The Money Market in September

The money market remained generally firm in September. Reserve positions of banks in the money centers came under pronounced pressure at times as a result of heavy borrowings by corporations and Government securities dealers in connection with midmonth tax and dividend payments and the Treasury's refunding operation. These pressures were met without serious strain, however, particularly through very heavy purchases of Federal funds, and average borrowings from the Federal Reserve Banks actually declined for the month as a whole. As in August, Federal funds traded predominantly at the 3½ per cent ceiling. Rates posted by the major New York City banks on new and renewal call loans to Government securities dealers rose to a 3¾ to 4 per cent range in the early part of September, and then receded to a 3⅝ to 3⅞ per cent range over the remainder of the month.

While Treasury bill rates were generally unchanged for the month as a whole, upward rate adjustments on several other short-term money market instruments continued. Rates on various maturities of directly placed sales finance company paper generally were advanced by ⅛ to ¼ of a percentage point. The offering rates for new time certificates of deposit of leading New York City banks rose further, while the range of rates at which such certificates were offered in the secondary market rose by about 10 basis points on three-month maturities and by a somewhat lesser amount in the six-month category.

Interest in the market for Government notes and bonds was dominated during September by the largest Treasury advance refunding offer ever made. In a combined "prerefunding" and "junior" advance refunding, $32 billion of outstanding Treasury issues, maturing from May 1964 through August 1967 and including $23 billion held by the public, became eligible for conversion into securities maturing from 1968 through 1989-94.[1] The refunding was highly successful, with more than $6.5 billion—or 28.3 per cent—of the eligible securities held by the public exchanged for the Treasury's offerings of securities maturing in 1968, 1973, and 1989-94 (details given below). The large investor response, particularly for the 1973 and 1989-94 maturities, was generally taken in the market as a sign of investor confidence in current rate levels, and was particularly gratifying in view of some recent comments suggesting that current rate levels had been rendered artificial because of official purchases of intermediate- and long-term issues.

The Treasury estimated that the refunding extended the average maturity of the marketable debt by over four months, to more than five years and three months as of the end of September, the longest average maturity since July 1956. The Treasury also expressed the view that the success of the refunding should enable the Government securities market to accommodate readily the additional securities that must be sold to meet Treasury cash needs for the remainder of the calendar year. At the time of the refunding offering, the Treasury had made clear its intention to rely mainly on the bill market in filling these further needs.

Prices of outstanding Government notes and bonds receded during the opening days of the month in response to persisting expectations that an advance refunding was imminent. Market reaction to the September 4 refunding announcement was quite favorable, and lively trading ensued as investors adjusted their portfolios in light of the new investment opportunities presented by the exchange operation. Prices of outstanding issues declined in partial adjustment to the higher yields available on the newly offered securities, but a firm tone quickly emerged in the favorable atmosphere surrounding the financing. After the results of the refunding were announced on September 18, prices turned up, edging higher over the remainder of the period. In the market for Treasury bills, rates declined in the opening days of September, moved higher around the middle of the period, and then tended slightly lower toward its close, showing little net change for the month as a whole. Prices of corporate bonds adjusted downward in early September in response to the attractive yield available on the long-term bond of 1989-94 included in the Treasury's refunding package. The market recovered

[1] In a prerefunding, the securities eligible for conversion mature in not more than one year; a junior advance refunding might be defined as an operation where the securities eligible for exchange mature in from one to five years.

after midmonth, however, and prices edged up over the balance of the period. In the tax-exempt sector, prices declined over much of the month primarily under the weight of large dealer inventories and a heavy schedule of future offerings. Late in the month, however, a somewhat steadier tone emerged.

BANK RESERVES

Market factors provided reserves on balance from the last statement period in August through the final statement week in September. Reserve gains—stemming mainly from the usual September rise in float and from a contraction in Treasury deposits at the Federal Reserve Banks—more than offset excess reserves drained by a seasonal expansion in required reserves and by an outflow of currency into circulation. System open market operations during the month more than offset the net reserves released through market factors. System outright holdings of Government securities contracted on average by $34 million from the last statement period in August through the final statement week in September, while holdings under repurchase agreements declined by $68 million. Net System outright holdings of bankers' acceptances increased by $2 million. From Wednesday, August 28, through Wednesday, September 25, System holdings of Government securities maturing in less than one year decreased by $130 million, while holdings maturing in more than one year remained unchanged.

CHANGES IN FACTORS TENDING TO INCREASE OR DECREASE MEMBER BANK RESERVES, SEPTEMBER 1963

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

Factor	Daily averages—week ended				Net changes
	Sept. 4	Sept. 11	Sept. 18	Sept. 25	
Operating transactions					
Treasury operations*	+ 112	− 22	− 127	+ 115	+ 78
Federal Reserve float	− 70	+ 139	+ 508	− 58	+ 519
Currency in circulation	− 151	− 167	+ 50	+ 166	− 122
Gold and foreign account	− 9	+ 18	+ 10	+ 3	+ 22
Other deposits, etc.	− 6	− 19	+ 77	+ 27	+ 70
Total	− 121	− 73	+ 616	+ 255	+ 677
Direct Federal Reserve credit transactions					
Government securities:					
Direct market purchases or sales	+ 180	+ 88	− 141	− 169	− 34
Held under repurchase agreements	+ 106	+ 120	− 294	—	− 68
Loans, discounts, and advances:					
Member bank borrowings	+ 81	+ 29	− 101	+ 105	+ 114
Other	− 1	+ 1	+ 1	− 2	− 1
Bankers' acceptances:					
Bought outright	+ 2	− 1	− 1	+ 2	+ 2
Under repurchase agreements	—	—	—	—	—
Total	+ 349	+ 234	− 596	+ 27	+ 14
Member bank reserves					
With Federal Reserve Banks	+ 228	+ 161	− 80	+ 282	+ 591
Cash allowed as reserves†	− 98	− 15	+ 184	+ 34	+ 55
Total reserves†	+ 130	+ 146	+ 54	+ 316	+ 646
Effect of change in required reserves†	− 58	− 109	− 239	− 186	− 592
Excess reserves†	+ 72	+ 37	− 185	+ 130	+ 54
Daily average level of member bank:					
Borrowings from Reserve Banks	325	354	193	388	315‡
Excess reserves†	480	517	332	462	448‡
Free reserves†	155	163	139	74	133‡

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

* Includes changes in Treasury currency and cash.

† These figures are estimated.

‡ Average for four weeks ended September 25, 1963.

THE GOVERNMENT SECURITIES MARKET

In the market for Treasury notes and bonds, longstanding expectations of an advance refunding were confirmed early in the month when the Treasury revealed on September 4 the details of a massive debt-extension operation combining a prerefunding with a junior advance refunding. In the prerefunding phase, holders of the 3¼ per cent certificates, 3¾ per cent notes, and 4¾ per cent notes all maturing on May 15, 1964 were given the opportunity to exchange their holdings for a new issue of 3⅞ per cent bonds of November 15, 1968, for new 4 per cent bonds of August 15, 1973, or for reopened 4⅛ per cent bonds of May 15, 1989-94 which had originally been sold through auction in April of this year. Public holdings of the $14.5 billion of securities eligible for prerefunding totaled about $8 billion.

In the junior advance refunding, holders of the 3¾ per cent bonds of May 15, 1966, the 4 per cent notes of August 15, 1966, the 3⅝ per cent notes of February 15, 1967, and the 3¾ per cent notes of August 15, 1967 were given the option of converting their holdings into the new 4 per cent bonds of 1973 or into the reopened 4⅛ per cent bonds of 1989-94. Public holdings of the approximately $17.6 billion of securities eligible in the junior advance refunding totaled about $15 billion.

Subscription books for the entire refunding operation were open from September 9 through September 13; the settlement date was September 18. Based on September 3 prices of the issues eligible for conversion and taking account of price adjustments paid by the Treasury in connection with the exchange, investment yields for the offerings were estimated at about 4.02 per cent on the new 3⅞ per cent bonds of 1968, 4.14 to 4.15 per cent on the new 4 per cent bonds of 1973, and 4.20 to 4.21 per cent on the reopened 4⅛ per cent bonds of 1989-94. On September 18, the Treasury announced that more than $6.5 billion, or 28.3 per cent, of the eligible securities held by the public had been exchanged for the refunding offerings.

Public holders subscribed for approximately $1.6 billion of the new 3⅞ per cent bonds of 1968, $3.7 billion of the new 4 per cent bonds of 1973, and $1.3 billion of the reopened 4⅛ per cent bonds of 1989-94.

The great size of the refunding took the market somewhat by surprise, as did the inclusion of a long-term bond in the offering. The market reacted quite favorably to the attractive new investment opportunities, however, and the quiet midsummer atmosphere quickly gave way to lively activity. Prices of "rights"—those issues eligible for refunding—advanced 2/32 to 4/32 in early trading, as a broadly based demand readily absorbed offerings. Prices of other outstanding issues adjusted downward on September 5, narrowing the spread between their yields and the yields offered on the new securities. Issues maturing through 1972 were generally unchanged to 6/32 lower, while most longer term bonds declined by 16/32 to 24/32, and the reopened 4⅛ per cent bonds of 1989-94 moved down by 1¾. Even after these price declines, however, yields available on outstanding maturities remained considerably below the yields available on the new Treasury securities. The market for outstanding bonds stabilized at the new levels, as offerings—which arose mainly out of demand for the new securities—were readily absorbed by professional short covering, some Treasury trust account buying, and demand from other investment sources.

In early trading of the new securities on a "when-issued" basis, interest centered on the 4 per cent bonds of 1973 and on the 4⅛ per cent bonds of 1989-94. Demand for the 3⅞ per cent bonds of November 1968 was light at first, but expanded somewhat toward the end of the subscription period. Pension funds and insurance companies were important buyers of the 4⅛ per cent bonds, while the 1968 and 1973 securities attracted commercial bank and other investment demand.

With the multitudinous price adjustments smoothly completed and with the success of the refunding virtually assured, a confident tone took root in the market and prices of outstanding notes and bonds fluctuated narrowly through September 17. Results of the exchange, announced before the market opened on September 18, surpassed Treasury expectations. Although exchanges for the new 4 per cent bonds of 1973 and for the reopened 4⅛ per cent bonds of 1989-94 were larger than most observers had anticipated, the market took the results in stride. After some initial hesitation, prices firmed when good professional and investment demand—both for the new refunding securities and for other outstanding issues—developed, while offerings remained light. Against this background, prices of Government notes and bonds generally moved higher from September 18 through September 23, and then fluctuated narrowly through the end of the period. Over the month as a whole, prices of intermediate- and longer term issues ranged from 15/32 higher to 1 18/32 lower.

Treasury bill rates declined moderately in early September, largely in response to a strong demand for bills from sellers of rights to the Treasury's prerefunding who were seeking reinvestment outlets. Beginning on September 9 a more cautious tone emerged, as demand tapered off and offerings expanded with the approach of the mid-month corporate tax and dividend dates. The absorption of these offerings by dealers subsequently added to the cost and volume of dealer financing. Caution was also induced by some feeling in the market that official concern might be aroused by the lower rate levels that had emerged earlier in the month and that the Treasury might soon offer a tax bill or a strip of bills. Therefore, rates edged generally higher from September 9 through September 17. During the remainder of the month, however, bill rates moved narrowly lower, as demand expanded moderately and offerings contracted after the passing of the tax date.

At the final auction of the month held on September 30, average issuing rates were 3.408 per cent for the new three-month issue and 3.515 per cent for the new six-month issue, about 2 and 3 basis points respectively above the rates established in the final auction in August. The outstanding three-month bill, which was the attractive December 26 maturity, closed the month at 3.37 per cent (bid) as against the end-of-August rate of 3.39 per cent (bid) for the three-month maturity. An average issuing rate of 3.586 per cent was set at the September 25 auction of the new one-year bills, compared with an average rate of 3.575 per cent at the first monthly auction of one-year bills on August 27. The bills, dated October 1, 1963 and maturing September 30, 1964, represented the second in the Treasury's new monthly series of one-year bills.

OTHER SECURITIES MARKETS

The inclusion of the 4⅛ per cent bonds of 1989-94 in the Treasury's advance refunding at a rate of return which reduced the existing yield advantage of corporate securities triggered substantial early-month price reductions in the corporate sector of the bond market. Syndicate price restrictions on several new utility issues were terminated during this period, and the resulting price reductions boosted yields by about 10 basis points. A firmer tone emerged over the midmonth period, however, as earlier price concessions attracted demand and the moderate calendar of forthcoming new issues contributed to an improved technical position in the market. Announceme of the large turn-ins for the longer term issues offered in the Treasury's refunding had little effect on the corporate sector, and prices of corporate bonds edged higher over the latter part of September.

In the tax-exempt market, price weakness persisted during much of the period, reflecting an expanding calendar of forthcoming issues and a heavy volume of dealer inventories which moved sluggishly even after sizable price concessions had been made. At the end of the month, however, a somewhat better tone emerged. Over the month as a whole, the average yield on Moody's seasoned Aaa-rated corporate bonds rose by 3 basis points to 4.32 per cent while the average yield on similarly rated tax-exempt bonds increased by 6 basis points to 3.15 per cent.

The total volume of new corporate bonds reaching the market in September amounted to approximately $280 million, compared with $255 million in the preceding month and $155 million in September 1962. New tax-exempt bond flotations during the month totaled approximately $415 million, as against $710 million in August and $395 million in September 1962. The Blue List of tax-exempt securities fell by $137 million during the month to $494 million on September 30. New corporate and tax-exempt bond issues marketed during the period were accorded mixed receptions by investors.

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