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Statement by

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before the

Committee on Banking and Currency
House of Representatives
February 24, 1971

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Mr. Chairman, I appreciate the opportunity you have afforded me to present the views of the Federal Deposit Insurance Corporation with respect to H.R. 4246, 92d Congress, a bill "To extend until March 31, 1973, certain provisions of law relating to interest rates, mortgage credit controls, and cost-of-living stabilization."

As the title of the bill indicates, it would extend until March 31, 1973, the statutory authority presently vested in the Board of Governors of the Federal Reserve System, the Board of Directors of the Federal Deposit Insurance Corporation, and the Federal Home Loan Bank Board to regulate in a flexible manner the rates of interest or dividends payable by insured banks on time and savings deposits and by members of the Federal Home Loan Bank System (other than those the deposits of which are insured by the Federal Deposit Insurance Corporation) on deposits, shares, or withdrawable accounts. The bill would also extend for the same period of time the authority of the Federal Deposit Insurance Corporation and of the Federal Home Loan Bank Board to subject certain noninsured banks and institutions to interest- and dividend-rate controls comparable to those applicable to insured banks and institutions. Finally, the bill would extend through March 31, 1973, the authority of the President to issue orders and regulations which he deems appropriate for stabilizing prices, rents, wages, and salaries.

The Corporation, which shares with the Federal Reserve Board and the Federal Home Loan Bank Board authority to administer the interest-rate provisions of existing law, takes no position on the standby stabilization provisions of the bill since these matters are outside its area of expertise, but it does support a temporary extension of the interest-rate control powers now vested in the three regulatory agencies.

Flexible authority for regulating the rates of interest or dividends that may be paid by insured banks on time and savings deposits and by certain members of the Federal Home Loan Bank System -- most of them insured savings and loan associations -- on deposits, shares, or withdrawable accounts was first conferred upon the three regulatory agencies in September of 1966 for a one-year period. On four different occasions, however, the authority has been extended for varying and consecutive periods of time so that it now expires, unless further extended, at the close of business March 21, 1971.

Authority to regulate the rates of interest or dividends payable by certain noninsured banks and institutions was first given the Corporation's Board of Directors and the Federal Home Loan Bank Board in December of 1969, following indications that the differential between rates offered by institutions not subject to rate controls and those offered by institutions subject to rate controls had become significant enough to cause a diversion of funds, in certain areas of the country, away from institutions subject to rate controls. That authority, which formed the basis for action by the Corporation and by the Federal Home Loan Bank Board in January and July of 1970, also expires at the close of business March 21, 1971, unless further extended.

The greater flexibility accorded the Board of Governors of the Federal Reserve System and the Board of Directors of the Federal Deposit Insurance Corporation in September of 1966 to vary interest- and dividend-rate ceilings on time and savings deposits on different categories of deposits, and the extension of interest- and dividend-rate controls for the first time to certain members of the Federal Home Loan Bank System, have strengthened significantly the ability of the three regulatory agencies to moderate excessive competition for savings and other time deposits between various types of financial institutions during periods of rising interest rates in the money and capital markets. Such authority has proved valuable not only in coping with the problems existing in 1966 but also with conditions developing subsequent to that date. If now further extended, the three regulatory agencies would continue to find themselves able to take timely and appropriate action in the future, whenever needed, without precluding the possibility that dividend-rate ceilings on certain types of deposits may be suspended or removed depending on market conditions.

Immediately following enactment of the 1966 statute, the three agencies were able to act in concert to stabilize the relationships among financial institutions, and they succeeded in moderating the forces that had unsettled the flow of funds within the financial community during the preceding period. The Federal Reserve Board and the Corporation's Board of Directors were legally able to establish higher rate ceilings for large-denomination certificates of deposit (the instruments most sensitive to money-market pressures), lower ceilings for consumer-type time and savings deposits, and different ceilings as between thrift institutions and commercial banks. Such distinctions helped to stem the outflow of consumer savings from thrift institutions, while the higher ceilings on large-denomination certificates of deposit helped stem the outflows of funds from banks to financial markets. In the absence of such regulation, bank liquidity might have been drastically reduced for both types of institutions while other financial consequences might have adversely affected public confidence in the nation's financial structure.

The period since September 1966 has seen wide variations in economic conditions. In 1967, interest rates dipped and financial market conditions eased. These conditions began to reverse themselves in 1968, and interest rates continued to climb until early 1970 while pressures in the financial markets continued to mount. During this latter period, despite some adjustments in the maximum rates payable on consumer-oriented savings instruments, rate ceilings were fixed at levels below long-term market rates and below the levels which some institutions could have paid. Had there been no ceilings, the general level of rates offered by competing financial institutions might well have been higher than they actually were. Some institutions would not have had the resources to pay the higher competitive rates or, if they had paid them, would have experienced substantial operating losses. This problem would have been particularly acute for those thrift institutions heavily locked in to long-term, comparatively low-yielding investments.

Short-term market interest rates have declined since January 1970, and have fallen quite sharply since October (except for a brief pause in December), reflecting for the most part a decrease in the demand for funds relative to supply. Three-month Treasury bill rates averaged 3.63 percent in the week ended February 19, compared with about 6 percent in October and nearly 8 percent in January 1970. Yields on four-to-six month commercial paper averaged 4.38 percent in the week ended February 19 compared with 7 percent in early October and about 8 3/4 percent in January 1970. By the fourth quarter of 1970, large commercial banks were able to pare their offering rates on large certificates of deposit and still increase their holdings of these instruments. Offering rates on such certificates are currently in the 4 1/2 - 4 3/4 percent range, down 3 to 3 1/2 percentage points from mid-1970 levels, yet outstanding negotiable certificates of deposit more than doubled in volume at large commercial banks between February 1970 and January 1971 and now aggregate $27.4 billion. Total time and savings deposits at all commercial banks total $240 billion at the present time, up 25 percent from the level in February 1970.

The rates of interest available on consumer-type savings instruments at both commercial banks and thrift institutions have remained at or near the maximum rates authorized, despite the substantial decline in rates on competing instruments. As a consequence, these consumer-type savings instruments have become increasingly attractive to the general public, and both types of institutions have experienced substantial inflows of funds from the consumer sector since mid-1970.

There is mounting evidence that banks and thrift institutions are currently experiencing larger inflows of savings than they can expeditiously invest at high yields in the light of slackened loan demand. As a result, a few institutions have recently announced cuts in the rates offered on consumer-type time deposits and even on savings deposits; some institutions no longer offer individuals the opportunity to invest in longer-term, higher-rate time deposits; and in still other cases, minimum denominations for such deposit instruments have been raised.

This recent experience strongly suggests that conditions in financial markets can and do shift abruptly, particularly during periods of economic uncertainty. Rate ceilings that appear unnecessary today may again become desirable at a future date.

Accordingly, the Corporation supports a temporary extension of its present interest-rate authority. It believes further that questions concerning the long-term need for such authority should be resolved only after the findings and recommendations of the Presidential Commission on Financial Structure and Regulation have been received and analyzed, since we understand the scope of the Commission's work to include (1) interest-rate regulation generally and (2) the variations in operating powers and competitive capabilities of different types of financial institutions which seek loanable funds from the public -- variations which were a major factor in the original request for flexible interest-rate authority. A lapse, moreover, in the present interest-rate authority of the three Federal agencies would result in inequitable rate regulation under the permanent authority which would then be in force. That authority, for example, does not apply to savings and loan associations or to financial institutions that are not federally insured, nor does it permit the Federal Reserve Board to set varying rates on different types of deposits.

The Office of Management and Budget has advised that it has no objection from the standpoint of the Administration's program to the submission of this statement for consideration by your committee.