The Money and Bond Markets in March

Pressures intensified in the bond markets during the first two thirds of March, and yields on corporate and tax-exempt bonds and long-term Treasury coupon issues generally continued their ascent to record levels. Throughout this period, market participants focused attention upon the continuing policy of fiscal and monetary restraint. With no near-term relaxation in this policy expected and with bond yields rising steadily, investors became increasingly reluctant to commit their funds to longer term obligations. However, later in the month, bond market performance improved markedly amid rising hopes that progress was being made toward resolving the Vietnam conflict and as some participants came to the view that the record high yields, particularly on corporate bonds, might have been the product of an exaggerated pessimism regarding the outlook for interest rates. Throughout the month, a strong demand for Treasury bills prevailed and their rates generally declined. These debt instruments apparently served a time of great uncertainty as a haven for the liquid funds of a wide spectrum of investors. Special demands stemmed from the redemption of $2 billion of March tax anticipation bills as well as from the quarterly statement date and the April 1 Cook County, Illinois, tax date.

The banking system continued to experience a sharp runoff of large-denomination certificates of deposit (CD's) in March. To a considerable extent, banks compensated for funds lost in this way by sharply expanding their Euro-dollar borrowings, even at relatively high interest rates.

Market expectations were confirmed on March 17, when many of the nation's leading commercial banks raised their prime lending rate from 7 percent to 7½ percent—the fourth increase in this key rate since early December. The move triggered renewed market discussion of the possibility of new action in the pursuance of monetary restraint, including a potential increase in the Federal Reserve discount rate. These expectations were also confirmed on April 3 when the Board of Governors of the Federal Reserve System announced its approval of actions by eleven of the twelve Federal Reserve Banks raising the discount rate to 6 percent from 5½ percent. At the same time, the Board of Governors increased reserve requirements against demand deposits at all member banks by ½ percent-

Table I

FACTORS TENDING TO INCREASE OR DECREASE MEMBER BANK RESERVES, MARCH 1969

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

Factors	Changes in daily averages—week ended on				Net changes
	March 5	March 12	March 19	March 26	
"Market" factors					
Member bank required reserves	+ 115	+ 259	— 104	+ 269	+539
Operating transactions (subtotal)	— 4	— 264	— 78	— 161	— 507
Federal Reserve float	— 184	— 132	+ 142	— 226	— 350
Treasury operations*	+ 36	+ 97	— 20	— 116	— 8
Gold and foreign account	+ 4	— 31	— 5	— 4	— 36
Currency outside banks	+ 163	— 225	— 424	+ 84	— 402
Other Federal Reserve accounts (net)†	— 73	+ 28	+ 227	+ 101	+ 283
Total "market" factors	+ 111	— 5	— 182	+ 108	+ 32
Direct Federal Reserve credit transactions					
Open market instruments					
Outright holdings:					
Government securities	— 69	— 15	— 41	— 98	— 223
Bankers' acceptances	— 1	— 1	— 1	— 2	— 5
Repurchase agreements:					
Government securities	+ 6	— 72	+ 146	— 11	+ 69
Bankers' acceptances	— 35	— 12	+ 31	— 9	— 25
Federal agency obligations	+ 2	— 7	+ 9	+ 2	+ 6
Member bank borrowings	— 24	+ 138	— 97	+ 188	+ 205
Other loans, discounts, and advances	—	—	—	—	—
Total	— 120	+ 31	+ 45	+ 70	+ 26
Excess reserves	— 9	+ 26	— 137	+ 178	+ 58
	Daily average levels				
Member bank:					
Total reserves, including vault cash	26,950	26,717	26,684	26,593	26,736‡
Required reserves	26,783	26,524	26,628	26,359	26,574‡
Excess reserves	167	193	56	234	162‡
Borrowings	734	872	775	963	836‡
Free, or net borrowed (—), reserves	— 567	— 679	— 719	— 729	— 674‡
Nonborrowed reserves	20,216	25,845	25,909	25,630	25,900‡
Net carry-over, excess or deficit (—)§	145	96	123	36	100‡
	Changes in Wednesday levels				
System account holdings of Government securities maturing in:					
Less than one year	+ 129	— 154	+544	+ 4	+ 523
More than one year	—	+ 75	— 530	—	— 455
Total	+ 129	— 79	+ 14	+ 4	+ 68

Note: Because of rounding, figures do not necessarily add to totals.
* Includes changes in Treasury currency and cash.
† Includes assets denominated in foreign currencies.
‡ Average for four weeks ended on March 26, 1969.
§ Not reflected in data above.

Table II

RESERVE POSITIONS OF MAJOR RESERVE CITY BANKS MARCH 1969

In millions of dollars

Factors affecting basic reserve positions	Daily averages—week ended on				Averages of four weeks ended on March 26
	March 5	March 12	March 19	March 26	
Eight banks in New York City					
Reserve excess or deficiency(—)*	— 34	66	— 91	85	7
Less borrowings from Reserve Banks	104	—	84	43	58
Less net interbank Federal funds purchases or sales(—)	420	1,049	301	469	560
Gross purchases	*1,693*	*1,960*	*1,631*	*1,650*	*1,734*
Gross sales	*1,273*	*911*	*1,330*	*1,182*	*1,174*
Equals net basic reserve surplus or deficit(—)	— 558	— 982	— 475	— 427	— 611
Net loans to Government securities dealers	538	451	407	440	459
Net carry-over, excess or deficit(—)†	51	— 11	43	— 46	9
Thirty-eight banks outside New York City					
Reserve excess or deficiency(—)*	2	— 3	—	12	3
Less borrowings from Reserve Banks	112	342	168	309	233
Less net interbank Federal funds purchases or sales(—)	918	1,222	1,633	1,186	1,240
Gross purchases	*2,991*	*3,163*	*3,442*	*3,030*	*3,157*
Gross sales	*2,073*	*1,941*	*1,809*	*1,845*	*1,917*
Equals net basic reserve surplus or deficit(—)	—1,028	—1,567	—1,802	—1,484	—1,470
Net loans to Government securities dealers	75	22	— 57	— 116	— 19
Net carry-over, excess or deficit(—)†	32	31	16	21	25

Note: Because of rounding, figures do not necessarily add to totals.
* Reserves held after all adjustments applicable to the reporting period less required reserves and carry-over reserve deficiencies.
† Not reflected in data above.

Table III

AVERAGE ISSUING RATES* AT REGULAR TREASURY BILL AUCTIONS

In percent

Maturities	Weekly auction dates—March 1969			
	March 3	March 10	March 17	March 24
Three-month	6.215	6.049	6.108	5.946
Six-month	6.342	6.233	6.221	6.096

Maturities	Monthly auction dates—January-March 1969		
	January 28	February 20	March 26
Nine-month	6.195	6.307	6.058
One-year	6.144	6.234	6.132

* 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.

age point. (For full details, see the statement of the Board of Governors reproduced in full on page 75 of this *Review*.)

The tone of the money market generally remained firm in March. Most Federal funds transactions were completed in a 6⅝ to 7 percent range. Average nationwide reserve availability fell by $65 million, and member bank borrowings at the Federal Reserve Banks averaged $836 million in March, unchanged from February.

BANK RESERVES AND THE MONEY MARKET

Although nationwide net reserve availability was little changed in early March from its late February range, pressure on reserve positions of banks in New York City increased somewhat—partly as a result of their expanded lending to Government securities dealers. On the other hand, the average basic reserve deficit of the thirty-eight major banks in other money centers was little changed from the preceding period (see Table II). The money market was firm during the statement period ended on March 5, as the leading New York banks expanded their net purchases of Federal funds, which traded predominantly in a 6⅝ to 7 percent range. At the same time, they also increased their average borrowings from the Federal Reserve Banks by $83 million to $104 million.

Over the following statement period, pressures mounted on the reserve positions of banks both in New York and in other money market centers, principally as a result of a contraction in deposits. The money market became a shade firmer, and member bank borrowings from the Federal Reserve Banks expanded by $138 million (see Table I). Most Federal funds trading occurred in a 6½ to 6⅞ percent range during the period.

The money market readily accommodated the sizable flows of funds which arose in connection with the mid-March quarterly corporate dividend and tax payment period. The tone of the money market remained steadily firm during the March 19 statement week, as banks in the large money centers managed to fill their reserve needs on a daily basis without accumulating either large reserve excesses or deficits. Federal funds traded mainly in a 6⅝ to 6⅞ percent range, while member bank borrowings from the Federal Reserve Banks declined by $97 million on a daily average basis. In the final statement period of the month, nationwide reserve availability contracted moderately but reserve distribution shifted in favor of the money market banks and no unusual pressures developed.

The volume of large-denomination CD's outstanding at commercial banks continued to contract in March. At the weekly reporting banks in New York City, the decline amounted to approximately $575 million between February 26 and March 26, while CD's outstanding at all weekly reporting banks declined by $1,173 million. At the same time, liabilities of United States banks to their foreign branches rose in March by $1,049 million, as against an increase of $213 million in February.

In the wake of the ½ percentage point increase in the prime rate of commercial banks that was initiated on March 17, rates on some money market instruments were adjusted upward. Rates on dealer-placed prime four- to six-month commercial paper moved ⅛ of a percentage point higher to 6⅞ percent offered, and rates on some maturities of directly placed commercial paper increased by the same amount.

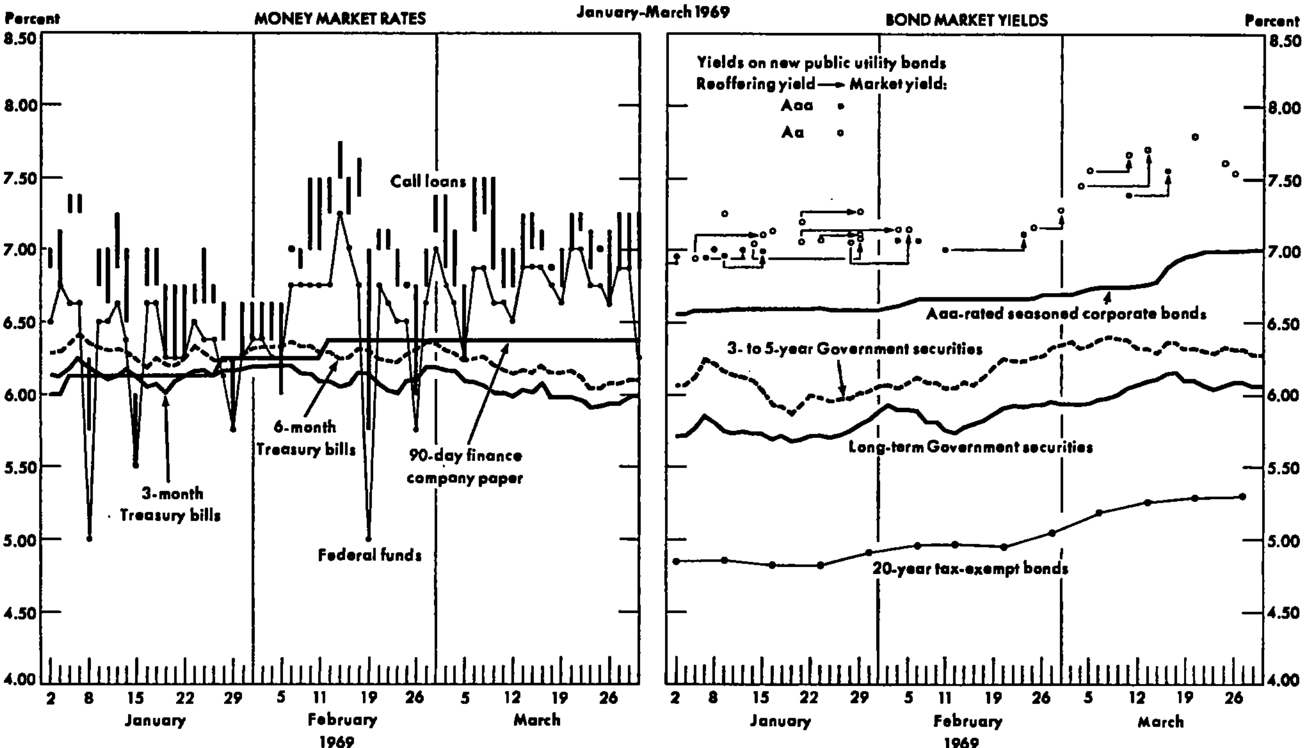
THE GOVERNMENT SECURITIES MARKET

A very cautious tone was evident in the market for Treasury notes and bonds as March began. In the early days of the month, prices generally edged lower as commercial bank offerings of coupon issues expanded, dealers seemed anxious to avoid an increase in inventories, and little significant investment demand developed. The pessimism of market observers was being fed by the apparent slow pace of the Vietnam peace negotiations, the weakness in the French franc, and the heavy tone of the corporate and tax-exempt bond markets. A somewhat better atmosphere soon developed in the intermediate-term maturity area, however, when commercial bank selling tapered off and demand improved somewhat. Participants were also moving to the view that a possible hike in the prime rate and discount rate had been largely discounted and that such changes might not occur in the immediate future, contrary to earlier expectations following the February 27 increase in the British bank rate. Thus, prices of intermediate-term Treasury issues edged higher from March 10 through midmonth. At the same time, however, prices of longer term issues continued to decline, mainly in reaction to the persisting weakness in the corporate and tax-exempt bond markets and to some switching transactions from Treasury bonds into corporate issues.

In the wake of the prime rate increase on March 17, prices of Treasury coupon issues were immediately marked sharply lower throughout the maturity range. A steadier tone quickly emerged in the intermediate-term sector, however, and prices resumed their modest upward movement. Then, on March 19, reports of a new approach to the Vietnam peace negotiations sparked price increases in the coupon sector, ranging from about $\frac{2}{32}$ to $\frac{8}{32}$ for intermediate-term issues and from $\frac{12}{32}$ to $\frac{24}{32}$ for long-term obligations. Subsequently, prices generally moved irregularly higher through March, primarily in response

SELECTED INTEREST RATES

January-March 1969



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 (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 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, and The Weekly Bond Buyer.

to renewed hopes for peace in Vietnam which stimulated short-covering demand from professional participants. Over the month as a whole, prices on most intermediate-term issues were $\frac{2}{32}$ to $\frac{27}{32}$ higher, while those on longer term issues were $1\frac{6}{32}$ to $1\frac{26}{32}$ points lower.

In the Treasury bill market, a strong tone persisted in March. Over much of the month, a steady investment demand for bills emanated from a wide range of sources, including commercial banks, public funds, institutions, corporations, and professional market participants, thus keeping the market's available supply of bills scant. During the first half of March, bill rates generally declined by 5 to 40 basis points. After news of the prime rate increase reached the market, bill rates rose briefly. However, a good tone quickly reappeared, and rates resumed their downward trend from March 18 through the following week. Thereafter, rates briefly came under some renewed upward pressure but at the month end had leveled off. Bill rates closed down over the month by amounts generally ranging from 15 to 30 basis points for maturities of ninety days or longer.

On March 18, the Treasury announced that it would auction a \$1.8 billion "strip" of bills on March 25 for payment on March 31. The offering represented a \$300 million addition to each of six outstanding weekly bill issues maturing from May 8 through June 12, with subscribers required to take equal amounts of each of the reopened issues. Commercial banks bid fairly aggressively for the strip for which they were permitted to make full payment in the form of credits to Treasury

Tax and Loan Accounts, and the bills were auctioned at an average issuing rate of 5.027 percent.

At the regular monthly auction on March 26, average issuing rates on the nine- and twelve-month bills were set at 6.058 percent and 6.132 percent, respectively, 25 and 10 basis points lower than the average rates at the comparable February auction (see Table III). At the final regular weekly auction of the month held on March 24, average issuing rates for the new three- and six-month bills were set at 5.946 percent and 6.096 percent, respectively, 13 and 16 basis points lower than the average rates established at the last weekly auction in February.

OTHER SECURITIES MARKETS

Prices of corporate and tax-exempt bonds declined steadily through most of the month in a very cautious setting. Market participants apprehensively weighed the interest rate outlook, particularly in the light of the midmonth rise in the commercial bank prime rate that had been widely expected. During the month, many recent corporate and tax-exempt bond flotations, which had encountered considerable investor resistance, were released from syndicate price restrictions with sharp subsequent upward yield adjustments. Moreover, new issues which reached the market at progressively higher yields were frequently accorded apathetic investor receptions. The high interest rate levels and the disheartening investment interest prompted reductions in the size of some offerings and postponements of other planned flotations. A significantly improved tone emerged in the corporate bond sector during the latter part of March, when participants became more optimistic about the outlook for peace in Vietnam and the reduced volume of new issues being offered at record high-yield levels drew excellent investor interest.

Price cutting was widespread, and market conditions led to the postponement of a large volume of new issues. The weak tone which predominated in the corporate bond sector during the first half of the month was vividly illustrated when a $150 million Aaa-rated telephone company flotation of 7½ percent refunding mortgage bonds was reoffered to investors on March 11 at a 7.375 percent record yield and generated very little investor interest. The issue, which featured five years of call protection, carried a yield 37 basis points higher than had a similar flotation a month earlier. On March 17, in the wake of the prime rate increase, syndicate price restrictions were removed on this slow-moving issue and the yield on the new bonds initially rose by 20 basis points to 7.57 percent. The sharp price concessions on the telephone company issue eventually attracted some investor interest to the bonds, and their yield subsequently receded moderately. On March 19, an A-rated $80 million utility company offering of 7.90 percent first and refunding mortgage bonds was marketed at par. As hopes for Vietnam peace were rekindled, this issue benefited from a more favorable market atmosphere, attracted good institutional interest, and was quickly sold. The improved tone in the corporate bond market continued throughout the latter part of the month, and prices on many outstanding issues rose from the low levels reached earlier in the period. In addition to the optimism generated by reports of secret Vietnam talks, the market responded favorably to renewed investor interest at the higher yield levels and to the lightened schedule which resulted from several postponements of sizable new issues.

In the tax-exempt sector, there was little evidence of any significant investment interest on the part of commercial banks and this factor continued to exert considerable restraint upon market sentiment throughout the month. As the month progressed, dealer inventories and new issues in syndicate were reduced sharply by the cancellation or postponement of some $475 million of new issues previously planned for March. In some cases, the cancellations stemmed from the borrowing government's inability to get underwriter bids at its statutory interest ceiling rate. Nonetheless, the calendar of new issues scheduled for offering remained high during March, and at the month end the 28-day calendar was nearly double the late February level.

At the end of March, *The Weekly Bond Buyer's* yield index of twenty seasoned tax-exempt issues was quoted at 5.30 percent, 26 basis points higher than a month earlier (see chart). Moody's index for seasoned Aaa-rated corporate bonds closed the month at 7.00 percent, 31 basis points higher than a month earlier. The Blue List of advertised dealer inventories of tax-exempt securities fell by $224 million to $345 million at the month end, as underwriters cleared their shelves in advance of the large April calendar.