

Supervisory authorities have used their influence to resist higher rates on funds supplied to intermediaries, fearing deterioration of lending and investing standards or responding to a public opinion that increases in such rates encourage higher general market interest rates. Maximum rates which commercial banks have been permitted to pay under Regulation Q have exercised a restraint on aggressive banks. In early September Regulation Q controls were tightened, limitations on rates paid by savings and loan associations were formalized while liberalized, and more formal restraints were placed on mutual savings banks.

An exceptionally small share of the total flow of funds went through financial intermediaries in 1966. In 1964 and 1965, 44 percent of the net sources of credit in the economy flowed through time and savings accounts of deposit-type financial institutions. In the first quarter of 1966 these institutions received 30 percent of available funds, and in the second and third quarters they received 26 percent. With market rates higher than interest rates paid by banks, savings and loan associations, and other intermediaries, there was an incentive for suppliers of funds to place them in stocks, bonds, commercial paper, and direct loans. This diversion tended to favor the larger suppliers of funds and the large borrowers, notably the U.S. Government, large State and municipal borrowers, and major businesses, which obtain funds in a national market. Smaller savers generally received lower rates than large suppliers, while less well-known borrowers, who must usually rely on local financial institutions, had fewer funds for which to compete.