FEDERAL RESERVE BANK
OF NEW YORK
Fiscal Agent of the United States

Circular No. **10,030**
May 2, 1986

TREASURY ANNOUNCES ELIMINATION OF 20-YEAR BONDS AND CONSIDERATION OF REDUCTION IN SAVINGS BONDS INTEREST RATE FLOOR

To All Banking Institutions, and Others Concerned,
in the Second Federal Reserve District:

The following statement has been adapted from a press release issued April 30 by the Treasury Department:

20-year bond

The Treasury Department announced today that it will eliminate the regular quarterly 20-year bond cycle. The Department announced on March 18 the cancellation of the 20-year bond that it normally would have auctioned in late March, because Congress had not yet acted to increase the amount of Treasury's authority to issue long-term bonds without regard to the 4¼ percent statutory interest rate ceiling. The Department stated at that time that it wished to preserve its then remaining bond authority for the 30-year bond to be offered in the May refunding, because the 30-year bond is a more attractive issue in the market and thus less costly to the Treasury. Over the past month Treasury has carefully assessed the market's reaction to the cancellation of the March 20-year bond and concluded that it would be more cost-effective for the Treasury to issue larger amounts of 10- and 30-year securities rather than 20-year issues. That decision is reflected in the significant increases in the amounts of the 10- and 30-year issues announced today. While there will be no 20-year issues in the near future, the maturities and timing of Treasury issues over the longer run will, of course, depend upon market conditions and total financing needs at the time.

Savings Bond rate

The Treasury also announced that it is considering the need to reduce the guaranteed minimum interest rate on new issues of U.S. Savings Bonds.

The Treasury is pleased with the success of the market-based variable rate savings bond introduced in November 1982. Since then Series EE savings bonds held for at least 5 years have provided a yield equivalent to 85 percent of the average market yield on 5-year Treasury marketable securities. Such bonds, like the previous EE bonds, have early redemption and tax deferral advantages not offered on Treasury marketable securities, and also have a guaranteed minimum rate of 7.5 percent if held at least 5 years. The new savings bond has been well received by savers, while at the same time it has been a cost effective means of financing a portion of the public debt, as compared to financing with marketable securities. Sales of savings bonds have more than doubled, from $779 million in the third quarter of 1982 to $1.7 billion in the first quarter of 1986.

Market yields have declined substantially since the current terms of the market-based savings bond were established. The market-based savings bond rates are calculated in six-month blocks, and are announced early in May and November each year. The first market-based rate announced in November 1982 was 11.09 percent. The rate for the 6-month period ended April 30, 1986 was 8.36 percent. The rate for the May-October period is 7.02 percent. Thus, the variable market-based rate, for the first time, is lower than the 5-year floor rate of 7.5 percent.

In these circumstances, Treasury is considering a reduction in the 7.5 percent floor for future issues of Series EE savings bonds, in order to preserve the cost effectiveness of the program and to avoid excessive competition with other savings forms. The Department is not considering a change in the market-based formula, and any reduction in the 7.5 percent guaranteed minimum rate will apply only to bonds sold, or extended in maturity, after the reduction is announced.

Additional copies of this circular will be furnished upon request.

E. GERALD CORRIGAN,
President.