operations†	+ 221	− 141	+ 34	+ 47	+ 161
Gold and foreign account	− 10	− 67	− 3	− 6	− 86
Currency outside banks*	− 441	− 109	+ 168	+ 188	− 194
Other Federal Reserve accounts (net)‡	+ 145	+ 42	− 148	− 15	+ 24
Total "market" factors	− 290	+ 79	+ 644	− 370	+ 63
Direct Federal Reserve credit transactions					
Open market instruments					
Outright holdings:					
Government securities	− 11	− 110	− 372	+ 281	− 212
Bankers' acceptances	− 2	+ 1	− 2	− 4	− 8
Repurchase agreements:					
Government securities	+ 380	− 23	− 391	—	− 34
Bankers' acceptances	− 25	+ 25	− 25	—	− 25
Federal agency obligations	+ 5	− 1	− 4	—	—
Member bank borrowings	—	+ 143	+ 21	+ 37	+ 201
Other loans, discounts, and advances	—	—	—	—	—
Total	+ 346	+ 34	− 773	+ 314	− 79
Excess reserves*	+ 56	+ 113	− 129	− 56	− 16
	Daily average levels				
Member bank:					
Total reserves, including vault cash*	25,953	25,529	25,275	25,625	25,595§
Required reserves*	25,575	25,038	24,913	25,319	25,211§
Excess reserves*	378	491	362	306	384§
Borrowings	241	384	405	442	368§
Free reserves*	137	107	− 43	− 136	16§
Nonborrowed reserves*	25,712	25,145	24,870	25,183	25,227§
	Changes in Wednesday levels				
System Account holdings of Government securities maturing in:					
Less than one year	+ 235	− 878	+7,697	+ 297	+7,351
More than one year	—	—	−7,658	—	−7,658
Total	+ 235	− 878	+ 39	+ 297	− 307

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 February 28.

Table II

RESERVE POSITIONS OF MAJOR RESERVE CITY BANKS FEBRUARY 1968

In millions of dollars

Factors affecting basic reserve positions	Daily averages—week ended on				Averages of four weeks ended on Feb. 28*
	Feb. 7	Feb. 14	Feb. 21	Feb. 28*	
Eight banks in New York City					
Reserve excess or deficiency(−)†	18	127	28	4	44
Less borrowings from Reserve Banks	1	144	131	119	99
Less net interbank Federal funds purchases or sales(−)	321	410	161	25	229
Gross purchases	*931*	*1,026*	*953*	*849*	*940*
Gross sales	*610*	*616*	*792*	*824*	*711*
Equals net basic reserve surplus or deficit(−)	− 304	− 427	− 264	− 140	− 284
Net loans to Government securities dealers	1,252	878	985	966	1,020
Thirty-eight banks outside New York City					
Reserve excess or deficiency(−)†	23	72	7	54	39
Less borrowings from Reserve Banks	54	67	110	75	77
Less net interbank Federal funds purchases or sales(−)	668	782	600	540	648
Gross purchases	*1,692*	*1,858*	*1,558*	*1,770*	*1,720*
Gross sales	*1,025*	*1,076*	*958*	*1,230*	*1,072*
Equals net basic reserve surplus or deficit(−)	− 698	− 778	− 703	− 561	− 685
Net loans to Government securities dealers	792	680	673	719	716

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—Feb. 1968			
	Feb. 5	Feb. 9	Feb. 19	Feb. 26
Three-month	4.957	5.040	4.940	5.063
Six-month	5.119	5.275	5.133	5.236

Maturities	Monthly auction dates—Dec. 1967-Feb. 1968		
	Dec. 26	Jan. 25	Feb. 21
Nine-month	5.555	5.254	5.239
One-year	5.544	5.267	5.281

* 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.

basis points over the month. The three-month Euro-dollar rate was generally quoted in a narrow range around 5.50 per cent.

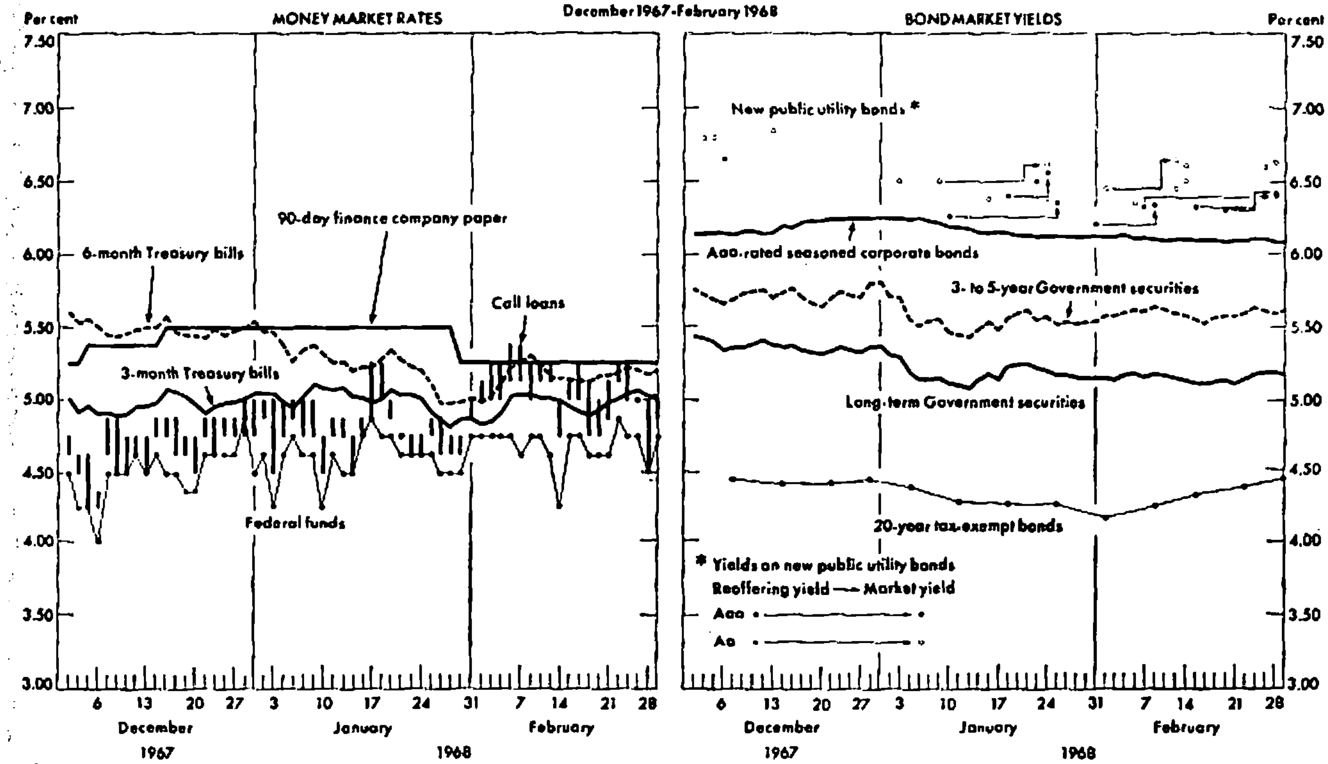
The principal feature of the markets for intermediate- and longer term securities was the Treasury exchange offering (including a prerefunding) involving a 5¾ per cent seven-year note and the subsequent cash offering of $4 billion of a 5⅝ per cent fifteen-month note. Both were well received. Federal agency offerings of $1.4 billion of short- and intermediate-term securities in mid- and late February were quite successful. Over the month, yields on coupon issues were generally steady to somewhat higher. Prices were supported by a growing conviction among market participants that capital market pressures arising from greater expenditures in the event of further escalation in Asia would be mitigated by stringent fiscal measures. In such an event, consensus born of crisis would be expected to offset the legislative stalemate now plaguing the proposed tax increase.

BANK RESERVES AND THE MONEY MARKET

On balance, money market rates were slightly higher in February than in January. The effective rate for Federal funds was generally 4¾ per cent, ⅛ percentage point above the most frequently prevailing rate a month earlier, and trading at 4⅞ per cent was not uncommon. Rates on commercial paper were generally unchanged during the month, but early in February rates on bankers' acceptances were raised ⅛ percentage point to 5¼ per cent (offered) and rates on 60- to 89-day finance company paper declined by a similar amount to 5⅛ per cent. Treasury bill rates

SELECTED INTEREST RATES

December 1967-February 1968



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.

rose sharply in early February from the lows of the previous month, and rates were fairly steady—particularly in shorter maturities—throughout the balance of the month. Increases early in the month, which generally ranged from 10 to 30 basis points, reflected adjustments in dealer positions emanating from smaller than anticipated reinvestment demand associated with the Treasury refunding operations and higher dealer financing costs. The principal increase in the cost of financing occurred in the first week, when rates quoted by New York City banks on call loans to Government securities dealers rose as much as ¼ percentage point. These rates fluctuated narrowly for the balance of the month.

At banks in New York City, rates posted on C/D's in the 90- to 179-day maturity range fluctuated mostly between 5⅛ per cent and 5½ per cent, ⅛ to ¼ percentage point higher than at the end of January. Rates for other maturities were generally steady: 60 to 89 days at 5 per cent and over 180 days at the 5½ per cent Regulation Q ceiling. Although on balance New York City banks experienced a decline in the volume of outstanding C/D's in February, much of this outflow was offset by gains in funds drawn from their own foreign branches. These funds, which are not subject to reserve requirements and deposit insurance assessments, became attractive as the three-month Euro-dollar rate declined about 1 percentage point during January and then stabilized between 5.40 per cent and 5.60 per cent for most of February. Indeed, the availability of these funds reduced upward pressure on domestic money market rates.

Aggregate daily average free reserves declined on balance during February, and borrowings from Federal Reserve Banks increased markedly after the first week. Although over the first two statement weeks free reserves were little changed from average January levels, there was a sharp contraction in the last two weeks, when net borrowed reserves averaged $43 million and $136 million, respectively (see Table I). The shift from free to net borrowed reserves during the third week was strongly influenced by a decline of $794 million (on a daily average basis) in System holdings of open market instruments, which more than offset an increase in float of $467 million.

"Country" banks were responsible for most of the gain in borrowings from Federal Reserve Banks in February, when their daily average borrowings reached the highest level since October 1966. Moreover, borrowings by New York City banks for the month were the largest in a year, and this resort to the discount window was evidence of increased money market pressure. Reserve stringency at reserve city banks mounted in the first half of February after some easing in the final two weeks of January. Although nationwide net reserve availability contracted in the last half of February, reserve distribution was more favorable to money market banks, particularly those in New York City, than earlier in the month (see Table II).

THE GOVERNMENT SECURITIES MARKET

Prices of Treasury notes and bonds fluctuated irregularly during February, and at the month end yields on both intermediate- and longer term coupon issues were little changed from levels a month earlier. In part, the firmness of prices during the month reflected an attitude that the worsening Asian situation would not significantly affect fixed-income securities. It was believed that an aggravation of hostilities which stimulated greater defense expenditures would at the same time result in the imposition of fiscal measures which would relieve market pressures.

Two sizable Treasury financing operations were conducted in February. In the first, a new 5¾ per cent seven-year note was offered in exchange for a maturing note and, as a prerefunding, for issues maturing in August and November 1968. Subscription books were open for three days beginning February 5. Although initial enthusiasm waned somewhat, the exchange was regarded as very successful. About 72 per cent of the $1.7 billion in February maturities held outside Federal Reserve and Government accounts was exchanged, and 25 per cent of the $10.3 billion in other maturities was tendered. On February 13 the Treasury received subscriptions for a $4 billion offering of a 5⅝ per cent fifteen-month note. Banks were allowed full Tax and Loan Account credit, and settlement was made on February 21. Allotments of 39 per cent on subscriptions in excess of $200,000 were within the range of market expectations, and the new note was generally quoted around par in subsequent trading.

Treasury bill rates moved higher in early February, influenced partially by higher dealer financing costs, which stimulated aggressive selling. Rates for bills due in two to six months rose from 6 to 22 basis points during the first week, while rates on longer maturities were only slightly higher. At the higher yield levels interest emerged at mid-month, when demand by banks and state funds—particularly for shorter maturities—moved rates lower. Rates rebounded somewhat thereafter as these influences abated, and there was little reaction to the expected Treasury announcement that an additional $100 million would be offered in the regular three-month bill auctions, probably for a full thirteen-week cycle. Interest in the monthly auction of nine- and twelve-month bills favored the shorter issue, and accepted bids covered a wide range of prices. The average issuing rates of 5.239 per cent and 5.281 per cent, respectively (see Table III), were little changed from those a month earlier.

Prices of Federal agency securities fluctuated narrowly during February. On February 14 the Federal Home Loan Banks offered $400 million of a 5.70 per cent note maturing on September 25, 1968 at par and $200 million in a 6 per cent note due March 25, 1970, priced at 100⅛. The next day the Federal Intermediate Credit Banks offered $453.5 million of a 5.75 per cent nine-month debenture at par. At the month end the Federal National Mortgage Association offered $350 million of a 6 per cent three-year debenture, priced to yield 6.02 per cent. All issues were very well received, and the earlier offerings subsequently traded at premiums.

OTHER SECURITIES MARKETS

Prices in the market for corporate bonds were generally steady throughout February, although some weakness developed toward the end of the month. While the volume of new offerings was light, investor resistance was fairly pervasive—especially to issues priced aggressively by underwriters. The successful conclusion of Treasury financing operations during the first half of the month did not trigger a renewal of demand for new issues, nor did the prospect of a relatively low volume of offerings in March stimulate buying. As a result, dealer inventories rose during the month. At the same time, spreads between new and seasoned high-grade issues were slightly wider on balance than during January (see chart). On February 28 four underwriting syndicates were disbanded, and unsold issues were released to trade at yields about 10 basis points higher than originally offered. The Moody index of yields on Aaa seasoned corporate bonds changed little during February and closed at 6.08 per cent.

Prices in the market for tax-exempt bonds drifted steadily lower during February. Late in the month the prospect of a revival in industrial revenue bond financing added further pressure to prices. Buying by commercial banks favored issues with short maturities. As a rule, longer maturities of new issues moved slowly throughout the month, and the Blue List of dealer-advertised inventories rose from $443.8 million at the end of January to $488.8 million a month later. This swing about offset the decline in inventories during January, and the resultant market congestion contributed to the postponement of a major offering scheduled for late February. Over the month, *The Weekly Bond Buyer's* series of twenty seasoned tax-exempt issues (carrying ratings from Aaa to Baa) rose by 19 basis points to 4.44 per cent, only slightly below the 1967 peak reached last December.