

Published once in June and July, twice in May and Aug., 3 times in Jan., Feb., Sept., Oct., Nov., and Dec., 4 times in April, and 5 times in March by the University of Nebraska-Lincoln, Dept. of Publications Services & Control, 209 Nebraska Hall, Lincoln, NE 68588. Second-class postage paid Lincoln, Nebraska.

Prepared by the Bureau of Business Research
College of Business Administration

REGULATION Q: THE CRIME OF '66*

This presentation sounds a single theme, but a theme which has many variations: that the congressionally mandated system of deposit-rate ceilings at commercial banks, mutual savings banks, and S&Ls is a monstrous economic and political crime wave, monstrous because its principal victims are the nation's least fortunate citizens. The root crime was committed in 1966 when, as a "temporary" emergency measure to forestall a few S&L bankruptcies, Congress extended Regulation Q ceilings to thrift institutions. Although this system of comprehensive ceilings on deposit interest rates has been administered in ways that discriminate grossly against small savers, Congress has renewed it routinely. It is currently on the books through 1980.

This "Crime of '66" and its aftermath should disturb even the imperturbable conscience of a cultivated modern congressperson. The structure of these ceilings mocks our constitution's fundamental commitment to equal opportunity. It cynically permits vastly higher interest rates to be paid on sizable accumulations of funds.

Regulation Q ceilings tax the poor to finance "welfare" for the rest of us, equivalent in their distributional effects to a confiscatory federal tax that falls on the financial wealth of *small* savers only and whose proceeds are designated to subsidize homebuilders, homeowners, and inefficient depository institutions.

DIFFERENTIAL OPPORTUNITIES FOR REGULATORY ESCAPE IN FINANCIAL MARKETS

Regulation Q ceilings victimize small savers disproportionately for several reasons. First, small savers are frozen out of securities markets by the structure of transactions costs. One of the main functions depository institutions perform is to intermediate securities denominations by pooling small individual deposits into amounts large enough to trade in fully diversified round lots of high-denomination instruments. The smaller the amount of funds a household controls, the fewer the alternative assets into which it can economically put its savings. Whether ceilings exist or not, small savers tend to hold a large proportion of their accumulated savings in "regulated financial assets," a term I use to designate assets (deposits and U.S. savings bonds) whose yields are held down administratively as a result of deposit-rate ceilings.

*This article [reprinted with permission from *Illinois Business Review* 36, No. 7 (August 1979)] is taken from testimony given on 20 March 1979 before the Subcommittee on Commerce, Consumer, and Monetary Affairs. Hearings by this subcommittee of the Committee on Government Operations of the U.S. House of Representatives have been part of an overall review of congressionally mandated deposit-rate ceilings at commercial banks, savings and loan associations, and other thrift institutions.

However, sophisticated households with sizable amounts of savings can shop among a variety of assets. They can and do rearrange their financial-asset portfolios to lessen the burden that deposit-interest ceilings would otherwise place on them. Moreover, the longer the ceilings have remained in force, the more fully have financial markets and institutions been able to adapt to help them. The rapid growth of money-market mutual funds and credit unions—and the development of small denomination bonds by large issuers such as Sears—provide examples of this adaptation. Although such regulation-induced innovations reduce the burden of deposit-interest ceilings on large savers, they institutionalize imperfectly diversified patterns of intermediation that are economically less efficient than the ones they replace. This is a cost borne by society as a whole.

For small savers, possibilities for adapting their *financial* portfolios are severely limited and have been further compressed by government action to reduce disintermediation, notably the 1970 increase in the minimum denomination of U.S. Treasury bills. Small savers lessen the burden of low ceiling rates of interest on regulated financial assets principally by reducing their saving. But cutting back their savings plans prevents them from improving their station in life and spreads the burden that this regulation places on their standard of living far into the future. These households will continue to bear the costs of the Regulation Q era long after it has faded into history.

Ceilings on thrift-institution deposit interest were not intended to shaft small savers and promote inefficient financial arrangements. They were adopted to protect the solvency of the nation's weakest S&Ls and savings banks against the effects of rapidly increasing market interest rates and to promote housing activity by assuring a continued flow of mortgage funds. But every regulation must be judged by its unintended effects as well as its intended ones.

REAL ESTATE AS AN OPPORTUNITY FOR ESCAPE

During the Regulation Q era, for most households the inflation-adjusted after-tax rate of return has been negative on the few *financial* assets their wealth permits them to buy. Even in the 20 percent tax bracket, a 5.25 percent return on passbook savings yields only 4.20 percent after taxes. In the 30 percent bracket, the after-tax yield falls to 3.68 percent. It is hard to remember when the rate of inflation in product prices did not exceed these low rates of return. This means that savings invested in these assets have less real value with each passing year.

In the absence of government-enforced (Continued on page 2)

(Continued from page 1) ceilings on deposit interest rates, market forces would have pushed financial-institution deposit rates up at least enough to promise low-bracket depositors a small anticipated net yield. Given the Q ceilings are in place and that transactions costs keep small savers out of bond and stock markets, many households have found that real estate assets offer their accumulated savings the best protection against erosion in purchasing power. Real estate has been traditionally attractive to Americans and returns on real property have been taxed much more favorably than returns on financial assets. Federal tax treatment of a property's capital income is especially generous for owner-occupants. Real estate gained attractiveness under comprehensive deposit-rate ceilings because well-developed mortgage markets provided a convenient vehicle for small savers to leverage their modest savings enough to cover the purchase price of a residence or rental property.

Survey data depicting the composition of household assets indicate that in the face of unremitting inflation, deposit-rate ceilings have markedly changed the age distribution of real-estate ownership. This is shown in the table. Even as early as 1970 (unfortunately, this is the latest year for which representative household balance sheet data have been collected), households whose heads were less than 55 years in age had sharply increased the proportion of their accumulated savings held in real estate, while older households had shifted their funds out of both real estate and regulated financial assets into "unregulated financial assets" (stocks, marketable bonds, and mutual funds).

Although this point is not yet widely appreciated, small savers' efforts to protect their savings against the effects of unfair deposit-rate ceilings provide the motive force for the current speculative boom in housing. These ceilings have greatly contributed to secular inflation in housing costs and, by discouraging the flow of

saving into strictly financial instruments, have also reduced the pool of savings available for new business investment. Even though Regulation Q is intended to help housing, authorities by no means meant to push it so assiduously and at such a high cost in macro-economic destabilization.

COSTS AND VICTIMS OF DEPOSIT-RATE REGULATION

Costs imposed on households by deposit-rate regulation fall into two categories: (1) forgone interest on regulated assets actually held; and (2) distortions in the level of household saving and in its allocation among competing assets.

The value of deposit interest forgone by households has been assessed for scattered years or regions by several economists, but the most comprehensive figures are those of David H. Pyle ["Interest Rate Ceilings and Net Worth Losses by Savers" in Kenneth Boulding and Thomas Wilson, eds., *Redistribution Through the Financial System* (New York: Praeger, 1978), pp. 87-101]. Pyle estimates that between 1968 and 1975 holders of savings accounts lost at least \$22 billion. Although open-market interest rates did not greatly exceed ceiling rates on passbook savings in 1976 and the first half of 1977, since then the ceilings have misappropriated many more billions of dollars of household interest.

Even neglecting the forgone interest that accrued during 1976 and the first half of 1977, one can easily support an estimate of \$20 billion in lost interest for the three years and three months that have passed since Pyle's period of estimation. In September 1978, roughly \$425 billion were held in passbook savings accounts at commercial banks, savings banks, and S&Ls, with about another \$610 billion in certificate accounts at these institutions. Using these totals as a base and assuming that, over the last 18 months, forgone interest averaged two percentage points on passbook accounts and one percentage point on certificates provides a relatively simple way to justify my \$20 billion figure. One could conservatively add another \$1 billion a year in interest that would have been paid on U.S. savings bonds if the Treasury had not feared upsetting the Regulation Q appercart. Pulling these figures together produces a grand estimate of about \$55 billion dollars in forgone interest. Because senior citizens (those over 65 years of age) hold a vastly disproportionate amount of total funds in savings accounts (35 percent of regulated assets in the 1970 survey), about \$19 billion of these dollars were diverted from the old.

The second category of costs is much harder to evaluate. These must be viewed as "people costs" rather than mere dollar magnitudes. Households have been able to rearrange their portfolios to push their overall portfolio rate of return well above the 5-to-6 percent level available on regulated assets. Except for relatively high-income and older families, they have accomplished this principally by stepping up investments in real estate to counterbalance the low yields available to them on financial assets.

The big losers in the Regulation Q game are family units who do not own any real estate assets at all. Compared with other families, these households are drawn disproportionately from the ranks of the black, the female, the poor, and the young. In competing for mortgages, these groups are customarily disadvantaged. However, deposit-interest ceilings severely aggravate that disadvantage by driving up both the cost of housing and demands for mortgages among other groups, while reducing the disadvantaged sectors' ability to accumulate the wherewithal to make an acceptable down payment.

(Continued on page 6)

PERCENTAGE BREAKDOWN OF HOUSEHOLDS' PORTFOLIOS AND OF FINANCIAL ASSETS AND REAL-ESTATE EQUITY BY AGE CLASS IN 1962 AND 1970

Age of Household Head (in years)	Financial Assets			Real-Estate Equity		
	Regu- lated	Unregu- lated	Total ^a	Total	Equity in Home	Equity in Investment Real Estate
1962 data set						
Under 25	19.5	57.4	76.9	23.2	8.8	14.4
25 to 34	18.9	12.2	31.1	68.9	48.1	20.8
35 to 44	13.0	20.2	33.2	66.8	50.2	16.6
45 to 54	14.6	20.0	34.6	65.4	51.0	14.4
55 to 64	17.6	17.7	35.3	64.7	47.1	17.6
65 and over	27.0	12.8	39.8	60.2	42.0	18.2
2,117 Respondents	18.1	17.9	36.0	64.0	47.1	16.9
1970 data set						
Under 25	44.8	8.7	53.5	46.5	36.1	10.4
25 to 34	19.9	8.1	28.0	72.1	53.2	18.9
35 to 44	14.8	12.0	26.8	73.2	49.2	24.0
45 to 54	15.9	9.5	25.4	74.6	55.6	19.0
55 to 64	17.0	27.0	44.0	56.1	37.6	18.5
65 and over	21.3	25.8	47.1	53.0	32.7	20.3
2,576 Respondents	18.0	19.4	37.4	62.6	42.5	20.0

^aThe sum of the two totals shown may not add to 100.0 because of rounding.

Source: Calculated from *Survey of Consumer Finances* data tapes. (For a description of these surveys, see George Katona, L. Handell, and J. Schmiedeskamp, *1970 Survey of Consumer Finances* [Ann Arbor: Survey Research Center, Institute of Social Research, 1971].)

GOAL PROGRAMMING: A NEW MANAGEMENT TOOL

In today's complex organizational environment, the decision maker is regarded as one who attempts to achieve a set of objectives to the fullest possible extent in an environment of conflicting interests, incomplete information, and limited resources. The soundness of decision making is measured by the degree of organizational objectives achieved by the decision. Therefore, recognition of organizational objectives provides the foundation for decision making.

Decisions are also constrained by environmental factors such as government regulations, welfare of the public, and long-run effects of the decision on environmental conditions (pollution, quality of life, use of nonrenewable resources, and the like). To determine the best course of action, therefore, a comprehensive analysis of multiple and often conflicting organizational objectives and environmental factors must be undertaken. Indeed, the most difficult problem in decision analysis is the treatment of multiple conflicting objectives.

The issue becomes one of value trade-offs in the complex socioeconomic structure of conflicting interests. Regardless of the type of problem on hand, it is extremely difficult to answer questions such as: What should be done now? What can be deferred? What alternatives are to be explored? What should be the priority structure for the objectives?

Important developments in the field of management have indicated that "management by multiple objectives" is the most difficult and important area of management science. In my opinion, the most important research topic in the field of management science today is the area of multi-criteria decision analysis. Organizations and society have become so fragmented into interest and value groups that there is no longer one predominant objective for any organization. Consequently, one of the most important and difficult aspects of any decision problem is to achieve an equilibrium among the multiple and conflicting interests and objectives of the various components of the organization.

Several recent studies concerning the future of the industrialized society have echoed this same theme. When the society is based on enormous technological development and change, stability of the system must be obtained by achieving a delicate balance among such multiple objectives as food production, industrial output, pollution control, population growth, use of natural resources, international cooperation for economic stability, and civil rights and equal opportunity provisions.

Suppose a city is to formulate a long-range economic plan that is to evaluate long-range objectives and their resource requirements. The city needs new water tanks; extended transit systems; new streets; extended water, garbage, and sewage services; new welfare programs; job-training programs; and so on. The resources required usually surpass resources available. There exists competition for resources among projects. If substantial resources are to be invested in water and sewage services, other projects must be reduced in scale, deferred, or abandoned completely. Therefore, the assignment of priorities to the competitive projects becomes the first decision problem. Next, the sources of funds should be analyzed. Should the city increase property tax, sales tax, city income tax, business tax, service fees, or use a special bond to acquire resources for necessary projects? There are conflicting interests, and the decision maker must assign certain priorities.

A formal management process by multiple objectives through the use of priorities is a new frontier of management science. The goal programming approach appears to be an appropriate, powerful, and flexible technique of decision analysis for the troubled modern decision maker who is burdened with achieving multiple conflicting objectives under complex environmental constraints. Goal programming allows a simultaneous solution to a system of complex multiple objectives. Goal programming is capable of handling decision problems that deal with a single goal, with multiple goals, and multiple subgoals.

In evaluating multiple goal outcomes, a manager is often faced with the fact that some outcomes are relevant to organizational objectives but cannot easily be analyzed in terms of cost, profit, or utility. Conventional linear programming has the inherent difficulty that its unidimensional objective criterion requires cost, profit, or utility information that is often practically impossible to obtain. For example, in a production scheduling problem, costs associated with change in employment level are not easy to determine if costs of hiring, laying off, low employee morale, change in the public image of the firm, and so forth, are to be considered.

Goal programming is a modification and extension of linear programming. The goal programming approach allows the simultaneous solution of a system of complex objectives rather than a single objective. In addition, the objective function of a goal programming model may be comprised of nonhomogenous units of measure, that is, pounds and dollars, rather than one type of unit. The only requirement in goal programming is that there be a hierarchy of importance among these conflicting goals so that the low-order goals are considered only after the higher-order goals are satisfied or have reached the point beyond which no further improvements are desired. In other words, if management can provide an ordinal measure of goals in terms of their contributions of their importance to the organization, the program can be solved by goal programming.

In goal programming, instead of trying to maximize or minimize the objective criterion directly through structural variables, the deviations between goals and what can be achieved within the given set of constraints are to be minimized. Unlike linear programming, the goal programming objective function contains deviational variables to represent each goal or subgoal. The objective function then becomes the minimization of these deviations based on the relative importance or priority assigned to them. The objective function, in effect, tends to cause the deviational variables to "drive" the values of the decision variables.

Applications of goal programming to real-world decision problems are just beginning to be explored. Example applications include: advertising media planning, manpower planning, production planning, academic planning, financial analysis, economic policy analysis, transportation logistics, marketing strategy planning, environmental protection, and health care planning.

Information concerning educational programs which will gain familiarity and practice for the decision maker in utilizing the concepts and methods of goal programming can be obtained from the writer or from the Bureau of Business Research.

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Review and Outlook

The level of economic activity in Nebraska rose slightly in January 1980, although three of the five sectors recorded losses when compared to December 1979. The physical volume index for the state increased 0.4 percent from its December level, but was 0.4 percent below its value of January 1979. Nationally, a similar pattern was exhibited as the index rose 0.4 percent from December, and was 0.7 percent below its value of last year.

The December-to-January increase in state economic activity was concentrated in the agricultural sector, where activity rose 9.5 percent. In contrast, nonagricultural output fell 0.6 percent, with three of the four sectors declining. The month-to-month percentage changes for the nonagricultural sectors were: distributive,

unchanged; manufacturing, -0.3 percent; government, -1.2 percent; and construction, -3.9 percent.

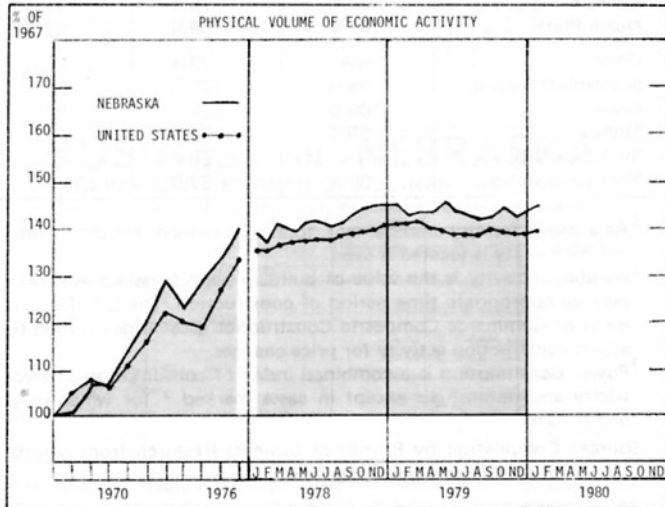
These December-to-January changes are based upon revised data which produced significant changes in some of the sectoral indexes for many of the months in 1978 and 1979. These changes primarily were due to annual revisions in the data series which are used to construct the indexes, especially the employment and cash farm marketings data series. The indexes in Table 2 reflect these changes and, as a result, are not directly comparable to data published in previous issues of *Business in Nebraska*.

In addition to data revisions, the factors used to adjust some of the data for seasonal variations were updated after all the revised data for 1979 had been (Continued on page 5)

Notes for Tables 1 and 2: (1) The "distributive" indicator represents a composite of wholesale and retail trade; transportation, communication and utilities; finance, insurance, and real estate; and selected services. (2) The "physical volume" indicator and its components represent the dollar volume indicator and its components adjusted for price changes using appropriate price indexes—see Table 5, page 5.

ECONOMIC INDICATORS: NEBRASKA AND UNITED STATES				
1. CHANGE FROM PREVIOUS YEAR				
January 1980	Current Month as Percent of Same Month Previous Year		1980 Year to Date as Percent of 1979 Year to Date	
	Nebraska	U.S.	Nebraska	U.S.
Dollar Volume	110.8	111.8	110.8	111.8
Agricultural	106.6	105.6	106.6	105.6
Nonagricultural	111.4	112.0	111.4	112.0
Construction	88.0	115.9	88.0	115.9
Manufacturing	118.3	115.1	118.3	115.1
Distributive	113.3	111.5	113.3	111.5
Government	102.7	106.7	102.7	106.7
Physical Volume	99.6	99.3	99.6	99.3
Agricultural	101.1	103.8	101.1	103.8
Nonagricultural	99.4	99.1	99.4	99.1
Construction	80.1	105.5	80.1	105.5
Manufacturing	103.9	99.7	103.9	99.7
Distributive	99.4	97.9	99.4	97.9
Government	98.3	101.5	98.3	101.5
2. CHANGE FROM 1967				
Indicator	Percent of 1967 Average			
	Nebraska	U.S.		
Dollar Volume	331.1	313.3		
Agricultural	304.3	317.7		
Nonagricultural	335.0	313.2		
Construction	267.5	327.7		
Manufacturing	351.7	282.7		
Distributive	347.3	332.6		
Government	300.2	297.4		
Physical Volume	144.5	139.6		
Agricultural	121.7	132.9		
Nonagricultural	147.9	139.8		
Construction	95.9	117.5		
Manufacturing	171.0	135.8		
Distributive	148.9	142.6		
Government	138.5	146.2		

3. NET TAXABLE RETAIL SALES OF NEBRASKA REGIONS AND CITIES (Adjusted for Price Changes)			
Region Number ¹ and City	City Sales ²	Sales in Region ²	
	Jan. 1980 as percent of Jan. 1979	Jan. 1980 as percent of Jan. 1979	Year to date '80 as percent of Year to date '79
<i>The State</i>	94.5	94.4	94.4
1 Omaha	90.5	89.9	89.9
Bellevue	81.9		
2 Lincoln	91.9	92.8	92.8
3 So. Sioux City	117.9	99.2	99.2
4 Nebraska City	75.1	85.9	85.9
5 Fremont	89.4	86.8	86.8
Blair	80.2		
6 West Point	93.5	91.8	91.8
7 Falls City	82.9	88.6	88.6
8 Seward	84.1	86.3	86.3
9 York	96.1	91.0	91.0
10 Columbus	94.5	98.6	98.6
11 Norfolk	91.6	96.3	96.3
Wayne	99.3		
12 Grand Island	95.0	96.5	96.5
13 Hastings	95.3	92.0	92.0
14 Beatrice	97.8	94.3	94.3
Fairbury	81.9		
15 Kearney	92.9	94.5	94.5
16 Lexington	95.1	98.3	98.3
17 Holdrege	78.9	89.3	89.3
18 North Platte	88.3	90.4	90.4
19 Ogallala	86.1	101.6	101.6
20 McCook	84.6	90.8	90.8
21 Sidney	90.6	99.2	99.2
Kimball	111.3		
22 Scottsbluff/Gering	98.2	93.3	93.3
23 Alliance	88.5	92.3	92.3
Chadron	73.3		
24 O'Neill	90.0	91.6	91.6
25 Hartington	99.1	97.8	97.8
26 Broken Bow	100.9	100.3	100.3

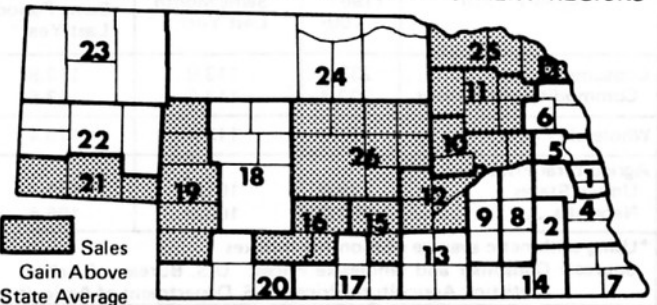


¹ See region map below.

² Sales on which sales taxes are collected by retailers located in the state. Region totals include motor vehicle sales; city totals exclude motor vehicle sales.

Compiled from data provided by Nebraska Department of Revenue.

1980 YEAR TO DATE AS PERCENT OF 1979 YEAR TO DATE IN NEBRASKA'S PLANNING AND DEVELOPMENT REGIONS



(Continued from page 4) collected. These seasonal adjustment factors changed significantly for cash farm marketings, as patterns of marketings in the late 1970s differed considerably from those established earlier. The chart at the bottom of page 4 graphically illustrates the effect of these changes. As can be seen, many of the sharp movements in Nebraska economic activity, which were evident in previous issues of *Business in Nebraska*, have been moderated.

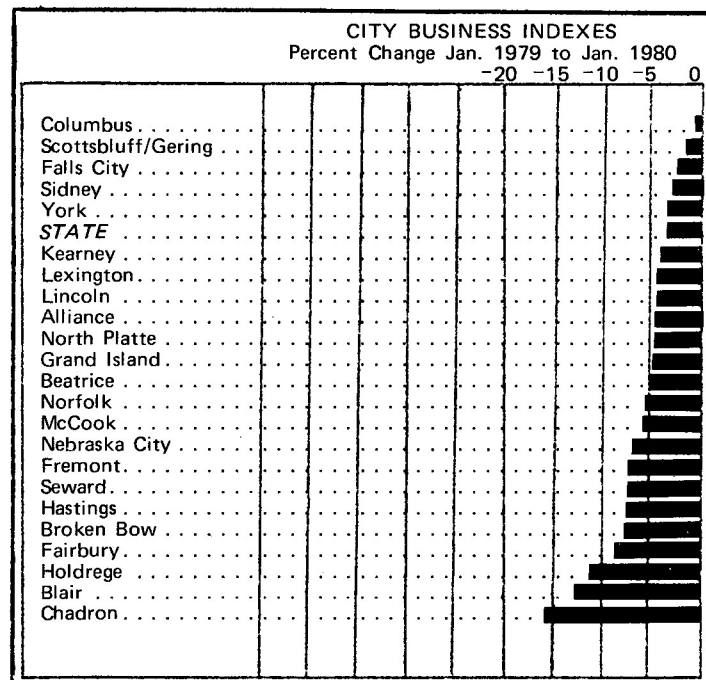
As a result of its January decrease, the index of nonagricultural activity fell 0.6 percent below the level of January 1979. Previous years have shown that nonagricultural output reflects the underlying trend in the Nebraska economy, while changes in agricultural output produce the sharp month-to-month variations. Since the nonagricultural sectors exhibited considerable weakness during 1979, they should be watched closely during the first few months of 1980. Construction and government appear to be the weakest sectors entering 1980, as their activity dropped during 1979. If nonagricultural output is to increase or maintain previous levels during 1980, the strength will have to come from the manufacturing and distributive sectors.

Employment continued its trend of growth established in 1979, as the number of employed persons increased 1.5 percent in January 1980 compared to January 1979. The gain in employment was nearly 11,000 persons, but it was slightly less than the increase in the labor force so that the number of unemployed also increased. January's unemployment rate of 4.2 percent (seasonally unadjusted), however, was still among the lowest in the nation and compares favorably with the national rate of 6.8 percent. Compared to January 1979, twelve of the twenty-three cities (with available data) registered increases in employment.

After adjustment for price changes, net taxable retail sales in Nebraska for January were 5.6 percent below the sales of January 1979. Retail sales at the national level recorded a 1.3 percent decline over the same period. The January decrease was felt throughout Nebraska, as all but two of the state's twenty-six planning regions had total sales below those of last year. Moreover, non-motor vehicle sales in twenty-nine of the thirty-two principal trading centers were lower than last January's sales. South Sioux City, Kimball, and Broken Bow were the only cities reporting increases.

Relative to January 1979, all of the twenty-three available cities registered losses. The moderate gains in employment were insufficient to offset the losses in retail sales, building activity, and power consumption. Columbus, with a loss of 0.3 percent, was the only city to experience a loss of less than 1 percent.

J. A. D.



Source: Table 3 (page 4) and Table 4 below.

The State and Its Trading Centers	Percent of Same Month a Year Ago		
	Employment ¹	Building Activity ²	Power Consumption ³
<i>The State</i>	100.5	84.9	88.9
Alliance	108.4	82.9	73.0
Beatrice	98.5	62.1	85.5
Bellevue	NA	79.0	106.3
Blair	100.1	41.1	89.6
Broken Bow	99.3	30.5	77.1
Chadron	96.4	69.0	81.4
Columbus	103.4	156.5	86.4
Fairbury	100.2	83.0	90.8
Falls City	100.3	352.4	87.7
Fremont	94.2	91.2	99.9*
Grand Island	100.1	66.6	88.2
Hastings	97.8	50.9	85.0
Holdrege	104.2	44.8	91.1
Kearney	100.7	97.1	84.6
Lexington	99.4	76.0	89.4
Lincoln	100.7	75.5	96.4
McCook	98.6	203.2	82.4
Nebraska City	106.6	161.4	85.6
Norfolk	100.1	76.4	92.3
North Platte	101.9	108.9	87.7
Omaha	NA	73.8	89.6
Scottsbluff/Gering	98.9	125.8	85.0
Seward	100.0	127.1	81.9
Sidney	99.4	160.3	87.5
So. Sioux City	NA	60.7	85.1
York	99.4	87.6	86.3

¹ As a proxy for city employment, total employment for the county in which a city is located is used.

² Building Activity is the value of building permits issued as spread over an appropriate time period of construction. The U.S. Department of Commerce Composite Construction Cost Index is used to adjust construction activity for price changes.

³ Power Consumption is a combined index of consumption of electricity and natural gas except in cases marked * for which only one is used.

Source: Compilation by Bureau of Business Research from reports of private and public agencies.

January 1980	Index (1967 = 100)	Percent of Same Month Last Year	Year to Date as Percent of Same Period Last Year*
Consumer Prices	233.2	113.9	113.9
Commodity component	222.4	113.6	113.6
Wholesale Prices	254.7	115.4	115.4
Agricultural Prices			
United States	239.0	101.7	101.7
Nebraska	250.0	105.5	105.5

*Using arithmetic average of monthly indexes.
Sources: Consumer and Wholesale Prices: U.S. Bureau of Labor Statistics; Agricultural Prices: U.S. Department of Agriculture.

WHAT CAN BE DONE TO LESSEN THESE COSTS?

The regulatory effort to keep deposit rate ceilings in place is reminiscent of the final stages of our nation's involvement in the infamous Vietnam War. Federal authorities have focused their energies on a few enclaves of savings funds, while guerrilla action has moved more and more household wealth to areas beyond regulators' sphere of control. When the current extension of deposit-rate ceilings expires in December 1980, authorities should plan to accept a staged withdrawal.

In the meantime, much could be done to undo at least the grosser elements of discrimination against small savers that is inherent in the current regulatory structure. First, early withdrawal penalties applicable to certificate accounts could be lightened or (better) deregulated completely. Current penalties impose an excessively punitive forfeiture of promised interest, one that is unrelated to differential costs that early withdrawals actually impose on depository institutions. Households that cannot *confidently* put funds aside until a certificate's maturity date have more to lose than to gain from buying a certificate whose maturity matches the holding period planned for their savings.

Second, the discriminatory effect of early withdrawal penalties need not be heightened by restrictions to minimum denominations. These restrictions could be abandoned or at least relaxed to allow institutions to assist their customers to *pool* their funds into eligible amounts.

Third, the principle of variable-rate ceilings—so successful in

the case of money-market certificates—could be extended to pass-book accounts.

Fourth, almost no justification exists for regulating interest rates on intermediate and long-term certificates of deposit. Treasury officials could induce industry pressure against regulatory ceilings and minimum denominations for long CDs by offering U.S. savings bonds at more competitive rates and maturities.

A MORAL PERSPECTIVE

In conclusion, let me emphasize that the issue is *not* whether homebuilding or thrift institutions should be subsidized. *Whether* to subsidize something and *how to finance* the resulting subsidy are separate issues. Deposit rate ceilings are far from the only way to help homebuilding and thrifts. The ceilings are merely the *sneakiest* way. They hide the subsidies from public view and leave the dollar magnitudes involved hard to evaluate.

The issue is, who should ultimately pay the freight for subsidizing S&Ls and housing, if indeed the government wants the subsidization to continue. The overriding question is whether our current *means* of helping the beneficiary industries—by a discriminatory system of deposit-rate ceilings—is morally defensible. How can we pretend that the end justifies the means?

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HIGHER INTEREST RATES ON SAVINGS

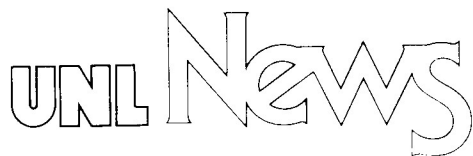
President Carter signed legislation permitting banks and savings institutions to pay higher interest rates on consumer deposits. The legislation also significantly expanded the Federal Reserve Board's regulatory authority.

The law permits a five-member board to supervise a six-year phaseout of interest ceilings on savings deposits. The legislation established a goal to increase interest ceilings of 0.25 percentage point during the next eighteen months, 0.5 percentage point in the subsequent eighteen months, and 0.5 percentage point per year in the final three years of the phaseout period. Over this six-year interval, regulated rates on savings accounts would be permitted to rise a total of 2.25 percent.

It is hoped that the elimination of interest rate ceilings will stimulate savings by consumers, especially small savers. Regulation Q, according to Professor Kane in the current issue of *Business in Nebraska*, has adversely impacted consumer savings.

The bill also permits interest payments on checking accounts; establishes uniform reserve requirements for all banks; eliminates state usury ceilings on home mortgage rates and business and agriculture loan interest rates (unless state legislatures override the legislation within three years); and increases from \$40,000 to \$100,000 the amount of bank deposits insured by the Federal Deposit Insurance Corporation.

D. E. P.



BUSINESS IN NEBRASKA

PREPARED BY BUREAU OF BUSINESS RESEARCH

Member, Association for University Business & Economic Research

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No. 428 May 1980

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