

Excerpt from an Address by
Frank E. Morris, President
Federal Reserve Bank of Boston

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The Congress may wish to consider a regional experiment in eliminating the interest rate differential under Regulation Q for the six New England States. In saying this, I am speaking only for myself and not for the Federal Reserve Board, which has not yet established a position on this issue.

The Congress, in providing for a regional experiment in NOW Accounts in New England, has removed the principal argument which historically has been made in support of the differential, i.e., that the ability of the commercial banks to offer one-stop banking made it necessary for the thrift institutions to be able to offer something extra if they were to attract savings deposits. This argument has been removed, of course, by the fact that New England thrift institutions by and large can now offer one-stop banking to the consumer.

The elimination of the differential would not, in my judgment, have any substantial effect on the flow of funds into thrift institutions as a group. Our experience with NOW Accounts suggests that most people do not change their depositing habits very readily, even when they have a significant incentive to do so; and the removal of the differential does not create any significant incentive to shift funds. The effect of the removal of the differential would be felt by most thrift institutions only very gradually over a considerable period of time. Our statistical monitoring system will alert us to any unforeseen developments long before any real damage to the thrift industry could be sustained and the issue could be re-examined.

Since I do not believe that the flow of funds to the thrift institutions would be substantially changed by the removal of the differential, I also do not believe that it would have any significant effect on the availability of funds for mortgages. As long as commercial banks are not permitted to pay higher rates than thrift institutions, the determinant of the flow of funds into thrift institutions will be the level of open market interest rates. The issue of the stability of the flow of funds into thrift institutions will, of course, have to be faced when the Congress concerns itself with the problem of phasing out Regulation Q altogether. However, this is not a significant issue, in my judgment, as far as the differential is concerned.

Much can be said for the wisdom of regional experiments with major changes effecting financial institutions. The Congress has been and will be considering such major changes, including the payment of interest on demand deposits nationally. The New England NOW Account experiment, traumatic as it has been for the commercial bankers of our area, does provide a wealth of experience for assessing the probable impact on our financial system of national NOW Account legislation, as well as giving us a good basis for assessing the impact of legislation permitting interest on demand deposits, at least as far as individual accounts are concerned. I think that if Congress undertook a regional experiment in the elimination of the differential in New England, it would also provide the Congress with a good basis for assessing the impact of a similar move on the national level.