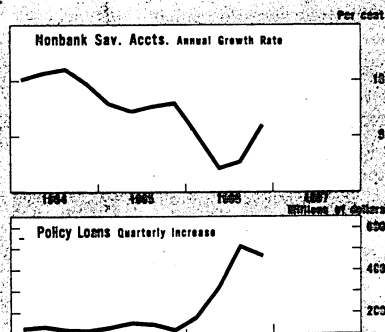
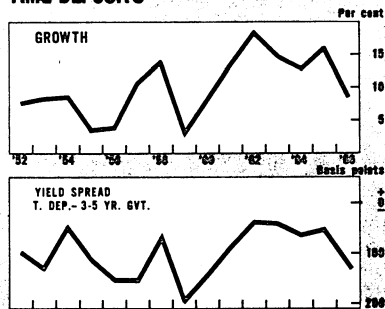


TIME DEPOSITS



nonbank institutions declined during the year.

Last year's experience was foreshadowed by earlier fluctuations in the growth rate of time deposits at commercial banks. These variations appear to be mainly the result of changes in relative yields. The bottom panel of the accompanying chart shows the yield spread, in basis points, between the rate on 3- to 5-year Governments—a representative market security—and the average effective rate paid on time and savings accounts. Time deposits became relatively more attractive when the yield spread moved up, and in those periods time deposit growth generally accelerated. When yields on time deposits became relatively less attractive, their growth usually slowed. Movements in these two series have not been perfectly correlated, to be sure, but they have been quite similar.

With holders of financial assets becoming more interest-sensitive, nonbank institutions have been increasingly influenced by the effects of monetary policy. Thus, the growth rate of nonbank savings accounts began to recede late in 1964, when competition from banks intensified. In last year's taut financial markets, with rates on market securities and banks' time deposits rising, net inflows to nonbank institutions dropped markedly, and then increased sharply in the fourth quarter when market rates began to fall.

The impact of monetary restraint also spread to insurance companies, where policy loans rose sharply, reducing the volume of funds available for investment in corporate securities and mortgages.

The more aggressive competition developing in financial markets over the postwar years, together with the decline in liquidity of financial institutions, has created an environment requiring a higher order of man-