The Money and Bond Markets in November

The rapid drop in prices of intermediate- and long-term securities, which began in the latter part of October following a rally earlier that month, carried market yields in many sectors to new highs during November (see Chart I). Vietnam and inflation continued to dominate market attention, and in large measure the sharp price declines during the month were fueled by discouragement over the absence of apparent progress in either area. In addition, market participants increasingly came to feel that fiscal restraint was lessening and that the prospect of any near-term relaxation of monetary restraint was remote. Borrowing demands continued to be very heavy, and the response of institutional investors to new offerings was often indifferent. Even at progressively higher offering yields, which reached as much as 60 basis points above those at the beginning of the month, many corporate flotations could not be fully placed. When unsold portions were released from underwriting syndicates to trade in the secondary market, their yields soared further. New offerings of tax-exempt issues also moved slowly despite record-high interest rates, and a considerable volume of flotations was again held off the market because of statutory rate ceilings.

Yields on most Treasury bills also climbed sharply higher to new record levels in November, with many increases ranging from 40 to 50 basis points. The bulk of the advances took place after midmonth, when auctions of bills on three successive business days—November 21, 24, and 25—taxed the capacity of the market. Upward bill rate pressures also resulted from large demands for new short-term funds by Federal agencies and tax-exempt borrowers and from sales of Treasury bills by foreign holders. Only in the short end of the bill market did strong demand place a damper on the rate advances. Prices of intermediate- and long-term Government securities dropped sharply, and yield increases of from 20 to 30 basis points were not uncommon. In the process, long-term bond yields registered new record highs, although yields on higher coupon intermediate-term issues failed to reach the early-October peaks.

Bank reserve positions continued to be hard pressed during November, and member bank borrowings remained sizable. Federal funds traded above 9 percent until late in the period, rates on three-month Euro-dollars climbed sharply around midmonth, and other short-term rates were as much as ½ percentage point higher at the end of November.

BANK RESERVES AND THE MONEY MARKET

Nationwide bank reserve availability remained relatively unchanged on balance during November. Member banks' net borrowed reserves averaged around $1 billion and their average borrowings at the discount window were $1.2 billion, both about the same as in October. Federal funds traded generally at 9 percent or above until the last week of the month, when the effective rate averaged below 8½ percent. Operating factors absorbed member bank reserves in each of the statement weeks ended in November (see Table I). The amount absorbed—over $2 billion—was considerably greater than usually occurs in November, partly because foreign central banks made large repayments of previous drawings under the Federal Reserve swap network. As an offset to the reserve absorption by market forces, the Federal Reserve injected reserves through open market operations, primarily by outright purchases of Treasury securities.

Money center banks, particularly those in New York City, experienced large deposit outflows early in the month, and in the week ended on November 12 the net basic reserve deficit of the forty-six major banks soared to $5.3 billion (see Chart II), the highest level of 1969. The combination of this swing and the aggregate reserve absorption by market forces placed heavy strains on the Federal funds market, where rates averaged 9¼ percent for the first two weeks of the month. That the rate did not push higher was due in part to recourse by the large banks to borrowings from Federal Reserve Banks. During the week of November 12, average borrowings for the forty-six banks reached $646 million (see Table II), the highest volume since the beginning of the year.

The large banks were slow to recoup their deposit losses after midmonth, and until the week of November 26 the Federal funds rate generally held steady around 9¼ percent. During that week, reserve deficits were pared considerably and, with a relatively small net shift in reserves caused by market factors, Federal funds rates eased a bit to a 7 to 9 percent range.

Most short-term money market rates moved higher over the month. Although ninety-day finance company paper remained around 7¾ percent, bankers' acceptances and prime four- to six-month dealer-offered commercial paper each rose ½ point. The three-month Euro-dollar rate was steady at 10 percent until midmonth, then jumped to around 11 percent for most of the balance of the period. In part, demands for Euro-dollar funds were spurred by the prospect of closer regulation of member banks' use of the commercial paper market.[1] At the end of October the volume of bank-related commercial paper outstanding approximated $3.6 billion, up over $1 billion during the month and $2.4 billion higher than in June.

Monetary aggregates moved up in November. According to preliminary data, the narrow money supply expanded at about a 5 percent annual rate after several months of little change, and total member bank deposits subject to reserve requirements (adjusted to include Euro-dollar liabilities) advanced 11 percent.

THE GOVERNMENT SECURITIES MARKET

Rates on most Treasury bills recorded their sharpest rises of the year in November and, in the process, swept to new all-time high levels. The advances reflected the spreading belief that monetary policy would have to remain restrictive for a protracted period before inflationary pressures would recede. Heavy Treasury and agency financing and bill sales by foreign holders also contributed to pressures in the short-term markets. Only in the very short bill maturities, where strong demand was in evidence, did rates fall. Over the month as a whole, one-month bill rates fell 35 basis points to 6.65 percent, while rates on three-month and one-year bills climbed 52 and 47 basis points, respectively, to 7.51 percent and 7.50 percent.

Most of the upward rate movement in bills came after midmonth, when the concentration of bill auctions on three successive business days, November 21, 24, and 25, contributed to an abrupt upsurge. Early on Monday, November 17, the Treasury announced that it would auction an additional $2.5 billion of April and June tax anticipation bills (TAB's) on November 21. The announcement immediately pushed longer bill rates higher and, in the regular weekly auction held later on Monday, the average rate of discount on the six-month bill reached a record 7.518 percent, 8 basis points higher than the week before (see Table III). In the TAB auction four days later the $1 billion of the April maturity commanded an average rate of 7.815 percent, and the rate on the $1.5 billion of the June maturity averaged 7.975 percent—53 and 77 basis points higher than the rates that had been set for the same maturities at two auctions during October. These were the highest auction rates ever recorded for new TAB issues.

In the span of the four business days from November 20 through November 25—which encompassed the offering of the TAB's and the regular weekly and monthly bill auctions—rates on issues maturing in three months or more soared as much as 25 to 35 basis points. These pressures pushed the new-issue rates to new highs in the auctions on November 24 and 25. On November 24 the auction rates for the new three- and six-month issues averaged 7.476 percent and 8.027 percent, respectively, up 34 and 51 basis points from the previous week's auction. The 8.027 percent rate was the highest ever set on any maturity in a Treasury bill auction. Then, on November 25, the new nine- and twelve-month bills were auctioned at average rates of 7.778 percent and 7.592 percent, respectively, 53 and 47 basis points higher than a month earlier. At the higher rates, considerable investor and dealer interest materialized in the longer maturing bills. At the close of the month the bid rate on the new six-month bills was 7.81 percent, down 22 basis points from the November 24 auction rate.

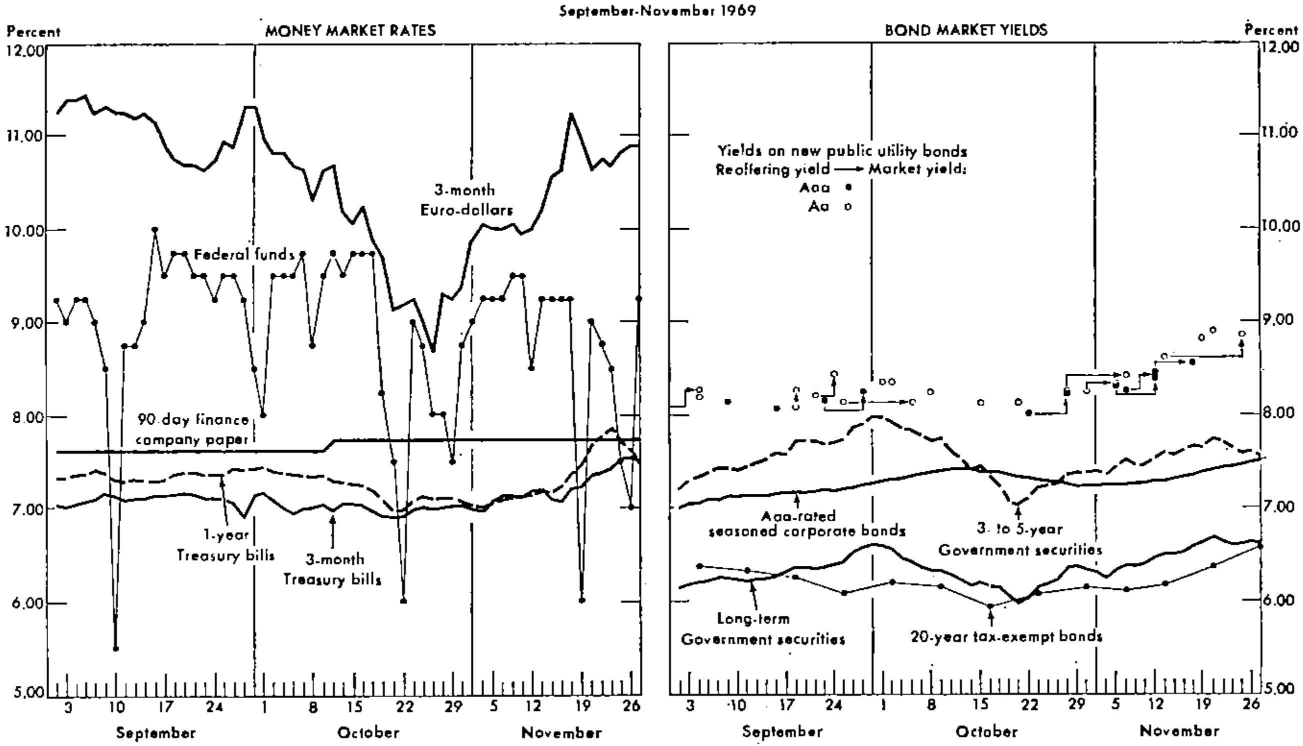
Yields on intermediate- and long-term Treasury coupon issues also forged higher in November—in many cases to record highs. The pressures generated by the large volume of Federal agency and corporate new-issue flotations were an important contributing factor. In addition, disappointment over the President's November 3 speech, which was interpreted in the market to mean that no new developments in Vietnam were in the offing, prompted dealers to lighten positions. Yields rose 20 to 35 basis points in light

[1] On October 29 the Board of Governors of the Federal Reserve System announced that it had determined that commercial paper and similar obligations issued by subsidiaries of member banks were, under the provisions of Regulations Q and D, subject to interest-rate limitations and reserve requirements to the same extent as obligations issued directly by member banks. The Board subsequently announced measures for the accommodation of an orderly adjustment by member banks to that determination. In another action on October 29, the Board announced that it was considering amending the provisions of Regulation Q to apply to funds received by member banks from the sale of commercial paper or similar obligations by either the parent holding company or a collateral affiliate of a member bank in a holding company system.

Chart I

SELECTED INTEREST RATES

September-November 1969



Note: Data are shown for business days only.

MONEY MARKET RATES QUOTED: Bid rates for three-month Euro-dollars in London; 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-month and one-year 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.

trading, with the 4¼ percent bond of 1987-92 reaching a record 6.86 percent during the month. Although the rise in rates in the intermediate-term sector was somewhat sharper than that of long-term, deep-discount bonds, yields on the high-coupon notes failed to reach the peaks registered in late September and early October, and yields on most intermediate-term issues moved lower during the last few days of November.

OTHER SECURITIES MARKETS

Yields on new corporate securities moved sharply upward almost without pause during November, leaving a wake of unsuccessful underwriting ventures as evidence of increasing congestion in the market. The continued manifestations of the strength of inflation cast a pall over market sentiment, and the fact that the President's November 3 address failed to contain encouraging news about immediate peace prospects was an additional disappointment.

The heavy volume of financing demands and the unwieldy positions of dealers and underwriters discouraged any rush by institutional investors to initiate new commitments. Utility offerings, which have tended to glut the market of late, were again under especially heavy pressure. The feature of the early part of the month was a $125 million offering on November 12 by South Central Bell Telephone Company. The issue carried an 8½ percent coupon and yielded investors 8.45 percent, 20 basis points above the previous record high for a Bell System offering set in September. Initial investor interest was light, however, and when the unsold portion was released from syndicate price restrictions on November 18, the yield soared as high as 8.67 percent in early secondary market trading.

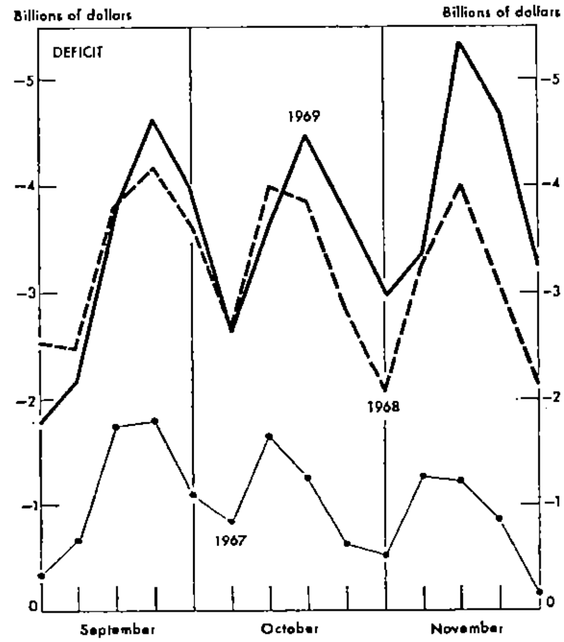
Only when new-issue yields approached the 9 percent level did investor interest quicken, but even then receptions were mixed. Two finance subsidiaries of large retail firms each offered $50 million of A-rated debentures at 9 percent, and sales were brisk. In contrast, on November 19 a very weak reception was accorded another utility, Pacific Gas and Electric Company, which offered $80 million of 9 percent mortgage bonds to yield 8.81 percent, a new record for Aa-rated issues. The next day, however, a quick sellout greeted the $50 million issue of Boston Edison Company, offered with a 9 percent coupon to yield 8.90 percent to investors. While much of the interest was reported to be from individuals, some institutional support again emerged. Although this response contributed to some added sales of the Pacific Gas and Electric offering, when the issue was finally released from pricing restrictions after the month end, the yield jumped 23 basis points. The generally unreceptive condition of the market, to which a succession of syndicate terminations testified, prompted Commonwealth Edison to defer a $100 million bond offering, which had been scheduled for November 25. At the month end, demand pressures remained very strong and the beginning of a seasonal slackening in the volume of scheduled offerings afforded little relief to the market. In the last week of November the four-week visible supply of forthcoming corporate financings approximated $1.3 billion.

Federal agency financings continued to be sizable, and new offerings provided an upward thrust to rates in both short- and long-term markets. The highlight of the month was a $1.1 billion financing on November 13 by the Federal Home Loan Banks. The issue, which raised $600 million in new funds, consisted of an 8⅜ percent ten-month note, an 8.20 percent 2¼-year bond, and an 8 percent five-year bond. The offering encountered investor resistance, in part because of the overhang of other imminent agency flotations, and at the close of the period bid-price discounts were $\frac{6}{32}$, $\frac{4}{32}$, and $\frac{16}{32}$, respectively.

In the tax-exempt market, statutory interest-rate ceilings, which have restricted new offerings throughout much of the year, again curtailed activity. A large volume of new issues carried short maturities as a means of tapping a less congested sector, where financing was less costly and rate ceilings less constraining. Indeed, some issues were sold at rates lower than earlier in the fall. In contrast, long-term bonds with serial maturities encountered investor resistance which resulted in higher costs and, in some cases, cancellations or postponements.

On November 6, for the second consecutive occasion, a 6 percent interest-rate ceiling impeded the flotation of tax-exempt Federally guaranteed housing bonds through the Federal Housing Assistance Administration. Only about $33 million of an offering totaling $139 million was awarded to bidders, and the issue cost averaged 5.996 percent—a record. However, short-term Federally guaranteed notes issued under the auspices of the Department of Housing and Urban Development (HUD) fared considerably better than the longer term housing bonds. On November 12, local renewal agencies marketed almost $330 million of project notes having an average maturity of about 9½ months at an average interest rate of 5.49 percent. This cost was about 10 basis points lower than that in an October financing. HUD announced that no placement fees had been paid, although such an option is open in the event borrowing costs exceed the 6 percent interest-rate ceiling generally applicable on these notes. In another financing on November 18, local public housing authorities sold almost $300 million of project notes

Chart II
BASIC RESERVE POSITION OF MAJOR MONEY MARKET BANKS



Note: Calculation of the basic reserve position is illustrated in Table II.

Table I

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

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

Factors	Changes in daily averages—week ended on				Net changes
	Nov. 5	Nov. 12	Nov. 19	Nov. 26	
"Market" factors					
Member bank required reserves	− 273	+ 23	− 480	+ 358	− 372
Operating transactions (subtotal)	− 729	− 266	− 304	− 722	−2,011
Federal Reserve float	− 198	+ 104	+ 597	− 197	+ 306
Treasury operations*	− 174	− 34	+ 94	+ 67	− 47
Gold and foreign account	− 19	− 1	− 10	+ 25	− 5
Currency outside banks	− 52	− 383	− 557	− 191	−1,183
Other Federal Reserve accounts (net)†	− 263	− 4	− 419	− 434	−1,120
Total "market" factors	−1,002	− 243	− 774	− 364	−2,383
Direct Federal Reserve credit transactions					
Open market operations (subtotal)	+1,075	+ 381	+ 725	+ 169	+2,350
Outright holdings:					
Government securities	+ 768	+ 585	+ 815	+ 164	+2,352
Bankers' acceptances	+ 1	+ 1	+ 1	+ 5	+ 8
Repurchase agreements:					
Government securities	+ 281	− 194	− 87	—	—
Bankers' acceptances	+ 7	− 3	− 4	—	—
Federal agency obligations	+ 18	− 8	− 10	—	—
Member bank borrowings	+ 144	− 83	− 173	+ 135	+ 24
Other loans, discounts, and advances	—	—	—	—	—
Total	+1,219	+ 298	+ 553	+ 304	+2,384
Excess reserves	+ 217	+ 55	− 311	− 60	+ 1

	Daily average levels				
Member bank:					
Total reserves, including vault cash	27,602	27,596	27,965	27,547	27,717‡
Required reserves	27,365	27,342	27,822	27,464	27,498‡
Excess reserves	237	254	143	83	219‡
Borrowings	1,267	1,144	1,072	1,207	1,213‡
Free, or net borrowed (−), reserves	−1,030	− 890	− 929	−1,124	− 993‡
Nonborrowed reserves	26,335	26,452	26,893	26,340	26,505‡
Net carry-over, excess or deficit (−)§	63	181	311	108	133‡

	Changes in Wednesday levels				
System Account holdings of Government securities maturing in:					
Less than one year	+1,471	+ 42	+1,647	− 95	+3,065
More than one year	—	—	−1,141	—	−1,141
Total	+1,471	+ 42	+ 506	− 95	+1,925

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 November 26.

§ Not reflected in data above.

Table II

RESERVE POSITIONS OF MAJOR RESERVE CITY BANKS NOVEMBER 1969

In millions of dollars

Factors affecting basic reserve positions	Daily averages—week ended on				Average of four weeks ended on Nov. 26
	Nov. 5	Nov. 12	Nov. 19	Nov. 26	
Eight banks in New York City					
Reserve excess or deficiency (−)*	96	79	35	7	54
Less borrowings from Reserve Banks	121	250	—	8	120
Less net interbank Federal funds purchases or sales (−)	199	1,583	1,396	568	937
Gross purchases	1,731	2,200	2,519	1,752	2,051
Gross sales	1,532	617	1,124	1,184	1,114
Equals net basic reserve surplus or deficit (−)	− 224	−1,754	−1,361	− 569	−1,002
Net loans to Government securities dealers	670	614	528	503	579
Net carry-over, excess or deficit (−)†	− 3	70	60	22	37
Thirty-eight banks outside New York City					
Reserve excess or deficiency (−)*	53	67	− 39	− 31	10
Less borrowings from Reserve Banks	425	308	389	438	387
Less net interbank Federal funds purchases or sales (−)	2,780	3,213	2,753	2,196	2,736
Gross purchases	4,346	5,164	4,830	4,130	4,615
Gross sales	1,566	1,951	2,067	1,935	1,880
Equals net basic reserve surplus or deficit (−)	−3,152	−3,452	−3,181	−2,665	−3,112
Net loans to Government securities dealers	178	138	161	216	173
Net carry-over, excess or deficit (−)†	− 6	43	37	14	22

Note: Because of rounding, figures do not necessarily add to totals.

* Reserves held after all adjustments applicable to the reporting period less required reserves.

† Not reflected in data above.

Table III

AVERAGE ISSUING RATES* AT REGULAR TREASURY BILL AUCTIONS

In percent

Maturities	Weekly auction dates—November 1969			
	Nov. 3	Nov. 10	Nov. 17	Nov. 24
Three-month	6.998	7.157	7.141	7.476
Six-month	7.281	7.435	7.518	8.027

Maturities	Monthly auction dates—September-November 1969		
	Sept. 23	Oct. 28	Nov. 25
Nine-month	7.257	7.244	7.773
One-year	7.350	7.127	7.593

* 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.

with an average maturity of 6½ months at an average rate of 5.36 percent. This cost was almost 50 basis points below that in October.

Not only did interest-rate ceilings block some flotations, but one recently raised ceiling proved barely high enough to allow a sale. The instance in question involved the Pennsylvania State Public School Building Authority, which in October had its ceiling raised from 6 percent to 7 percent. An offering of $53 million by the Authority was awarded at a net interest cost of 6.996 percent and was moderately well received by investors at yields ranging from 5.60 percent in 1972 to 7 percent in 2008.

The Blue List of dealer-advertised inventories advanced in November from the already sizable levels of October. At midmonth a new record 1969 high of $632 million was registered, and inventories were usually above $550 million throughout the period. Moreover, the four-week visible supply of forthcoming new financings generally exceeded $900 million until late in the month. Both furnished clear evidence of the congestion of the tax-exempt sector—a condition also reflected by *The Weekly Bond Buyer's* index of twenty municipal bond yields, which closed November at 6.58 percent, up 45 basis points over the month.