

MUTUAL SAVINGS BANKS

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I

To understand the investment problems and policies of mutual savings banks one must recall the nature and origins of these institutions. Mutual savings banks have no capital stock; they are operated by trustees solely for the benefit of the depositors, who receive as interest-dividends the earnings that remain available after payment of expenses and establishment of reserves against loss and surplus. The first mutual savings banks in the United States were formed in 1816. Two years later some of the organizers of the Bank for Savings in New York City termed their plan "A Bank for the Poor," designed "to effect a secure place of deposit for the laboring part of the community."¹

The movement spread rapidly through the eastern section in which there were an emerging working class lacking outlets for its funds and groups of public spirited citizens willing and able to organize and operate such institutions. Today there are 529 mutual savings banks in 17 states, with resources at mid-1951 aggregating 22.9 billion dollars, but all except 3 per cent, both in number and resources, lie "east of Buffalo and north of Baltimore." Throughout its history the mutual savings bank has emphasized its role as the bank for the "little fellow" and has been conscious of its quasi philanthropic origins. The law has usually limited the maximum size of the individual account; for example in New York at present to \$10,000, and its average account today stands at \$1,051.

The field of service of the mutual savings banks explains both the investment policy which they follow and the legal restrictions which set the framework within which that policy operates. Safety is paramount in the investment of their funds, both because of the nature of their depositors and because there is no stockholders' equity to cushion the investment of the funds supplied by the depositors. A major protection against adverse investment conditions can be furnished present and future depositors only by building up adequate reserves and surplus from the earnings on the banks' investments. That they have been successful over the years in achieving safety of their depositors' funds is shown by the enviable record of the mutual savings banks, in contrast to that of other institutions, in respect both to involuntary closings and to losses to depositors. Since savings bank deposits, despite the legal permission in most states to require 30, 60 or 90 days' notice of withdrawal,

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¹ CHARLES E. KNOWLES, *HISTORY OF THE BANK FOR SAVINGS IN THE CITY OF NEW YORK, 1819-1929* 16 (2d. ed. 1936).

are essentially liabilities payable on demand, the banks have also had to achieve liquidity. This has not been a major problem, reflecting in part relative stability in their deposit liabilities, and can be achieved from a limited section of their portfolios. Finally, in their investment policy the banks have sought to achieve the highest yields consistent with these two requirements of safety and liquidity.

Most of the 17 mutual savings bank states have enacted legislation regulating savings bank investments. The legislation restricts the banks to investments meeting statutory requirements designed to ensure high quality. In general, the requirements relate to type of security and the industry, size, and past financial results of the issuer. Since savings banks have long been regarded as institutions dedicated especially to serving their own communities, in some cases the laws also favor investments within the individual state by placing limits on the geographic area in which debtors reside, or by making more severe the standards which out-of-state investments must meet. In order to promote diversification in investments, some maximum limits have also frequently been set on certain classes of investments.

The mutual savings bank is also circumscribed by the available supply of legal investments. The relative supply of legal investments which is available changes over a period of time as the result of several factors. First, the supply varies with the ebb and flow of demands for loans as well as with changes in the volume of new issues and retirements of legally qualifying securities. Second, the volume of investments meeting fixed statutory requirements will tend to rise in prosperity and fall in depression. Third, the supply of available investments will change as new types of securities are added or legal standards imposed on individual securities of types already qualifying, are changed. Finally, since the savings bank is only one institution in a highly competitive market for investments, the supply of available investments at different times in effect also reflects the interest displayed by other classes of institutions in the several classes of investments.

Within the limits set by law and by the available supply of legal investments, the savings bank is a free agent in selecting the particular investments it will hold. The relative attractiveness of different investments reflects the relative rates of return available after allowing for investment expense and the relative degree of risk involved, and calls for a high degree of judgment on the part of the banker as to present conditions and prospective developments.

At the close of 1950 the mutual savings banks had invested almost half their funds in United States Government obligations, somewhat more than one third in mortgage loans, and less than one tenth in corporate securities. Table I, indicating the dollar amounts and per cent of total assets held in these and other forms on December 31, 1950, is based on data compiled by the National Association of Mutual Savings Banks from reports of the supervisors in the various states or obtained direct from individual banks. The figures used are, in general, net after deduction of reserves or valuation allowances. Of course, wide variation exists, both between states and between individual institutions, in the types of investment holdings.

II

Both historically and in point of fact, the investment policies of trustees and of mutual savings banks have been closely related. Having noted this fact, let us observe at once that in both fields the task faced by the state of ensuring adequate investment can be tackled in one of two ways. Only 2 of the mutual savings bank states follow the "prudent man" rule, namely Maryland and, with minor modification, Delaware. They permit the bank a wide range of latitude in which to exercise its discretion, provided it acts with prudence and in good faith. The other 15 states instead incorporate certain statutory requirements which form the basis for preparation of a legal list from which investments may be chosen. There are numerous conflicting standards due, usually, to historical influences, rather than to well defined policies designed to meet existing needs.² Also, the special charters held by certain older institutions set the investment restrictions under which they operate.

The laws governing mutual savings bank investments have by no means been static. There has been a continuous extension of the list of eligible investments, reflecting both the pressure of funds upon limited outlets and changing thought on investments as conditions changed. Even before the days of general acts of incorporation for savings banks, institutions experienced difficulty in investing their funds because of the few eligible categories. From time to time, economic change has resulted, first in the emergence, and then in the seasoning of new types of securities, which have sooner or later become recognized as suitable for mutual savings bank investment. The expansion of the list is well illustrated by the experience of New York state. The first general act, passed in 1875, restricted investments to three groups: United States Government issues, direct or guaranteed; obligations of states and New York municipalities; and first mortgage loans under specified restrictions. In 1898 certain railroad securities were added, and in 1904 a general law set forth a general earnings standard for rail issues. The real estate boom after the First World War, to make up for the housing shortage that had developed, helped postpone major revision. Only such minor changes were made as the admission of bankers acceptances in 1918. After discussions lasting almost a decade, New York in 1928 and 1929 became one of the last mutual savings bank states to admit public utility bonds to the legal list. At the same time, a wider selection of railroad securities was admitted and municipal bond restrictions were eased. Out of the depression arose, in reference to mortgages on real estate, formation of the Institutional Securities Corporation, the more liberal F.H.A. and V.A. lending provisions, and direct investment in housing corporations. In reference to security issues, there was the moratorium waiving temporarily the restrictions on railroad obligations, formation of the Savings Banks Trust Company (aside from its service as holder of cash balances of and lender to savings banks), and, in 1938, permission to the State Bank-

² White and Lawres, *The Modernization of Legal Lists*, 5 *LAW & CONTEMP. PROB.* 398 (1938).

ing Board to permit investment in specific corporate bonds upon recommendation of 20 savings banks or the Savings Banks Trust Company.

The problem of the magnitude and scope of the legal list for mutual savings banks may be indicated as follows. No tests are obviously provided for United States Governments, while mortgage lending in all 15 states has to meet specific standards. Admission of F.H.A. and V.A. loans means merely that the state accepts Federal Government standards instead of laying down its own. In nature the specific standards applicable to mortgage lending differ greatly from those applicable to municipal and corporate securities. It is on the latter group that the discussion of the legal list problem has centered. In 1950, as already noted, they comprised less than one-tenth the assets, after, as will be seen in Table 4, having stood at roughly one-third in 1920 and 1931.

Whether a legal list of securities is desirable, has actively been discussed for several decades. In favor of setting standards by law is the thought that, because of their very nature, the investment of savings bank funds should be safeguarded. Such restrictions were undoubtedly important during the earlier years of mutual savings banking when newly organized institutions often had to "feel their way" and were mostly operated by individuals who donated a portion of their time, instead of by full-time paid executives. But over the years several principal defects of the legal list have become increasingly evident, and it is upon them that discussion has focused.

(1) It is impracticable to devise fixed statutory standards which admit a large proportion of all sound securities without also qualifying a considerable volume of questionable securities.³ The standards now employed differ between states, so that perhaps only half or somewhat more than half the issues are common to several lists. The remainder meet only some of the tests set by each state, rather than all. They belong to the great bulk of securities that are neither distinctly superior nor distinctly inferior, yet which are generally satisfactory for investment, both in terms of safety and of yield. No legal list, if it is to be of use, can confine itself to the limited group of outstanding issues of unquestionable security, but must reach into the much larger stratum underneath, where doubt, even if of a minor nature, may appear. Yet in connection with such issues the usual standards set in the various laws give us the well known phenomenon of "good" issues barred because of non-compliance with purely technical considerations while also admitting what turn out actually to be "poor" securities.

(2) The wide cyclical changes that occur in the size of the legal list are undesirable. They occur because, first, most tests rely upon past in contrast to prospective performance, which frequently reflects factors that are intangible in nature. Second, changes in the size and composition of the legal list provide an

³ See George W. Edwards, *New Standards for Railroad Securities*, in *TRUST COMPANIES* 174 (1937). The exhaustive studies now being completed by the Corporate Bond Project of the National Bureau of Economic Research also shed much light upon the matter.

incentive for banks to buy at the "top" and sell at the "bottom"; they lead to unnecessary liquidation at low prices and thus to further depression of prices.

The outstanding example of difficulty in connection with legal lists is afforded, of course, by rail bonds during the 1930's. In this case, secular were added to cyclical factors; the changed position of the roads with the development of newer means of transportation, had also been ignored. Legislation had to be enacted in various states permitting retention of issues which no longer met the legal standards. In New York 7.6 billion dollars of rail obligations were legal at the opening of 1931, but less than 1 billion dollars qualified two years later, with 5.8 billion dollars remaining legal only under the moratorium.⁴

The problem is not completely solved by use of a variable standard such as that advanced in New Jersey in 1946. Instead of the usual constant ratio of earnings to fixed charges, the arithmetic average of all Class I railroads for the three preceding years was used. While a test of 50 important Class I roads showed that none of the 18 eligible for the period ending 1929 was forced into bankruptcy or obliged to put through a voluntary plan of readjustment involving placing part of the road's fixed charges on a contingent basis, only half of the 18 would have remained on the legal list in 1945 as well as 1932, while 31 roads met the test in at least one three-year period. In short, while the aggregate volume of legal bonds would have been better maintained under the plan, there would have been considerable shifting about as a result of changes in the operating results of the roads involved. The list would remain larger in size at the expense of stability in composition.

(3) The pressure of investment demand on a limited list of securities creates artificially low yields which handicap the mutual savings banks *vis-a-vis* competitors not similarly restricted. This has been a periodic complaint, highlighted at times by the fact that the mutual savings banks are largely, and in some states entirely, confined to creditor instead of equity securities—a matter which is considered below.

Recognition of defects has led some of the 15 states to introduce provisions to achieve flexibility as a substitute for or, more largely, as a supplement to the rigidities imposed by fixed statutory requirements. These provisions are of several types.

(1) *Supervisor discretion in preparing list*: Ohio permits investment in the marketable obligations of any corporation under such restrictions as may be prescribed from time to time by the superintendent of banks with the approval of the Banking Advisory Board.

(2) *Consultation with savings banks in preparing list*: Maine in 1937 authorized the bank commissioner, upon recommendation of a special committee of the savings bank association, to expand the list to include certain railroad securities he deems suitable for investment by savings banks. A year later New York empowered its state banking board, upon recommendation of 20 savings banks or the Savings Banks Trust Company, to add to the regular list corporate interest-bearing obligations

⁴ WELDON WELFLING, *SAVINGS BANKING IN NEW YORK STATE* 127 (1939), citing data of the New York State Banking Department.

not otherwise legal for investment. Massachusetts permits the commissioner, on application of 25 savings banks, approved by the Mutual Savings Central Fund, to admit any state or municipal or corporate interest-bearing obligation not otherwise eligible. Connecticut has set up a Savings Banks Railroad Investment Committee, appointed by the governor, on which the savings banks are largely represented, to certify to the commissioner the rail bonds it deems suitable for investment, instead of spelling out standards in the law, as for other classes of securities.

(3) *Limited investment in non-legal issues:* Minnesota permits 10 per cent of deposits to be invested outside the authorized list, under rules of the state banking commissioner, who limits such investment to marketable bonds, domestic or Canadian, payable in American dollars, and rated A; Connecticut permits 75 per cent of surplus to be placed in non-legal issues deemed prudent investments by the bank.

(4) Indiana restricts savings bank investment in corporates to those legal for fiduciaries and approved by the department of financial institutions.

(5) Vermont restricts investment in corporates to domestic and Canadian evidences of debt rated within the first four grades by two recognized investment rating agencies.

III

At the close of 1950 the mutual savings banks held 8.0 billion dollars, or 35 per cent of their assets, in mortgage loans. They included conventional and purchase money mortgages, 63 per cent; F.H.A.'s, 20 per cent; and V.A.'s, 17 per cent. In addition, they held a limited amount of construction loans.

In their regular or conventional mortgage loans, savings banks in the 15 states are quite generally confined to first mortgages. The further usual requirements, relating to location of the property, percentage of value that may be lent, and maximum aggregate holding of mortgage loans, may be summarized as follows.

(1) In general, the property must be located within the state in which the bank is located, or, if in another state, within 25 miles of the bank or in an adjacent county. This provision reflects the conception of mutual savings banks as institutions designed primarily to serve the communities in which they are located, as well as the thought that they can keep well informed as to real estate developments in their vicinity. But certain states in which opportunities for mortgage lending are limited permit loans elsewhere. Thus, Maine authorizes loans anywhere in the United States. Again, Minnesota and Wisconsin permit loans in their (somewhat differing) group of states, and Oregon admits loans in the Pacific states.

(2) The maximum percentage of the value of the property that may be loaned, is usually specified. Most common are percentages around 60 and 66 $\frac{2}{3}$ per cent. But the percentage is often graded, with higher percentages on improved than on unimproved property; on amortized than on unamortized loans; and on small residences (variously defined as single family, one or two family, and up to four family) in

contrast to multifamily housing and nonresidential property. The figure ranges all the way from 30 or 40 per cent on unimproved property to 80 per cent on small residences when the loan is amortized monthly, usually over 20 years. The 80 per cent may apply to the first \$10,000 to \$15,000 of the value, with a lesser percentage applicable to any excess. Some states include requirements for appraisal by trustees and for periodic reappraisal of the property.

(3) The maximum aggregate holding of mortgages is also specified by most states. A percentage of assets, varying from 50 to 75 per cent, is usual, or a percentage of deposits, varying from 60 to 75 per cent. Within these ranges, the lower are less frequent than the higher figures. A lesser percentage may apply to loans outside the state.

All mutual savings bank states authorize these institutions to hold F.H.A. insured mortgages. In general, the standards set by the F.H.A. and the federal legislation under which it operates, are accepted and no further restrictions are made. But in a few cases this type of investment is made subject to such regulation as the state supervisor deems "necessary and proper." In some cases, the permission was originally limited to mortgages on property located within the state. Sometimes F.H.A. lending comes under the overall limits set on maximum aggregate holdings of mortgages already cited, although rarely, as in Maine, the aggregate percentage may be increased from 60 to 70 per cent in case F.H.A. holdings comprise not less than 25 per cent of deposits. The authorization often includes modernization loans in moderate amount as well as long term mortgages.

Similarly, all mutual savings bank states permit these institutions to hold G.I. loans. For savings banks, the important loans are those made against real estate rather than business loans. In various states, the loan guaranteed by the V.A. is also made subject to such regulations as the supervisor deems "necessary and proper." Some states set forth conditions relating to matters such as location of the property and the minimum percentage of loan guaranteed. Savings banks have made some combination F.H.A. and V.A. loans.

Some banks originate and service their own loans. Others, however, acquire existing loans, either through correspondents or, within recent years, by taking over a block from the H.O.L.C. or the Federal National Mortgage Corporation. Depending upon competitive conditions, a premium may be paid for loans purchased, and the correspondent usually retains the right to service the loan for an annual fee such as $\frac{1}{2}$ of 1 per cent. There has been sharp competition for loans up to recently, so that refinancing with another institution has been frequent. So, too, has been repayment on loans in excess of that provided by the amortization schedule. As a result of both practices, repayments in 1950 were 14.5 per cent of the mortgages held when the year opened and 38 per cent of the total lent during the year. In other words, the mutual savings banks had to make about \$1.60 in new mortgage loans in order to show an increase of \$1 in the volume of mortgages held.⁵ The remaining 60

⁵ Repayments were relatively heaviest on conventional mortgages and lightest on FHA's, with corresponding effect on the amount which had to be lent to gain \$1 of loans held.

cents was absorbed by repayments from borrowers, often as a result of a new loan negotiated elsewhere.

Out-of-state mortgage lending by savings banks is of two types. Of minor importance is lending in a contiguous state. Vastly more important is lending regardless of location, today largely represented by F.H.A. loans. Individual banks may make their own arrangements to acquire mortgages through correspondents which act as servicing agent, but New York banks can use the facilities of the Institutional Securities Corporation which is owned by them. At the close of 1950 it had outstanding 46 million dollars of debentures held by the savings banks against its portfolio, composed predominantly of F.H.A. and V.A. mortgages, and also held 111 million dollars of F.H.A.'s as trustee or agent for investing savings banks to which it issued certificates of participation. In 1949 the Massachusetts banks organized a purchasing group, joined during the first year by 32 banks, which took allotments of the F.H.A. and V.A. purchases which were negotiated.

Of the 8.0 billion dollars of mortgages held by the savings banks at the close of 1950 about 1,250 million dollars or 15.5 per cent were on properties situated outside the state in which the bank was located. In addition, the banks held out-of-state commitments aggregating about 700 million dollars. Three quarters of the total loans and commitments are held by New York banks and another one eighth by Massachusetts banks, but out-of-state lending also bulks relatively large in Vermont, Rhode Island, and Minnesota. Three fifths of the out-of-state loans and commitments are on properties in other savings bank states, notably New Jersey, Pennsylvania, and, to a lesser extent, Maryland. The remaining two fifths is scattered widely over almost all the 31 non-mutual savings bank states, the District of Columbia, and Puerto Rico, but over two thirds is in 8 jurisdictions.

It is evident that mortgage loan policy varies widely from bank to bank. At the close of 1950 the per cent of assets placed in mortgage loans varied from 1 to 86, but about two thirds of the banks held between 20 and 50 per cent of their assets in mortgages. Some banks confine themselves to a limited number of conventional loans, covering commercial and multifamily residential structures; others favor a large number of loans on small residences. Again, some institutions prefer conventional mortgages and take no F.H.A.'s, while others have built their mortgage portfolio around F.H.A.'s. Similar differences appear by states. Thus, in the 10 major mutual savings bank states the percentage of the mortgage volume held at the close of 1950 in the form of F.H.A.'s varies all the way from less than 10 per cent in Massachusetts, New Jersey, and Connecticut to roughly 25 per cent in Rhode Island and 40 per cent in Vermont. These figures show the accumulated portfolio, rather than current lending; some states were building up their F.H.A. portfolios rapidly in 1950. The proportion of V.A. loans held showed a much narrower range, varying from roughly 15 to 30 per cent. So, too, did the proportion of conventional loans held, which ranged from about 58 to 70 per cent when Vermont (holding over

two thirds its mortgages in the other two forms) is omitted. The three states with a low percentage of F.H.A.'s showed the highest proportion of conventional loans.

Are mortgage loans good investments in view of the severe losses experienced by mutual savings banks during the period 1931-45—far more severe, in fact, than were the losses on their security holdings? The only comprehensive study of the matter is that made by Dr. John Lintner of Harvard University of the experience of the mutual savings banks in Massachusetts. He concludes:⁶

Mortgage lending has been good business for the mutual savings banks of Massachusetts, not merely from the standpoint of discharging a basic responsibility to their communities and to the economy, but also from the standpoint of increased net returns available for distribution as dividends to depositors after full allowances for all costs and losses incurred.

The evidence upon which he bases these conclusions may be stated, with his permission, as follows:

(1) There is the experience of the Massachusetts saving banks over the years. The period 1907-25 was one in which lending was heavy, rates attractive, and losses low. This had, in fact, been true also for the preceding quarter century. Real estate conditions began to become unfavorable beginning about 1926, although real difficulty only began to be experienced from 1931 on and the heaviest losses, in fact, were taken by the banks in the later 1930's and early 1940's after real estate had already begun to improve. The net yields for the periods 1907-25 and 1926-45, as well as that for the years of difficulty 1931-45, are indicated in Table 2.

(2) These results, based upon data contained in the Commissioner's reports, are confirmed by analysis of a large representative sample of loans made between January 1, 1918 and December 31, 1931, which shows an average net return down to mid 1946 of 4.64 per cent a year. This is again substantially higher than the average yield obtainable on long term United States Government bonds at any time after 1921. The net return obtained on all mortgage loans made each year 1919 through 1931, except 1920 and 1923, was also higher than the average yield of long term United States Treasury securities during the year in which the mortgage loans were made.

(3) The data cover uninsured loans in a period of extreme distress. Techniques of selecting risks (including credit study and income prospects of borrower and neighborhood trends), form of the mortgage instrument (including periodic amortization and current payment of taxes), and the amount and quality of service, have all improved very substantially over the last 15 years. Moreover, F.H.A. and V.A. insurance and guarantees bear little similarity to the older guaranteed mortgage whose record was so disastrous. On the other hand, we may add, a substantial fraction of present portfolios is made up of loans made in a period of high real estate prices, and frequently at a higher per cent of appraised value than was permitted during the 1920's.

⁶ JOHN V. LINTNER, *MUTUAL SAVINGS BANKS IN THE SAVINGS AND MORTGAGE MARKETS* 310-311 (GRADUATE SCHOOL OF BUSINESS ADMINISTRATION, HARVARD UNIVERSITY, 1948).

Recent laws in about one third the mutual savings bank states authorize these institutions to participate in financing large scale housing developments. The laws differ greatly. Some authorize investment in obligations of a public housing authority, urban redevelopment company, private housing company, or similar public or private corporate entities. A second type allows savings banks to participate with other savings banks or other mortgage lenders either in making mortgages secured by large scale housing developments or in purchasing such real estate and owning it outright. Allied hereto is the authorization given savings banks by other states to participate in such financing through the medium of a corporation wholly owned by savings banks. Finally, another form of law authorizes savings banks to participate in mortgages on large scale housing when these are insured by the F.H.A. Savings banks have displayed some interest in the field, but have undertaken construction of only a limited number of housing projects themselves, due to the rise in construction costs.

Loans other than on real estate are of minor importance, and will not be considered here. Instead, we will turn at once to the banks' security holdings.

IV

At the close of 1950 the mutual savings banks held 10.9 billion dollars or 48.6 per cent of their assets in direct or guaranteed obligations of the United States Government. In addition, they held 77 million dollars or 0.3 per cent in Canadian or other foreign government bonds. Most states admit Canadian but not other foreign obligations.

Holdings of state and municipal obligations totalled 92 million dollars, or 0.4 per cent, on December 31, 1950. With the sharp rise in federal income tax rates, the tax exempt status of such issues has had increased appeal to other classes of investors as contrasted with the mutual savings banks, which until 1952 were free of federal income tax. Obligations of states are generally admitted, subject frequently to non-default for a specified period such as 5, 10, or 20 years, in several cases on obligations issued after 1878 or 1890. In rare cases, a limit is placed on total holdings of state obligations, such as 20 per cent of assets, or of any one state, such as 2 per cent.

The legal requirements governing investment in obligations of political subdivisions of a state are far more extensive and technical. Most states permit investment in the obligations of their own subdivisions without limit. Standards instead are imposed on obligations of subdivisions in other states and relate to matters such as population, taxing power, and amount and character of debt burden. Some also require that the unit shall have been in existence for a specified period, ranging from 10 to 25 years. More frequent is a requirement that there shall have been no default for a stated period, usually 10 but ranging from 5 to 25 years. Population requirements vary widely, with frequent correlation to debt limits. Thus Massachusetts limits the ratio of net debt to assessed value of real property to 6 per cent in cities of less than 100,000 and 8 per cent in larger centers. Incidentally, the debt limit

requirement, ranging from 3 per cent to 12 per cent, raises a question as to whether obligations for financing municipal utilities should be included in its computation. The requirement is sometimes also made that in order to qualify its obligations the unit shall have unlimited power to tax real property for the payment of the obligations. Several states limit aggregate investment in municipal obligations, as well as that in the obligations of any one municipality.

Mutual savings banks holdings of corporate securities are also small in comparison with holdings of United States Governments, though large in contrast to state and municipal obligations. At the close of 1950 rail and public utility bonds each aggregated 865 million dollars and represented 3.8 per cent of the portfolio, while industrial bonds equalled 119 million dollars and added 0.5 per cent. While some observations have already been made on the shortcomings of the legal list for rails, the conventional standards contained in the various laws may be examined briefly. They are extremely technical and often overlap, but their principal features may be summarized under the following headings:

- (1) *Size*. A frequent requirement is that a road must have a minimum single track mileage of 500 miles; another that minimum gross operating revenue be 10 or 15 million dollars for a period such as 3 of the last 4 or 5 of the last 6 years.
- (2) *Earnings*. A frequent requirement is that a road must have shown available earnings $1\frac{1}{2}$ times fixed charges for some period such as the last year and either the average for the last 5 years or 5 of the last 6 years.
- (3) *Dividends*. New York requires that payment of cash dividends equal one fourth fixed charges in 5 of the last 6 years, unless fixed charges were earned $1\frac{1}{2}$ times in 9 of the last 10 years.
- (4) *Capital structure*. Another test is that funded debt does not exceed 3 times capital stock.
- (5) *Nature of security*. Provision is made for admission of terminal and bridge bonds and bonds on leased lines, as well as for mortgage bonds on owned property, to take account of the intricate capital structures of many systems.
- (6) *Limits*. The usual aggregate limits are often set, such as 20 or 25 per cent of assets or 30 per cent of deposits and $1\frac{1}{2}$ to 5 or 10 per cent for one road.

Massachusetts, it may be noted, has added a comparative type of test. Despite the shortcomings of the New Jersey plan based on the arithmetic average for all Class I roads, Massachusetts now requires that (a) for a 3 year period, gross revenue average $\frac{1}{4}$ of 1 per cent of that for all Class I roads; (b) average earnings cover fixed charges, not only at least $1\frac{1}{2}$ times, but also at least as much as for all Class I roads; and (c) the margin of safety (average income less fixed charges, divided by average gross revenues) be at least equal to that for all Class I roads. The Commonwealth has also provided modified requirements for reorganized roads' obligations.

Rail equipment obligation standards may more easily be summarized. The nature of the lien is specified, the obligations may not represent more than 80, 85 or 90 per cent of the cost of the equipment, and the maximum maturity is 15 years, subject to annual or semi-annual reduction in equal installments.

Public utility bond standards on the whole are less intricate than those for rails, partly because they are a relatively recent type of obligation and the capital structure of such operating companies is today less complicated. Electric light and gas, water, and telephone companies are recognized, generally with separate though somewhat similar standards for each, but street railways play a subordinate role. The types of provision may be sketched as follows:

- (1) *Supervision.* Several states require that the issuer be under supervision of a public service commission.
- (2) *Franchise.* Several states which treat an in-state company more leniently than an out-of-state, require the issuer to have an exclusive franchise. A number require that the franchise either be indeterminate, subject to a public service commission, or determinate and expire at least 3 years after the bonds mature.
- (3) *Size and nature of business.* Minimum gross revenues are frequently set, and a minimum percentage that must be derived from electric and gas operations by non-water and non-telephone companies.
- (4) *Value of property.* Several states do not permit the bonds to exceed two thirds or three fourths the depreciated value of the property.
- (5) *Capital structure.* Several states require that funded debt shall not exceed a stated percentage of total capital, usually 60.
- (6) *Earnings.* Various states specify the minimum ratio of net earnings for a specified period to fixed charges. The period is often the last year and the average for the last 3 to 5 years or 4 of the last 5 years, while the coverage varies from $1\frac{3}{4}$ to $2\frac{1}{2}$.
- (7) *Debentures.* Where debentures as distinct from mortgage bonds are admitted, the standards are more severe. This is generally true also of telephone bonds, where coverage for debentures may be 3 instead of the 2 required for mortgage bonds.
- (8) *Limits.* The usual maximum percentages are set, both in the aggregate and for obligations of one issuer. Ranges are wide, from about 15 to 40 per cent, and from 2 to 5 per cent of deposits, respectively.

Investment in equities is another story. At the close of 1950 bank stock holdings were 163 million dollars, or 0.7 per cent of assets, while other stock holdings (omitting those in organizations such as the Savings Banks Trust Company) aggregated only 16 million dollars, or less than 0.1 per cent. In fact, bank stock is important only

in New England; Massachusetts and Connecticut account for four fifths of the total, but bank stock is at least relatively as important in savings bank portfolios in Rhode Island and New Hampshire. Other stock is of importance only in New Hampshire, in which the holdings exceed those of bank stock.

The bank or trust company whose stock may be held must meet certain standards, which may be summarized for the New England states as follows:

- (1) *Location.* All admit stock of institutions in their own state. Connecticut also permits holding of stock of institutions in New York City, Boston, and Philadelphia, while Maine and Vermont permit the institution to be located in New England or New York. Vermont also admits Canadian bank stock, while Massachusetts, New Hampshire, and Rhode Island permit a location anywhere in the United States. Population tests are set in Maine (cities of 250,000) for banks located outside the state, and in New Hampshire (cities of 500,000) and Rhode Island (cities of 200,000) for banks located outside New England and New York.
- (2) *Federal Reserve membership.* Investment is restricted to stock of Federal Reserve members by Maine and Massachusetts for banks located outside the state and by New Hampshire and Rhode Island for banks located outside New England and New York.
- (3) *Size.* A capital stock, surplus, and undivided profits of 10 million dollars is specified for banks located outside the state in Connecticut and Maine and 40 million dollars in Massachusetts. The figure is 15 million dollars in New Hampshire and 5 million dollars in Rhode Island for banks located outside New England and New York. In Rhode Island such an institution or its predecessors must be at least 10 years old.
- (4) *Dividends.* Dividends of 4 per cent must have been paid in each of the last 5 years by all institutions eligible in Connecticut and for intrastate institutions in Massachusetts, and, to be eligible in New Hampshire, for each of the last 4 years by banks outside New England and New York. Furthermore, a surplus equal to 50 per cent of capital stock is required for these categories by New Hampshire. Massachusetts requires payment of 4 per cent dividends in each of the last 10 years for out of state institutions and a stockholders' investment equal to 6 per cent of deposits.
- (5) *Aggregate holdings.* The maximum is related either to deposits (5 to 25 per cent), assets (10 per cent), or surplus (one half or two thirds). Moreover, holdings of the stock of one bank are limited, in relation to either deposits (0.5 to 3 per cent), assets (5 per cent), or surplus (5 per cent or one fifteenth). In order to prevent too close a link with a commercial bank, the per cent of the latter's capital stock that may be held is often

limited to from 10 to 25 per cent. In several cases the percentages include loans against stock of the bank, while several states also limit deposits held with a commercial bank.

The desirability of more widespread investment by savings banks in equities has been raised again since New York in 1950 became the fortieth state to permit life insurance companies to hold common stock, after having a year before authorized trust companies to place up to 35 per cent of the funds of "legal" trusts in equities. Increased interest on the part of institutions in equity securities is due, first, to the high yield that a portfolio of selected equities will give as against any other type of institutional investment. Over the past decade the differential has been unprecedented. High income taxes have removed many individuals in the middle and upper income brackets as purchasers of stock, while a greater portion of people's savings is finding its way into the hands of financial institutions which have placed them elsewhere than in equities. In addition to thus reducing demand for stock, bond yields have been depressed by credit control and debt management policies. Second, corporations over the last 5 years have retained over half their earnings, which have been reinvested for the benefit of stockholders and should lead to increases in earnings in the future.

Equities, of course, carry greater price risks, even though fluctuations may in the future be less extreme than between 1929 and 1932, when the Dow Jones average fell to 41 after having reached 381. Sounder business finance and commercial banking, coupled with restrictions on margin transactions and the policies likely under the Full Employment Act of 1946, may serve to place a "floor" under the market. At the same time, increasing earnings give an opportunity for secular appreciation, accelerated should inflation go forward. Savings banks could if permitted make their investments in equities directly or through intermediaries. Most institutions, particularly the smaller banks, lack the knowledge and experience essential to proper selection of issues and timing of purchases. They must either obtain competent advice, for example from a central bureau (perhaps, in New York, the Savings Banks Trust Company) or must participate through an intermediary. The latter in turn offers two alternatives. First, savings banks might buy shares of open and mutual funds, which have been selling their shares to the public at an increased pace in recent years. This has the defect of costliness—an average initial loading at time of purchase of 7 per cent or more, and an annual expense deducted from income running up to more than 0.5 per cent. The more promising alternative appears to be to have the savings banks, if permitted to make equity investments, set up their own mutual fund, with a specialized organization suited to their own needs.

V

The present investment problems and policies of the mutual savings banks can be understood only in the light of the historical record. During the first half

of the twentieth century they have faced two world wars and a major depression. All have left their mark on mutual savings bank investments. For our present purpose it will suffice to examine the period since the First World War. These three decades fall naturally into three periods:

- (1) The "decade" of prosperity—1921-31, inclusive;
- (2) The "decade and a half" of pressure—1932-45, inclusive;
- (3) The postwar era—1946-50, inclusive.

The decade of the 1920's seemed to the savings banks to be one of relatively smooth sailing. Their assets increased year by year during the 11 years ending in 1931, and almost doubled from the 5.8 billion dollars held at the opening of the period. Hence the problem facing the banks appeared primarily that of placing the 5.2 billion dollars of additional funds in the best of a group of outlets with generally attractive yields. In 1920, as shown in Table 4, the banks held 40 per cent of their assets, or 2.3 billion dollars, in mortgages and 33 per cent, or 1.9 billion dollars, in corporate and municipal securities. United States Government obligations, a heritage from the First World War, totalled only 900 million dollars, or 16 per cent. Over the decade, the banks placed somewhat more than the entire increase in their assets in private obligations in contrast to public. They increased their mortgage holdings to two and one-half times the 1920 figure and almost doubled their holdings of corporate and municipal securities. In other words, 3.6 billion dollars went into mortgages and 1.6 billion dollars into corporate and municipal securities (while holdings of United States Governments, reflecting in part retirement of public debt, declined 200 million dollars) to increase these to 53 per cent and 32 per cent of assets, respectively, in 1931. The concentration on mortgages reflected primarily the rapidly increasing supply of mortgages, due to new construction and increased transfers of existing properties. It also reflected the relatively favorable net yields, especially in view of the successful experience with mortgages over the preceding half century or so. As the demand for mortgage money fell off in the later 1920's, available corporate issues, both railroad and public utility, increased, with larger yields after early 1928. Rail obligations reached 14 per cent of assets in 1931 and utility issues 7 per cent.

The period beginning about 1932 and lasting through 1945 presents a sharp contrast. Private obligations absorbed none of the increase in assets, but suffered sharp reductions instead. All the asset increase, together with that obtained from liquidation of other assets, went into United States Governments. Thus the entire character of the banks' portfolios changed, so that in 1945 they held only 25 per cent of their assets in mortgages and another 7 per cent in corporate and municipal securities, in contrast to 63 per cent in United States Governments. Holdings of mortgages fell 1.7 billion dollars to 4.2 billion dollars, and of corporates and municipals 2.3 billion dollars to 1.2 billion dollars, whereas holdings of United States Governments rose nearly 10 billion dollars. The shift may be explained, as was

the policy of the 1920's, in terms of the availability and yield of the different classes of investments, in addition to the patriotic desire to aid the war effort. Over the entire period interest rates were falling and the differential in yield of these classes over Governments was narrowing, especially in view of the losses experienced on other classes of investments. Meanwhile, too, the par value of marketable United States Governments rose from 21 billion dollars in 1932 to 36 billion dollars in 1940 and 199 billion dollars at the close of 1945.

Two sub-periods may be conveniently distinguished between 1932 and 1945: the depression and recovery years through 1940, and the war years through 1945. They differ in rate of growth of assets and also in investment problems. Between 1932 and 1940 savings banks assets gained roughly only 900 million dollars. As the changed conditions, already evident before 1932, brought defaults on mortgage loans and on securities held, the savings banks were forced to re-examine and re-adjust their portfolios. This resulted in a reduction of 1.5 billion dollars, or 40 per cent, in corporates and municipal securities, to 2.0 billion dollars or 17 per cent of total assets. Railroad obligations were particularly hard hit, declining more than half, or 850 million dollars, to 700 million dollars, or from 14 per cent to 6 per cent of total assets. Public utilities and municipals each declined about one third, or 300 million dollars, to reach respectively 600 million dollars and 500 million dollars, or 5 per cent and 4 per cent of total assets. However, bank stocks actually increased 11 million dollars, to remain at one per cent of assets. The period also showed a decrease of 1.1 billion dollars in mortgage holdings, with an accompanying rise of 500 million dollars in real estate acquired in foreclosure or similar proceedings. Hence, mortgage loans fell to 4.8 billion dollars or 41 per cent of assets, while other real estate rose to roughly 600 million dollars or 5 per cent of total assets. This reflects a lag in mortgage demand and heavy repayments, combined with a reluctance to make new mortgage loans.

The war years 1941-45 added to the task of completing the re-adjustment of the portfolio that of finding an outlet for the 5.0 billion dollar increase in the banks' assets. The entire sum, together with 2.4 billion dollars derived from the reduction in other classes of investments, was placed in United States Government obligations and raised their total to 10.7 billion dollars, or 63 per cent of assets, at the close of 1945. Re-adjustment of the mortgage portfolio was largely completed; mortgages declined 600 million dollars to 4.2 billion dollars, or 25 per cent of assets, while other real estate declined 500 million dollars to a nominal figure below that of 1920. Holdings of corporate and municipal securities fell 800 million dollars, to 1.2 billion dollars, or 7 per cent of assets. Rails continued their decline, falling 200 million dollars, or one third, to 460 million dollars, or roughly 3 per cent of assets, while public utilities fell 100 million dollars, or one sixth, to 400 million dollars, or 3 per cent of assets. More spectacular was the drop of 400 million dollars or two thirds in municipals, to leave holdings at 200 million dollars, or 1 per cent of assets. Bank stock holdings remained almost unchanged in amount.

The investment problem faced by the mutual savings banks is seen more clearly when the operating record of these years is examined. While no adequate published figures are available for the country as a whole, there is available the careful study made by Lintner of the experience of mutual savings banks in Massachusetts, based largely upon the Annual Reports of the Commissioner of Banks of that Commonwealth. The experience in that state, it is believed, speaking generally, parallels that elsewhere. The following account is based, by permission, upon that study. During the 15 years 1931-45 the mutual savings banks of Massachusetts experienced net losses of 238.1 million dollars on their investments, as shown in Table 3, as compared with total assets of 2,317.7 million dollars held at the end of 1930. Total losses and charge-offs of 346.6 million dollars, excluding charge-offs at time of purchase of premiums on securities, were reduced by profits and recoveries on all assets of 101.4 million dollars and a return to surplus of 7.1 million dollars of previously established reserves. Mortgages accounted for three fifths of all gross losses and charge-offs, but due to the small profits and recoveries on them, accounted for three fourths of the net losses on all assets.⁷ Moreover, not only did mortgages entail heavier losses and relatively smaller recoveries than did securities, but there were highly significant differences in the time at which the losses were taken. Losses on securities were written off rapidly, whereas losses on foreclosed real estate remained relatively small in the early years of the depression. In 1940 the banks still had to make three fifths of all their write-offs on foreclosed real estate, in contrast to one third of the write-offs on securities. Otherwise stated, little more than one fifth of the gross losses taken on securities were deferred until time of final sale, but virtually three fifths of such gross charges on foreclosed real estate remained to be taken when the properties were finally sold.

The investment problems faced by the Massachusetts savings banks during this period had their impact on operating policies. The net loss absorbed during the 15 years was substantially more than one third larger than the book surplus at the beginning of the period. It could therefore come only out of net operating income remaining after expenses, despite the fact that such net operating income (reflecting the rapid and persistent decline in rates of earnings in the face of a continuing tendency for current expenses to rise) fell every year to 1941 from the 109.3 million dollars in 1930 and only recovered to 69.8 million dollars in 1945. In fact, the loss equalled almost one fifth of the net operating income over the entire 15 year period. Disregarding year to year fluctuations, the remaining four fifths was available for payment of dividends and for maintaining surplus, which stood at 8.5 per cent of deposits in 1930. The remainder was less than the average percentage distributed in

⁷ No breakdown is available for losses on different classes of securities, although it is known that losses on U. S. Governments (excluding the charge-off of premiums omitted in the calculation) were negligible, with the loss ratio on rails higher and that on public utilities lower than the average for all securities. The statistical record of U. S. Governments was aided by profits realized on such obligations.

dividends during the 1920's and far below the 90 per cent paid out in 1930. Thus the dollar amount of dividends paid fell off sharply until 1941, and the average rate paid fell every year during the entire period, from 4.73 per cent of deposits in 1930 to 1.77 per cent in 1945. By thus sharply increasing retained earnings at the expense of dividends, in the face of persistently falling net income, the savings banks succeeded in showing net additions to their surplus accounts which somewhat more than matched their growth in deposits, while covering out of the earnings all the losses which developed in their assets. Only by limiting dividend disbursements to 864.7 million dollars out of their net operating income of 1,190.7 million dollars, were the Massachusetts savings banks enabled to cover their net losses of 238.1 million dollars, yet increase their surplus to 9.73 per cent of deposits.

Savings banks have at times been criticized—as have other lenders—for not pursuing more liberal loan and investment policies in the depression. It is claimed that their standards were too severe and that the lack of loan and investment expansion in those years aided in prolonging if not intensifying the depression. The best answer to this attack is given by the above figures. No individual institution, conscious of its trusteeship to its depositors and faced with possible lack of new money, falling security prices, and mounting loan delinquencies, can act other than as the savings banks did. Countercyclical policy is a matter for concerted, not individual action.

The year 1945 represents the low point of savings bank investments in forms other than United States Governments. Thereafter, the rapid expansion of the public debt halted, while there was a substantial decline in the outstanding volume of middle and long-term issues in which savings banks are interested for investment. Gone, also, was the opportunity for profits in the Government bond account. Moreover, the drop in the price of long-term Governments on two occasions—the close of 1947 and the spring of 1951—when Federal Reserve support slackened, changed the disposition of many bankers to regard long-term Governments as a good secondary reserve. Over the recent 5 year period, therefore, savings banks have concentrated on private obligations. Over two thirds the gain in assets, or 3.8 billion dollars, has found its way into mortgages, increasing them to 8.0 billion dollars, or 36 per cent of assets, from the low of 24 per cent in 1946. Corporate obligations also almost doubled, reaching 2.3 billion dollars or 10 per cent of assets in 1950. Utilities more than doubled, with a gain of 470 million dollars, and rails did not quite double, with a gain of 400 million dollars, so that holdings of each now equal 865 million dollars, or 4 per cent of assets. Bank stock holdings rose by about 50 per cent but municipals fell more than 50 per cent. Meanwhile, holdings of United States Governments rose 200 million dollars to 10.9 billion dollars, but the proportion of assets represented declined to 49 per cent in 1950 from the peak of 63 per cent reached in 1946.

The situation of the mutual savings banks at mid-1951 may be summarized briefly as follows:

- (1) After a lag beginning in mid-1950, despite sharp competition from other classes of institutions, new money has resumed its flow in substantial volume into the banks.
- (2) With the decline in the volume of new construction, the available supply of mortgages has fallen. The amount of new lending by the banks has declined somewhat in recent months, having been maintained by the large volume of their outstanding commitments.
- (3) New corporate issues—for example, those of public utilities—have attracted some attention as an outlet for funds.
- (4) The pace of the decline in the banks' holdings of United States Governments has slackened. Reliance had been placed upon such issues to provide funds to take advantage of attractive investment opportunities in other fields, but the sharp drop in prices of long-term Governments when Federal Reserve support was relaxed in the spring of 1951 forced some institutions with heavy mortgage commitments to take losses on some of their Governments, hence tended to "freeze" the United States Government bond holdings of many institutions.
- (5) The voluntary credit restraint program and legislation in reference to terms on mortgages, is influencing the supply of new investments, as is the entire defense program with its rechanneling of economic activity.
- (6) The inauguration of federal taxation, effective January 1, 1952, on the income of mutual savings banks remaining after payment of interest-dividends to depositors and after building up of surplus and reserves to specified levels, may well help to alter greatly the composition of the banks' portfolios. For one thing, greater attention than heretofore may be given to tax exempt securities such as state and municipal obligations. More important, the interest of savings bankers in the expansion of the legal list may be stimulated, in order to increase their earning power. Particular attention may well be directed towards general admission of a moderate amount of equities, perhaps under some such limits as are applicable to life insurance companies, both because of their attractive yields and because of the low effective rate of tax applicable to dividends paid on them. Only 15 per cent of the dividends received by a corporation from another taxable corporation are taxable, so that the actual rate payable by a bank on the income received from its holdings of equities is only 7.8 per cent, in contrast to the regular corporate rate of 52 per cent applicable to income derived from interest on loans and non-tax-exempt bonds.

- (7) Should those savings banks with adequate surplus (where required, with the approval of their supervisors) increase the rate paid their depositors, the inflow of funds to the banks might well be accelerated, and their own pressure for additional investment outlets be reenforced. But various matters in connection with the tax remain to be clarified and the complete effects cannot be clearly foretold at this time.

TABLE I
PRINCIPAL FORMS OF ASSETS HELD BY MUTUAL SAVINGS BANKS
December 31, 1950
(Dollar amounts in millions)

	Amount	Per Cent
Real Estate Financing:		
Mortgage loans.....	\$ 8,017.7	35.7
Other real estate (acquired under foreclosure, etc.).....	7.6	.0 *
Other Loans:		
Personal and collateral loans.....	91.4	.4
Loans to municipalities and corporations.....	29.5	.1
Securities:		
Bonds:		
Government:		
U. S. Gov't, direct and guaranteed.....	10,888.0	48.5
Canadian and foreign government.....	77.1	.3
State and municipal.....	92.1	.4
Corporate:		
Railroad, including terminals and equipments.....	864.6	3.8
Public utilities, including electric, gas, water, telephone, and street railway.....	865.0	3.8
Industrial.....	118.6	.5
Miscellaneous.....	129.1	.6
Stocks:		
Bank.....	162.9	.7
Other.....	15.7	.1
Acquired to settle debt and under agreement.....	4.9	.0*
Facilitating:		
Cash on hand and in banks.....	797.1	3.5
Banking house, including furniture and fixtures.....	110.5	.5
Investment in deposit insurance funds, etc.....	47.8	.2
Other, including advances for taxes and insurance, and interest accruals....	104.9	.5
	\$22,424.4	100.0

*Less than $\frac{1}{2}$ of 1 per cent.

TABLE 2

SUMMARY OF MORTGAGE LOAN EXPERIENCE OF MASSACHUSETTS SAVINGS BANKS ON
MORTGAGES OUTSTANDING IN SPECIFIED PERIODS

Period	Average Gross Return Per Year	Average Losses on Foreclosed and Outstanding Mortgage Portfolios Taken During Period As a % of Average Portfolio	Net Return on Mortgage Portfolios After Allowing for all Losses and Costs* at 0.4% Per Year
1907-25....	5.16%	0.02%	4.6%
1926-45....	5.19%	0.87%	3.9%
1931-45....	4.96%	1.16%	3.4%

*Acquisition and servicing.

Source: Computed by LINTNER, *op. cit.* supra note 6, at 308 (table 40), from ANNUAL REPORTS, COMMISSIONER OF BANKS, COMMONWEALTH OF MASSACHUSETTS.

TABLE 3

PROFIT AND LOSS ON ASSET ACCOUNTS IN MASSACHUSETTS SAVINGS BANKS: 1931-1945
(In millions of dollars)

	Gross Charge-offs and Losses	Profits and Recoveries	Adjustments for Reserves	Net Losses
Foreclosed Real Estate.....	\$169.7	\$ 16.0	{ -3.3 ¹ +2.5 ²	\$152.8
Other Real Estate Mortgages ³	38.1	5.2	{ -2.5 ² -2.8 ¹	27.6
Subtotal: Real Estate Mortgages.....	207.8	21.2	-6.1	180.4
Other Loans ³	9.0	0.3	0	8.7
Securities.....	121.1 ⁴	76.6 ⁴	-1.0 ¹	43.5
Miscellaneous.....	6.8	3.3	0	3.6
Total Allocated Losses.....	344.7	101.4	-7.1 ¹	236.2
Plus: Losses Charged Directly to Guaranty Fund ⁵	1.9	1.9
Total.....	346.6	101.4	-7.1	238.1

¹Published data in the Commissioner's Reports indicate that a total of 7.1 million dollars of reserves set up to cover losses were returned to the profit and loss account. Unpublished data in the Commissioner's office indicate that 3.3 million dollars of such unused reserves had been originally established for foreclosed real estate. Exact figures are not available for the unused reserves set up for losses on unreforeclosed real estate mortgages and on securities, so that the allocation of the remainder had to be somewhat arbitrary. The figures given, however, appear to be reasonable in view of the known fact that most of such reserves were carried in connection with real estate accounts.

²This entry recognizes the fact that substantial amounts of losses taken on properties in foreclosure were charged against reserves originally set up against the loans before foreclosure proceedings were instituted. As a result, the losses on foreclosed real estate shown in the capital section of the income statement were less than those shown in the reconciliation of the foreclosed real estate account, also published annually in the Commissioner's Reports. For the 15 years as a whole this difference amounted to 2.5 million dollars, which has correspondingly been added to the losses on foreclosed real estate otherwise indicated in the capital section of the income statement.

³The Commissioner's Reports do not segregate losses on real estate loans (apart from those incurred in foreclosure) from those taken on all other loans. It is known, however, that most of the losses on other loans were taken quite early in the depression while most of the losses on real estate loans were not taken until the recovery was well under way. The data given in the table are based on the assumption that both gross losses and profits and recoveries on non-real estate loans over the 15-year period were equal in amount to the charge-offs and recoveries shown for all loans in the years 1931-1935 inclusive; and that gross losses and recoveries on all real estate loans not in foreclosure for the entire 15 years were equal in amount to the corresponding entries for all loans in the years 1936-1945 inclusive.

⁴During the period covered, most banks followed the practice of immediately writing any securities purchased at a premium down to par. The amounts of such premiums charged off are separately reported and have been excluded from gross charge-offs and losses, and correspondingly deducted from reported profits and recoveries.

⁵This item was determined from the published reports as the difference between (a) the sum of the guaranty fund at the beginning of the year and reported transfers into the fund during the year, and (b) the sum of the guaranty fund reported at the end of the year and reported transfers from the fund during the year. Such differences appeared in the six years 1931-1936 and in 1938.

Source: LINTNER, *op. cit.* supra, note 6, at 252-253 (table 30), based upon ANNUAL REPORTS, COMMISSIONER OF BANKS, COMMONWEALTH OF MASSACHUSETTS.

TABLE 4

LEADING CLASSES OF ASSETS OF MUTUAL SAVINGS BANKS, DEC. 31 OF SELECTED YEARS

	1920*	1931	1940	1945	1950			
A. Actual Amounts (000,000 omitted):								
Cash.....	\$ 235.5	\$ 382.6	\$ 954.9	\$ 606.2	\$ 797.1			
U. S. Gov't obligations.....	899.2	709.0	3,193.4	10,649.5	10,888.0			
Other securities.....	1,881.8	3,527.0	2,040.1	1,200.9	2,325.4			
Mortgages.....	2,327.4	5,887.9	4,836.3	4,202.1	8,017.7			
Other real estate.....	40.7	76.1	562.2	36.8	7.6			
Total.....	\$5,780.4	\$11,018.3	\$11,916.4	\$16,962.3	\$22,424.4			
B. Percentage Distribution								
Cash.....	4.1	3.5	8.0	3.6	3.6			
U. S. Gov't obligations.....	15.6	6.4	26.8	62.8	48.6			
Other securities.....	32.6	32.0	17.1	7.1	10.4			
Mortgages.....	40.3	53.4	40.6	24.8	35.8			
Other real estate.....	.7	.7	4.7	.2	.0**			
Total.....	100.0	100.0	100.0	100.0	100.0			
C. Principal Sources and Uses of Funds During These Periods (000,000 omitted):								
	1921-31		1932-40		1941-45		1946-50	
	Sources	Uses	Sources	Uses	Sources	Uses	Sources	Uses
Cash.....		+\$147.1		+\$572.3	-\$348.7			+\$190.9
U. S. Gov't obligations.....	- 190.2			2,484.4		+\$7,456.1		238.5
Other securities.....		1,645.2		-1,486.9		- 839.2		1,124.5
Mortgages.....		3,560.5		-1,051.6		- 634.2		3,815.6
Other real estate.....		35.4		486.1		- 525.4		-31.2
Total Assets..	+5,237.9		+ 898.1		+5,045.9		+5,462.1	

*Estimated. **Less than 1/2 of 1 per cent.