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MAXIMUM INTEREST RATE PERMITTED ON UNITED STATES SAVINGS BONDS

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Mr. BYRD, from the Committee on Finance, submitted the following

REPORT

[To accompany H. R. 5520]

The Committee on Finance, to whom was referred the bill (H. R. 5520) to amend the Second Liberty Bond Act to increase the maximum interest rate permitted on United States savings bonds, having considered the same, report favorably thereon with an amendment and recommend that the bill as amended do pass.

I. GENERAL STATEMENT

H. R. 5520, as passed by the House, would increase the maximum permissible interest rate on savings bonds (and savings certificates) held to maturity from 3 percent to 3¼ percent a year, compounded semiannually. It would authorize the Secretary of the Treasury, in his discretion, to increase the yield on savings bonds (and savings certificates) bearing issue dates of February 1, 1957, or later. It would also authorize the Secretary of the Treasury, in his discretion, to increase the maximum interest rate on series E savings bonds maturing on February 1, 1957, or later, which the holder retains for an extension period (of not more than 10 years) beyond their maturity dates. However, the discretion of the Secretary to increase interest rates in this latter case would be limited to interest payable with respect to the period beyond maturity.

In a statement to the public on February 14, 1957, the Treasury Department announced that it plans to increase to 3¼ percent the interest rate on series E bonds with issue dates of February 1, 1957, or later when held to maturity. This is an increase of one-quarter of a percentage point from the present 3 percent rate. The announcement also stated that the issue price and face value of the new bonds would remain unchanged; instead the increase in investment yield would be achieved by shortening the present 9 years and 8 months maturity to 8 years and 11 months. The Treasury Department also plans to increase redemption values for the new bonds during their earlier years. The announcement indicated that the rate on a new bond held for 3 years would be 3 percent instead of the present 2¼ percent. There was no indication, however, that the Treasury plans to change the interest rate with respect to bonds held beyond maturity.

The Treasury also indicated that it plans, effective February 1, 1957, to offer a revised 10-year series H-bond with an interest rate of 3¼ percent if held to maturity. The announcement further stated that the Treasury plans to reduce from $20,000 to $10,000 for each series the face amount of series E- and H-bonds which may be purchased by one individual in any one year.

Your committee held 3 days of hearings on this bill during which attention was given both to the recent deterioration of the market for savings bonds and to the potentially harmful effects on the economy of a program of high interest rates. Your committee has amended the House bill to lower the maximum rate permissible on savings bonds to 3.26 percent in lieu of 3½ percent. This limit will permit the Treasury to sell a $75 bond that will mature in 8 years and 11 months for $100.

It is believed that this change is desirable for several reasons. If a 3½ percent limit is provided there would be some expectation on the part of the public that the rate would in fact be raised and this would tend to reduce sales of the 3¼ percent bonds. Furthermore this adoption of this reduction of the limit to 3.26 percent expresses the opposition of the Congress to any increase in interest rates not absolutely essential in the interests of economic stability.

The Treasury has argued that there should be greater administrative flexibility in the Treasury to raise interest rates if redemptions of savings bonds again rise relative to sales. Your committee does not believe that the situation requires such delegation of authority to the executive since this deterioration of the market for savings bonds has in the past developed only slowly.

II. SAVINGS BOND PROGRAM

The legislation initiating the savings bond program in 1935 established a maximum interest rate of 3 percent. The first series E bonds were offered to the public on May 1, 1941, at a 2.9 percent yield to maturity, which was raised to 3 percent on May 1, 1952. Series E bonds maturing on or after May 1, 1952, earn interest after maturity at a rate of approximately 3 percent a year. H bonds, first issued in 1952, yield a 3 percent rate of return when held to maturity.

Series E and H bonds can be held only by individuals. While the rates of return on the two types of bonds are the same, they appeal to different buyers since the E bond is a discount bond, providing only one payment on redemption and the H bond pays interest annually by check. Savings bonds of the J and K series were designed for sale to organizations as well as individuals. The Treasury Department has indicated that sales of J and K series of bonds will terminate April 30, 1957. Series A–D and series F and G bonds were parts of the savings bond program but have not been issued in recent years. The current redemption value of outstanding savings bonds is shown in table 1 for the end of each year 1945–56 and for January through March of

1957. It can be seen that the $38,045 million of Series E bonds constitute the bulk of the $56,068 million of total savings bonds.

TABLE 1.—*Savings bonds outstanding, all series*

[Current redemption values in millions of dollars]

	Series E	Series H	Total, series E and H	Series F, G, J, K	Total, all series [1]
Dec. 31:					
1945	30,727		30,727	13,979	48,224
1946	30,263		30,263	16,366	49,864
1947	30,997		30,997	18,314	52,174
1948	32,188		32,188	20,613	55,197
1949	33,766		33,766	21,501	56,910
1950	34,493		34,493	23,089	58,248
1951	34,727		34,727	22,859	57,739
1952	35,143	181	35,324	22,616	58,046
1953	36,036	627	36,663	21,190	57,934
1954	36,778	1,455	38,233	20,058	58,358
1955	37,510	2,553	40,063	18,432	58,548
1956	38,087	3,310	41,398	15,576	57,018
Jan. 31, 1957	38,066	3,365	41,430	15,096	56,570
Feb. 28, 1957	38,058	3,392	41,450	14,824	56,317
Mar. 31, 1957	38,045	3,418	41,463	14,563	56,068

[1] Includes series A–D.

Source: Office of the Secretary of the Treasury, Analysis Staff, Debt Division.

III. NEED FOR LEGISLATION

Since May 1, 1952, when the Treasury Department raised the investment yield on savings bonds held to maturity to the maximum permitted by statute, this rate of return has necessarily remained stationary. However, the rates of return on most other forms of investment have risen sharply since that time. This can be seen by the average rates of return on the following types of investments:

[Percent]

	1952	1956
Mutual savings banks	2.43	2.89
Savings and loan associations	2.69	[1] 3.00
Insured commercial banks, time and savings departments	1.15	[1] 2.00
High-grade municipal bonds (Standard & Poor's)	2.19	2.93
Corporate bonds, Aaa (Moody's)	2.96	3.36
Corporate bonds, Baa (Moody's)	3.52	3.88
Average rates, short-term bank loans to business (selected cities)	3.5	4.2

[1] Estimated.

Compiled from statistics obtained from the Office of the Secretary, Analysis Staff, Debt Division, and from the Economic Report of the President, January 1957.

This stationary interest rate for savings bonds, while other investment yields have been rising, has been unfavorable to the relative position of savings bonds. This can be seen in table 2 which compares the annual increment in different forms of savings, those in savings and loan associations, mutual savings banks, commercial bank time deposits held by individuals and series E and H savings bonds. Due to the increment in value in bonds already held and also to the fact that the interest rate disparity was not so great among the various forms of savings, the savings bonds actually improved their position relative to the other forms of savings in the 3 years preceding 1956. However, in 1956, when the interest rate disparity became a significant factor, these savings bonds accounted for 13.3 percent of the annual increment in savings, the smallest percentage in the entire 4-year period.

TABLE 2.—*Series E and H bond share of individual savings—Annual changes in savings*

[In millions of dollars]

Calendar years	Savings and loan	Mutual savings banks	Commercial bank time deposits (individuals)	Series E and H savings bonds	Total	Percent series E and H bonds of total
1953	+3,641	+1,774	+2,568	+1,339	+9,322	14.4
1954	+4,415	+1,964	+2,526	+1,571	+10,476	15.0
1955	+4,965	+1,837	+1,561	+1,830	+10,193	18.0
1956	[1] +5,085	+1,836	+1,762	+1,335	+10,019	13.3

[1] Preliminary.

Source: Office of the Secretary of the Treasury, Analysis Staff, Debt Division.

The increasingly unfavorable position of savings bonds is most accurately reflected by the trends in cash sales and cash redemptions in the past 2 years, shown in table 3. This table shows that redemptions in 1956 exceeded redemptions in the corresponding months in 1955 in all but 3 months. Also, beginning in June 1956, cash redemptions have exceeded cash sales in all but one of the months. Moreover, this excess of redemptions has for the most part increased month by month.

TABLE 3.—*Monthly sales and redemptions of series E and H savings bonds*

[In millions of dollars]

	Cash sales	Cash redemptions	Cash gain or loss		Cash sales	Cash redemptions	Cash gain or loss
1955—January	573	404	169	1956—March	465	400	65
February	465	343	122	April	414	402	11
March	518	406	112	May	418	412	6
April	448	376	72	June	398	405	−6
May	419	392	28	July	443	431	11
June	428	437	−9	August	403	414	−11
July	439	402	37	September	335	380	−45
August	439	399	40	October	390	411	−21
September	414	393	21	November	366	368	−2
October	404	358	46	December	363	392	−29
November	395	358	36	1957—January	465	547	−82
December	425	383	42	February	361	426	−65
1956—January	572	450	122	March	365	438	−73
February	476	368	108				

Source: Office of the Secretary of the Treasury, Analysis Staff, Debt Division.

The effect of your committee's bill will be to permit the Treasury Department to restore the competitive position of savings bonds with other comparable forms of saving without causing any significant change in the present distribution of investments.

In 1951 the Congress enacted legislation providing that the owners of matured series E savings bonds who did not desire to cash them could, at their option, retain their investment through an additional 10-year period. The Treasury Department announcement on February 14, 1957, stated that "terms of any extension privilege for the new bond will be determined later." Your committee's bill provides the same permissible maximum of 3.26 percent yield can be provided on savings bonds which mature on or after February 1, 1957, for the period the bonds are held after maturity. Although the Treasury Department did not request this authority, it will enable the Department, if it deems this to be a desirable policy, to encourage people to hold series E savings bonds which they may now have, beyond their regular maturity date. This bill, by giving the Secretary of the Treasury discretionary authority to pay up to 3.26 percent during the extension period on E bonds which mature on or after February 1, 1957, will enable him to provide more favorable treatment for this period without having to come to Congress to request such authority.

Table 4 shows the redemption values and investment yields of series E bonds outstanding at the present time. The first part of this table relates to bonds issued beginning May 1, 1952, with a maturity yield of 3.0 percent while the latter part relates to bonds issued before that date with a maturity yield of 2.9 percent.

TABLE 4.—*Series E bonds outstanding prior to first maturity, redemption values, and investment yields*

[Based on $75 bond—issue price]

Number of years held after issue date	Redemption value	Yield for—		
		Period held [1]	Period to maturity [2]	One additional 6-month period [2]
		Percent	*Percent*	*Percent*
Bonds issued beginning May 1952:				
0 to ½	$75.00	------------	3.00	1.07
½ to 1	75.40	1.07	3.10	2.12
1 to 1½	76.20	1.59	3.16	2.62
1½ to 2	77.20	1.94	3.19	2.59
2 to 2½	78.20	2.10	3.23	2.56
2½ to 3	79.20	2.19	3.28	2.53
3 to 3½	80.20	2.25	3.34	2.49
3½ to 4	81.20	2.28	3.41	2.46
4 to 4½	82.20	2.30	3.49	3.41
4½ to 5	83.60	2.43	3.50	3.35
Bonds issued before May 1952:				
4½ to 5	81.00	1.72	3.87	2.47
5 to 5½	82.00	1.79	4.01	2.44
5½ to 6	83.00	1.85	4.18	2.41
6 to 6½	84.00	1.90	4.41	4.76
6½ to 7	86.00	2.12	4.36	4.65
7 to 7½	88.00	2.30	4.31	4.55
7½ to 8	90.00	2.45	4.26	4.44
8 to 8½	92.00	2.57	4.21	4.35
8½ to 9	94.00	2.67	4.17	4.26
9 to 9½	96.00	2.76	4.12	4.17
9½ to 10	98.00	2.84	4.08	4.08
10 years (1st maturity)	100.00	2.90	------------	------------

[1] To beginning of each accrual period.
[2] From beginning of each accrual period.

Source: Office of the Secretary of the Treasury, Analysis Staff, Debt Division.

It can be seen from table 4 that if an outstanding series E bond has been held for over 2½ years there is no benefit obtained from cashing in the existing bond in order to buy a new 3.25 percent bond. After the bond is held for 2½ years the yield from holding the bond until maturity is 3.28 percent.

Table 5 shows a schedule of redemption values and investment yields that has been tentatively decided upon for the new series E bonds to be sold under this legislation.

TABLE 5.—*New E-bond—3¼ percent to maturity at 8 years, 11 months—Tentative schedule of redemption values and investment yields (based on $75 bond, issue price)*

Number of years held after issue date	Redemption value	Yield for—		
		Period held from issue date [1]	Period to maturity [2]	1 added period [2]
		Percent	*Percent*	*Percent*
0 to ½	$75.00		3.25	1.60
½ to 1	75.60	1.60	3.35	2.96
1 to 1½	76.72	2.28	3.38	3.13
1½ to 2	77.92	2.56	3.39	3.39
2 to 2½	79.24	2.77	3.39	3.43
2½ to 3	80.60	2.90	3.39	3.47
3 to 3½	82.00	3.00	3.38	3.41
3½ to 4	83.40	3.06	3.38	3.45
4 to 4½	84.84	3.11	3.37	3.39
4½ to 5	86.28	3.14	3.37	3.43
5 to 5½	87.76	3.17	3.36	3.37
5½ to 6	89.24	3.19	3.36	3.32
6 to 6½	90.72	3.20	3.37	3.35
6½ to 7	92.24	3.21	3.37	3.30
7 to 7½	93.76	3.21	3.39	3.33
7½ to 8	95.32	3.22	3.41	3.27
8 to 8½	96.88	3.23	3.49	3.22
8½ to 8 11/12	98.44	3.23	3.81	3.81
8 years, 11 months to maturity	100.00	3.25		

Source: Office of the Secretary of the Treasury.

[1] To beginning of each accrual period.
[2] From beginning of each accrual period.

IV. EXPLANATION OF BILL

Section 22 (a) of the Second Liberty Bond Act authorizes the Secretary of the Treasury (with the approval of the President) to issue United States savings bonds.

Under section 22 (b) (1) of the Second Liberty Bond Act savings bonds may be issued on an interest-bearing basis, on a discount basis, or on a combination interest-bearing and discount basis, and must mature not more than 20 years from the issue date. Such bonds may be sold at such price or prices, and may be redeemed before maturity upon such terms and conditions, as the Secretary of the Treasury may prescribe. However, the interest rate on, and the issue price of savings bonds, and the terms upon which they may be redeemed, may not be such as to afford as investment yield in excess of 3 percent a year, compounded semiannually.

Under section 22 (b) (2) of the Second Liberty Bond Act the Secretary of the Treasury (with the approval of the President) is authorized to provide by regulation that owners of series E savings bonds may (at their option) retain the bonds after maturity and earn interest upon the maturity values thereof for not more than 10 years at rates consistent with the provisions of section 22 (b) (1) of the Second Liberty Bond Act.

The first section of the bill amends section 22 (b) (1) of the Second Liberty Bond Act by changing the maximum permissible investment yield from 3 percent a year, compounded semiannually, to 3.26 percent a year, compounded semiannually. This will authorize, but it will not require, the Secretary of the Treasury to increase the investment yield on those bonds described in section 2 of the bill.

Section 2 of the bill provides that the authority provided by the first section of the bill may be exercised with respect to savings bonds bearing issue dates of February 1, 1957, or thereafter. Section 2 also provides that this authority may be exercised with respect to those series E savings bonds maturing on or after February 1, 1957, which are retained after maturity (but only for the period after maturity).

The following table illustrates the maximum interest rates on savings bonds permitted by existing law and by provisions of the bill, together with actual investment yields fixed by the Treasury Department on series E bonds.

Issue dates	E-bond investment yield (percent) [1]			
	Period to maturity		Full extension period	
	Maximum permissible	Actual	Maximum permissible	Actual
(1) May 1941 to April 1942	3.00	2.90	3.00	2.90
(2) May 1942 to January 1947	3.00	2.90	3.00	3.00
(3) February 1947 to April 1952	3.00	2.90	3.50	[2]
(4) May 1952 to January 1957	3.00	3.00	3.50	[2]
(5) February 1957 and on	3.26	[2, 3]	3.26	[2, 4]

[1] Compounded semiannually.
[2] To be determined by the Secretary of the Treasury, but not less than 3.00 percent.
[3] Based on information furnished to the committee by the Treasury Department, it appears that bonds issued under a new offering based on this legislation will afford an investment yield of approximately 3¼ percent to maturity.
[4] Based on information furnished to the committee by the Treasury Department, it appears that terms of any optional extension privilege on these bonds will not be decided until a later date.

V. CHANGES IN EXISTING LAW

In compliance with subsection (4) of rule XXIX of the Standing Rules of the Senate, changes in existing law made by the bill, as reported, are shown as follows (existing law proposed to be omitted is enclosed in black brackets, new matter is printed in italics, existing law in which no change is proposed is shown in roman):

SECOND LIBERTY BOND ACT, AS AMENDED

SEC. 22. (a) The Secretary of the Treasury, with the approval of the President, is authorized to issue, from time to time, through the Postal Service or otherwise, United States savings bonds and United States Treasury savings certificates, the proceeds of which shall be available to meet any public expenditures authorized by law, and to retire any outstanding obligations of the United States bearing interest or issued on a discount basis. The various issues and series of the savings bonds and the savings certificates shall be in such forms, shall be offered in such amounts, subject to the limitation imposed by section 21 of this Act, as amended, and shall be issued in such manner and subject to such terms and conditions consistent with subsections (b), (c), and (d) hereof, and including any restrictions on their transfer, as the Secretary of the Treasury may from time to time prescribe.

(b) (1) Savings bonds and savings certificates may be issued on an interest-bearing basis, on a discount basis, or on a combination interest-bearing and discount basis and shall mature, in the case of bonds, not more than twenty years, and in the case of certificates, not more than ten years, from the date as of which issued. Such bonds and certificates may be sold at such price or prices, and redeemed before maturity upon such terms and conditions as the Secretary of the Treasury may prescribe: *Provided,* That the interest rate on, and the issue price of, savings bonds and savings certificates and the terms upon which they may be redeemed shall be such as to afford an investment yield not in excess of **[**3**]** *3.26* per centum per annum, compounded semiannually. The denominations of savings bonds and of savings certificates shall be such as the Secretary of the Treasury may from time to time determine and shall be expressed in terms of their maturity values. The Secretary of the Treasury is authorized by regulation to fix the amount of savings bonds and savings certificates issued in any one year that may be held by any one person at any one time.

(2) The Secretary of the Treasury, with the approval of the President, is authorized to provide by regulation that owners of series E savings bonds thereafter maturing may, at their option, retain the matured bonds and earn interest upon the maturity values thereof for not more than ten years at rates consistent with the provisions of paragraph (1).