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CHAPTER 4

Commercial Banks

COMMERCIAL banks are distinguished from other financial institutions primarily by their acceptance of demand deposits. Deposits provide them with funds but their responsibility for the liquidity and safety of the deposits limits the use of these funds. The privilege of receiving deposits is accompanied by an elaborate framework of legal and supervisory controls designed to protect depositors and govern the monetary effects of demand deposits. In addition, most states have adopted laws that set ceiling rates on various types of consumer credit extended by commercial banks.

Consumer credit is a relatively new and, in most cases, still a minor outlet for the funds of banks. Commercial banks held $18.8 billion of consumer credit at the end of 1959, but this amounted to only 10 per cent of their total loans and investments. The importance of consumer credit at individual banks varies widely. Some smaller banks specialize in consumer lending and place a large part of their loan portfolios in consumer credit. Many larger banks view consumer credit as a promising new outlet for funds, but in most cases it represents only a small part of their over-all lending.

The study was necessarily limited to data obtained from a small number of banks. Although information was obtained from fourteen banks, only nine of these could provide enough detailed cost information to be included in the major tabulations. The banks covered by the study were all relatively large. Several of them were among the largest hundred banks and all of them had total deposits of over $100 million. Although they had large consumer credit operations, the outstanding amount of consumer credit at the sample banks accounted for only 7 per cent of the total at all commercial banks. The sample is described in greater detail in Appendix A.

Diversification of Lending Activities

Consumer credit accounted for only 6 per cent of the total assets of the sample of commercial banks at the end of 1959 (Table 15). Commercial and industrial loans dominated their loan portfolios, but they held other loans of many types, U. S. government securities, and municipal and state obligations.

Some of the banks tended to specialize in one or two types of consumer lending, but most of them engaged in nearly all of the major types of consumer credit. They purchased indirect automobile paper and

TABLE 15

USES OF FUNDS BY COMMERCIAL BANK SAMPLE, END OF 1959
(per cent)

Item	Mean Distribution	Range of Ratios[a] Maximum	Range of Ratios[a] Minimum
Earning assets, net	74.0	81.8	66.2
Consumer credit	5.7	12.2	1.3
Automobile paper, direct	1.4	7.8	0
Automobile paper, indirect	1.4	6.9	0
Other goods paper	.4	1.2	0
Modernization loans	.9	2.2	0
Personal loans	1.6	2.7	.6
Other	68.3	75.4	60.3
Cash and bank balances	24.5	31.9	16.8
Other assets	1.5	2.0	.8
Total	100.0	—	—

Source: Nine-bank sample.

[a] Components in columns for maximum and minimum ratios are not additive as ratios for individual items were taken from statements of different companies.

other contracts from dealers, made direct loans on automobiles and appliances, made repair and modernization loans, and extended direct personal loans of all types. In addition, their retail departments usually extended instalment credit to businesses to finance machinery, equipment, and other facilities.

Nearly half of their consumer credit was extended for the purchase of automobiles. Their lending on automobiles was split almost evenly between direct and indirect financing. About half of the sample banks held both direct and indirect automobile paper. The others concentrated either in direct or indirect automobile financing.

All of the banks in the sample reported some personal loans. The importance of these loans in their portfolio ranged from 51 per cent of total consumer credit outstanding at one bank to 11 per cent at another. All but one of the banks reported some repair and modernization loans and some indirect lending on appliances and other consumer goods.

Gross Finance Charges

Gross finance charges averaged $10 per $100 on the consumer credit outstanding at commercial banks in 1959. This average covers a wide variety of rates on many different types of loans. The average finance charge by type of loan ranged from about $11.15 per $100 on appliance and other consumer goods paper to $8.79 per $100 on direct automobile loans (Chart 7).[1] Individual banks showed variations in charges from $5.60 to $15.00 per $100 of outstanding credit, with both the lowest and highest rate being reported on modernization loans.

Since the average finance charge includes an estimate of the amount retained by automobile dealers, these rates overstate the banks' gross income. The dealers' share of the charge amounted to an estimated 62 cents per $100 on the average charge for all types of credit and to $2.70 per $100 on indirect automobile financing.

The average finance charge at commercial banks increased 16 per cent over the five-year period 1955–59 (Chart 7), reflecting an increase both in the average rate on all types of credit, except direct automobile loans, and in the importance of personal loans in the loan mix. The average rate on personal loans increased about 15 per cent from 1955 to 1959, and these loans expanded from 17 to 28 per cent of the total consumer credit held by the sample banks. The rates on both other goods paper and modernization loans also rose sharply during this five-year period, the latter from $6.59 to $9.02 per $100 of outstanding loans.

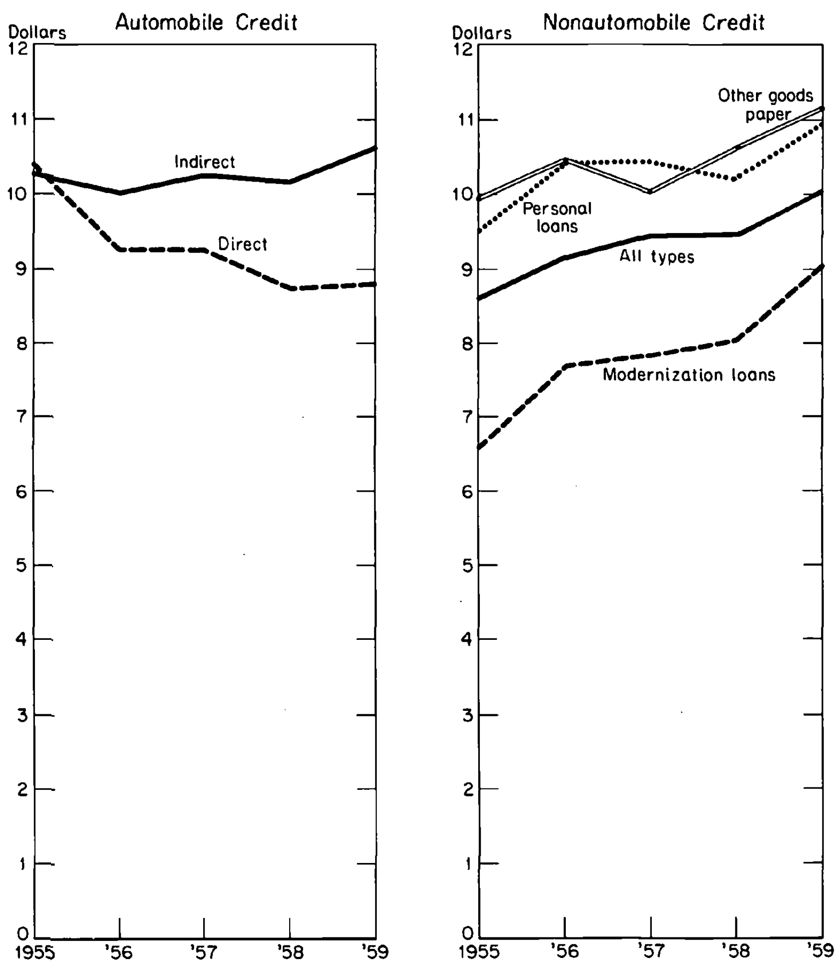
Components of Finance Charges

The gross finance charge includes the amount retained by dealers, the lenders' operating expenses, the cost of funds, and income taxes (Table 16). The determination of these components at banks is complicated by the wide scope of their operations and by the difficulties of separating the costs of any particular type of credit. Much of the information from the sample banks was based on cost accounting systems that imply judgments about the allocation of costs among various functions. Averages based on these records indicated that 42 per cent of the total finance charge at banks went into operating expenses, 6 per cent into payments to dealers, and 52 per cent into the cost of the money and taxes. Operating expenses included the salaries of people handling consumer loans, charges for space used for consumer credit activities, advertising costs, provision for losses, and the many other day-to-day expenses associated with consumer credit operations.

The cost of money included the cost of handling deposits, as well as interest payments and the cost of equity, or the bank's profit. In 1959

[1] Weighted averages based on the dollar size of outstanding credit of each type at each bank show somewhat different levels and trends in charges (see Table 35).

CHART 7
Gross Finance Charges on Consumer Credit at Commercial Banks, by Type of Credit, 1955–59
(per $100 of average outstanding credit)



SOURCE: All types based on nine-bank sample; types of credit based on eight-bank sample. Based on data in Table 35.

TABLE 16

COMPONENTS OF GROSS FINANCE CHARGES ON CONSUMER CREDIT
AT COMMERCIAL BANKS, 1959
(per $100 of average outstanding credit)

Item	Mean Distribution		Range of Ratios[a] (dollars)	
	Dollars	Per Cent	Maximum	Minimum
Gross finance charges[b]	10.04	100.0	--	--
Dealer's share of gross finance charges	.62	6.0		
Lender's gross revenue	9.42	94.0	12.30	6.78
Operating expenses	4.17	41.6	5.84	2.08
Salaries	2.33	23.2	3.25	1.28
Occupancy costs	.23	2.3	.36	.12
Advertising	.34	3.4	.79	.11
Provision for losses	.28	2.8	.42	.08
Actual losses	(.15)	(1.5)	(.28)	(.08)
Other	.99	9.9	1.69	.16
Nonoperating expenses	5.25	52.4	8.49	2.81
Cost of nonequity funds	1.50	15.0	2.35	.71
Income taxes	1.33	13.3	2.07	.70
Cost of equity funds (lender's profit)	2.42	24.1	4.40	.57
Dividends	1.49	14.8	3.19	.34
Retained	.93	9.3	2.14	0

Source: Nine-bank sample.

[a] Components in columns for maximum and minimum ratios are not additive as ratios for individual items were taken from statement of different companies.

[b] Includes all finance charges and fees collected on consumer credit activities. Charges for insurance are not included and the cost of free insurance provided to borrowers was deducted.

the average cost of nonequity funds amounted to $1.50 per $100 of outstanding credit, about 15 per cent of the average finance charge. The average cost of equity funds was 24 per cent of the finance charge or $2.42 per $100, about one-third of which was paid out to stockholders in dividends.

The increase in the average finance charge on consumer credit at commercial banks from 1955 to 1959 was accompanied by a growth in all the major components of cost. Operating expenses increased from $3.76 to $4.17 per $100 of outstanding credit, a rise of 11 per cent. The cost of nonequity funds rose 29 per cent from $1.16 to $1.50 per $100. Although the cost of equity (lender's profit) fluctuated from year to year with no clear trend, the figure for 1959 was higher than that of any of the earlier years covered by the study.

Operating Expenses

Salaries and wages accounted for more than half of the total operating expenses of commercial banks. They averaged $2.33 per $100 of loans in 1959. Individual bank variations in this figure, however, were sizable, ranging between plus and minus 50 per cent of the average. Salary expenses were higher in 1959 than in 1955 but fractionally below 1958 (Chart 8).

Occupancy costs averaged 23 cents per $100 of outstanding credit in 1959. These figures varied relatively little from year to year, ranging from 21 to 23 cents for all years. The amounts allocated for occupancy costs at different banks varied from 12 to 36 cents per $100 of credit.

The advertising figures include all promotional work directly involving the consumer credit department and a share of the bank's over-all public relations and advertising expense. These costs averaged 34 cents per $100 of outstanding credit in 1959, 40 per cent above the 1955 level. Since these costs reflect differences in management policies, the nature of the bank operations, and opinions regarding the desirability and effectiveness of promotional activities, the range among individual institutions was sizable. The highest advertising cost reported for 1959 was more than seven times as large as the lowest.

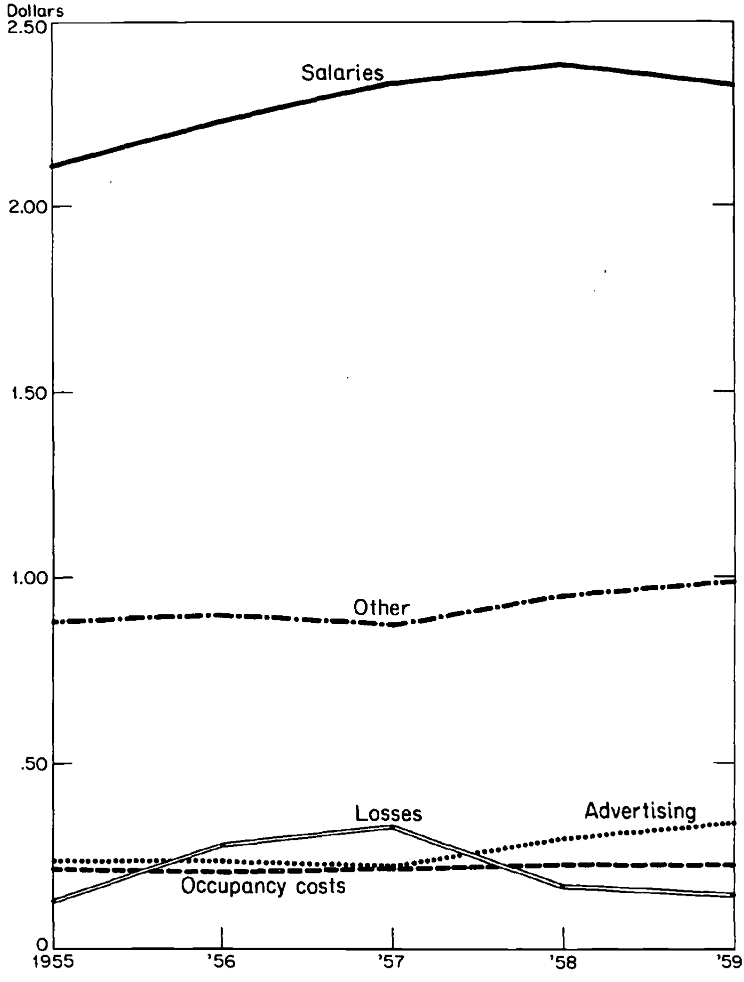
Provision for losses accounted for 7 per cent of total operating expenses at commercial banks. They averaged 28 cents per $100 of credit in 1959. Actual losses amounted to slightly more than half of this figure in that year. Actual loss fluctuated between 13 and 33 cents per $100 of credit during the five years covered by the study. The highest loss ratio was reported in 1957 when losses exceeded provision for losses by a small amount.

Miscellaneous expenditures amount to about $1.00 per $100 of credit, or 25 per cent of the total operating expenses, and cover a wide variety of expenses that were not classified uniformly by the reporting banks and could not be examined separately. They include credit reports, travel expenses, collection costs, legal fees, office supplies, equipment, and many others.

Cost records maintained by five banks by type of credit reveal substantial differences in costs associated with different types of credit

CHART 8

Operating Expenses on Consumer Credit at Commercial Banks, 1955–59 (per $100 of average outstanding credit)



SOURCE: Nine-bank sample. Based on data in Appendix Table D-4.

(Table 17). Operating expenses on appliances and other consumer goods were more than twice as large as those on automobile paper and substantially above those on personal loans. The variations in costs cannot be explained completely with information available. Part of difference, however, arises from number of accounts that must be handled for every $100 of credit. The outstanding amount of average nonautomotive consumer goods contract was only $220, compared with an average personal loan account of $468 and an average indirect automobile contract of $1,181. The variations in costs by type of credit are discussed in greater detail in Chapter 6.

Individual banks showed a range in their total operating costs from a high of $5.84 to a low of $2.08 per $100 of outstanding credit (Table 16). Banks that concentrated on automobile credit and modernization loans were able to report lower average costs for their entire operation. Banks with large personal loan and appliance operations showed a higher over-all cost.

In contrast to the downward trend in operating expenses at finance companies, bank costs increased from 1955 to 1959. Part of this rise probably reflects the growth in importance of high-cost types of loans. Although bank holdings of nonautomotive consumer goods paper declined in importance, the growth in personal loans more than offset this decline. Personal loans accounted for 28 per cent of their consumer credit in 1959, compared with 17 per cent in 1955.

Nonoperating Expenses

The total cost of funds (both equity and nonequity) and income tax payments was larger than total operating cost at commercial banks accounting for 52 per cent of the gross finance charge in 1959. Slightly more than a fourth of nonoperating expenses, or $1.50 per $100 of outstanding credit, covered the cost of handling time and demand deposits,

TABLE 17

OPERATING EXPENSES AT COMMERCIAL BANKS, BY TYPE OF CONSUMER CREDIT, 1957-59
(dollars per $100 of average outstanding credit)

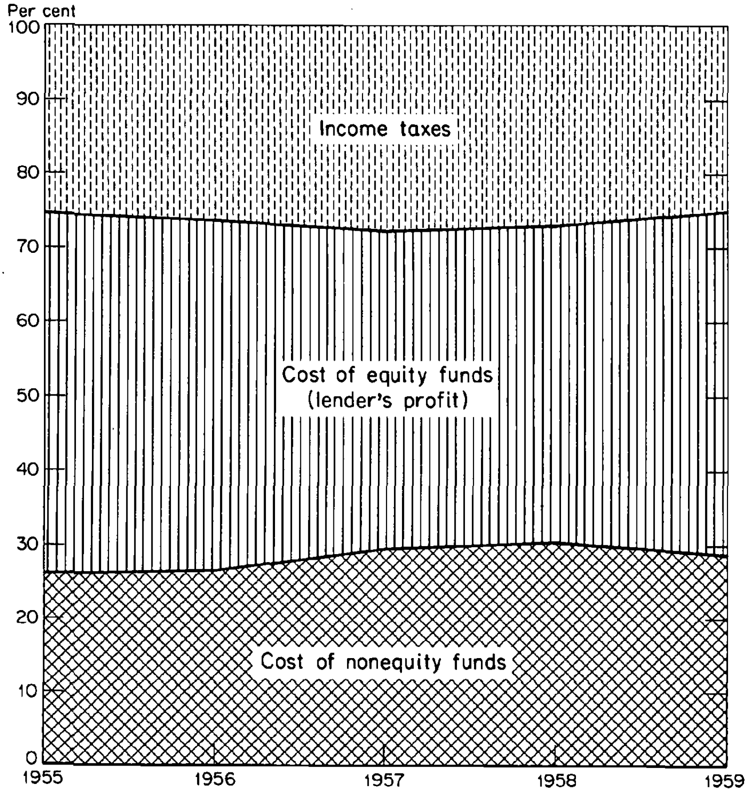
Type of Credit	1957	1958	1959
Total consumer credit	3.96	4.14	4.17
Automobile paper, direct	2.73	3.10	2.84
Automobile paper, indirect	2.92	3.03	3.09
Other consumer goods paper	7.43	8.22	7.40
Modernization loans	2.90	3.25	3.49
Personal loans	4.16	4.84	4.36

Source: Totals are based on nine-bank sample. Data by type of loans are based on five-bank subsample.

the payment of interest on these deposits and other nonequity funds. The remaining three-fourths represented income taxes and the lender's profit on consumer credit operations.

The cost of funds was 18 per cent higher in 1959 than in 1955 as a result of the higher cost of nonequity funds and higher profits. The cost of nonequity funds grew steadily during this period with the rise in rates paid on time deposits. The cost of equity funds fluctuated from year to year with no perceptible trend. For changes in the relative share of each category of nonoperating expenses, see Chart 9.

CHART 9
Distribution of Nonoperating Expenses on Consumer Credit at Commercial Banks, 1955–59



SOURCE: Nine-bank sample. Based on data in Appendix Table D-4.

SOURCES OF FUNDS

Deposits provided nearly 90 per cent of the funds used by commercial banks in 1959. Slightly more than two-thirds of these accounts were in the form of demand deposits with the remainder in savings or time accounts at the end of 1959 (Table 18). The importance of demand deposits varied at individual banks from 46 to 81 per cent. The proportion of demand to time deposits changed relatively little from 1955 through 1959, although the average rate paid on time deposits more than doubled during that period.

Although banks obtain some funds by borrowing from the Federal Reserve System or other banks, the amount of such debt is small. The year-end figures used in the study do not adequately measure the importance of these funds because of the widespread custom of paying down such debts before statement dates.

TABLE 18

SOURCES OF FUNDS FOR COMMERCIAL BANKS, END OF 1959
(per cent)

Item	Mean Distribution	Range of Ratios[a]	
		Maximum	Minimum
Debt	b	b	0
Deposits, total	89.0	92.6	85.8
Demand	61.8	80.8	46.1
Time	27.2	46.5	6.7
Dealer reserves	.2	.5	b
Other liabilities	.9	1.5	.5
Total nonequity funds	90.2	93.4	87.3
Equity funds, total	9.9	12.7	6.6
Reserves	1.9	2.4	.7
Stock and surplus	8.0	10.7	5.5
Total	100.0	--	--

Source: Nine-bank sample.

[a] Components in columns for maximum and minimum ratios are not additive as ratios for individual items were taken from statements of different companies.

[b] Less than 0.1 per cent.

The sample banks provided an average of 10 per cent of their total resources from equity sources in 1959.[2] The importance of equity funds increased slightly from the end of 1954 to the end of 1959, from 8.4 to 9.9 per cent of total resources, in contrast to the decline in importance of equity funds at finance companies. Individual banks showed a range in the use of equity funds from 6.6 to 12.7 per cent of total resources.

COST OF NONEQUITY FUNDS

The cost of nonequity funds averaged $1.50 per $100 of outstanding consumer credit at the sample commercial banks, or about 15 per cent of the gross finance charge. The costs of these funds reflected the banks' cost of acquiring deposits, the proportion of nonequity funds required for their consumer credit operations, and the proportion of resources held in nonearning forms.

Since interest payments are not permitted on demand deposits, the cost of these funds arises from the servicing of accounts. The total cost is reduced by the service charges paid by the depositors but part of the cost is borne by the bank. Estimates of handling deposits can only be obtained from cost accounting records because of the intermingling of the costs of handling deposits with other bank activities. The methods of allocating costs differed somewhat among the sample banks but all of the banks had made detailed studies of the costs of handling deposits. Estimates of the net costs of handling both time and demand deposits averaged 0.7 per cent of deposits in 1959. In addition, the banks paid an average of 2.7 per cent interest on their time deposits. The combined costs of all nonequity funds, including noninterest-bearing liabilities of various types, was 1.2 per cent in 1959 (Table 19, line 2).

During the period covered by the study, banks increased the rate paid on time deposits from 1.2 to 2.7 per cent. This increase was the principal factor in the rise in the total cost of nonequity funds from .9 to 1.2 per cent, although the costs of handling and servicing deposits rose slightly.

The effective cost of funds used in consumer lending by banks was increased by the cost of funds that had to be held in nonearning forms. Many banks compute the money costs of their lending by subtracting nonearning assets from the amount of nonequity funds in obtaining the effective rate on these funds. The large reserve balances required of

[2] Reserves for losses on loans have been included in equity funds for purposes of this study, although they are usually deducted in computing the value of loans and investments in bank statements.

TABLE 19

COST OF NONEQUITY FUNDS AT COMMERCIAL BANKS, 1955-59
(per cent of average outstanding balances)

Ratio of Dollar Cost of Nonequity Funds to:	1955	1956	1957	1958	1959
Debt and deposits	1.0	1.1	1.2	1.2	1.3
Total nonequity	.9	1.0	1.2	1.2	1.2
Nonequity funds minus nonearning assets	1.3	1.4	1.6	1.6	1.7
Consumer credit receivables[a]	1.2	1.3	1.5	1.5	1.5
Interest on time deposits to average time deposits	1.2	1.6	2.1	2.4	2.7

Source: Nine-bank sample.

[a]Based on the dollar share of the total cost of nonequity funds allocated to consumer credit receivables by the ratio of consumer receivables to total earning assets.

banks and other nonearning assets added about 25 per cent to the effective cost of funds used in their lending. Their total nonequity funds cost them an average of 1.2 per cent in 1959, but after allowance for nonearning assets the effective rate was 1.7 per cent.

Nonequity funds supply about 90 per cent of the funds used in consumer credit. The average cost of these funds per $100 of outstanding credit is, therefore, about 10 per cent less than the effective cost of the funds to the bank. This difference is indicated by the spread between the ratio of the cost of funds to net nonequity funds (Table 19, line 3) and the ratio of the cost of funds to consumer assets (Table 19, line 4).

COST OF EQUITY FUNDS

The cost of equity funds (lender's profit) amounted to 24 per cent of the gross finance charges on consumer credit at commercial banks, or $2.42 per $100 of outstanding credit in 1959. The cost of these funds varied from year to year without any clear trend indicated for the five years studied.

This component of the gross finance charge provides the inducement for banks to extend consumer credit and must be large enough in the long run to justify continuation of consumer lending. The banks in the sample obtained an average of from $2.06 to $2.42 per $100 of outstanding credit on the consumer activities during the five years of the study.

The adequacy of these amounts as return on funds invested can best be examined in the context of all factors affecting bank profits.

Lender's Rate of Profit

The bank's share from consumer credit is only one component of its profits. The sample commercial banks reported a profit on equity funds of 7.6 per cent after taxes in 1959, although they obtained only 2.4 per cent from their consumer lending. Thus they were able to earn 5.2 percentage points more on their equity than they received on the dollars per hundred invested in consumer credit. Their over-all profit on equity also depends upon: the return obtained from other loans and investments; the proportion of their total resources they invest in earning assets; and the financial advantages of the use of nonequity funds. The relative importance of these items in bank profits are illustrated in Table 20.

RETURN ON OTHER EARNING ASSETS

Banks invest in a wide range of loans and investments. Some of these investments may produce a higher net operating income than consumer credit, others a smaller income. The sample banks reported a net operating income on all earning assets of 3.4 per cent in 1959 (Table 20, line 2) as opposed to 5.3 per cent on consumer credit.

The relatively low return on some of their nonconsumer credit activities is related to the deposit function of banks. They are required to seek investment outlets that are liquid and of good quality to protect their depositors and provide the liquidity needed to service demand deposits. The low yield on such investments reduces their earning capacity and is a cost of accepting deposits.

In most cases the loan and investment decisions of commercial banks are not influenced directly by their consumer credit policies. However, some banks find it desirable to finance the inventory of the dealers from which they obtain retail paper or in other ways provide services related to consumer lending. In some states banks are permitted to handle insurance operations or to accept fees as agents for writing insurance. In such cases, the insurance that arises from consumer credit operations may add to or supplement the bank's income. Most of their earnings on other earning assets, however, have no relation to their consumer credit activities.

TABLE 20

FACTORS IN COMMERCIAL BANK PROFITS, 1955-59
(per cent of average outstanding balances)

Ratio	1955	1956	1957	1958	1959
1. Net operating income from consumer credit to consumer receivables[a]	4.5	4.9	5.0	4.9	5.3
2. Net operating income to earning assets	2.3	2.9	3.3	3.4	3.4
3. Net operating income to total assets	1.9	2.1	2.4	2.5	2.5
4. Profits before taxes to equity funds	12.5	13.6	14.8	15.5	14.5
5. Net return from nonequity to equity funds (line 4 minus line 3)	10.6	11.5	12.4	13.0	12.0
6. Provision for income taxes to profit before taxes	46.8	46.6	49.5	48.9	46.0
7. Net profits to equity funds	6.5	7.1	7.4	7.9	7.6
8. Percentage of profit obtained from leverage on nonequity funds (line 5 ÷ line 4)	84.8	84.6	83.8	83.9	82.7
ALTERNATIVE DERIVATION OF LINE 5					
a. Net operating income to total assets (line 3)	1.9	2.1	2.4	2.5	2.5
less					
b. Cost of nonequity funds to nonequity funds	.9	1.0	1.2	1.2	1.2
equals					
c. Net return from nonequity funds to nonequity funds	1.0	1.1	1.2	1.3	1.3
times					
d. Leverage coefficient (ratio of nonequity to equity funds)	11.0	10.5	10.1	9.9	9.6
equals					
e. Net return from nonequity to equity funds (line 5)[b]	11.0	11.6	12.1	12.9	12.5

[a] Equivalent to nonoperating expenses per $100 of average outstanding consumer credit, see Table 16.

[b] Differences between lines 5 and e result from rounding errors introduced by alternative methods of calculation.

COST OF NONEARNING ASSETS

Banks are required to hold a sizable part of their total resources in the form of reserves because of their unique responsibility to their depositors and their key role in the determination of the money supply. As a result, a large share of their total resources are immobilized for earning purposes. In 1959, 24.5 per cent of their resources were held in the form of cash, bank balances, or reserves with the Federal Reserve System. Another 1.5 per cent was held in other nonearning assets. These large idle balances reduce the earning potential and profitability of banking operations. Their net operating income of 3.4 per cent on earning assets produced a return of only 2.5 per cent on total resources in 1959 (Table 20, line 3).

FINANCIAL ADVANTAGE OF THE USE OF NONEQUITY FUNDS

The return of 2.5 per cent that banks earned on total resources is obviously too small to attract or hold equity funds. A satisfactory return can only be achieved by the sizable financial advantage that banks obtain on the use of deposit funds. The importance of this advantage depends on the cost of these funds and the proportion of total resources obtained from nonequity sources.

Banks obtained their total nonequity funds at an average rate of 1.2 per cent in 1959 and earned an average of 2.5 per cent on total resources. Thus they were able to net about 1.3 per cent on all the nonequity funds used. Their nonequity funds were 9.6 times larger than their net worth so that the return on equity from the use of nonequity funds was 9.6 times 1.3 per cent, or about 12.5 per cent (see lower panel of Table 20). This income, plus the return that could be earned directly on the owner's share of total resources resulted in a net profit before taxes of 14.5 per cent on equity funds. Provisions for income taxes absorbed 46 per cent of the profits before taxes leaving a return of about 7.6 per cent on equity in 1959.

TREND IN LENDER'S PROFITS

The ratio of net profits to equity funds at the sample banks increased steadily during the five years covered by the study. The improvement in profits reflected primarily an increase in net operating income as the sample banks were able to increase their net operating income on total assets by nearly a third. This income was more than enough to offset the increase in cost of nonequity funds and the decline in the ratio of nonequity funds to total resources.

Income from consumer credit added to the increase in earnings on total assets. Their net operating income from consumer credit rose from 4.5 to 5.3 per cent. Their net income from all earning assets rose by nearly a half, from 2.3 to 3.4 per cent. The increase in interest rates during the 1950's contributed materially to high earning rates at banks and was more than enough to offset the higher cost of their funds.

The sample banks used about half of their profits for cash dividends to shareholders and retained the rest. In 1959 they paid dividends amounting to two-thirds of their profits. These payments gave the stockholders an average yield of about 5 per cent on the book value of their stock, compared to 1955 when the sample banks paid out only 55 per cent of their profits for an average yield of only 3.6 per cent on the book value of their stock.

Comparison of Banks with Highest and Lowest Average Finance Charges

Two banks in the sample consistently showed high finance charges on consumer credit throughout the period covered; two others showed consistently low charges. The finance charges at the high-charge banks averaged $3.90 per $100 higher than those at the low-charge banks for the five-year period.

No clear-cut difference in the type of loans made by the banks involved could be found. They all performed a wide range of consumer lending operations. All but one of them had both direct and indirect automobile lending operations and some indirect paper on other consumer durable goods. All of them had about the same proportion of their receivables in personal loans and all but one had 10 to 15 per cent of their receivables in modernization loans.

The high-charge banks showed somewhat higher expenses in every item of operating expenses on consumer activities except advertising. They also reported 25 per cent higher costs on nonequity funds. The difference in cost of nonequity funds reflected primarily a greater dependence on time deposits by the high-charge banks. They obtained 30 per cent of their total resources from time deposits, compared with 10 per cent at the low-charge group.

Only 23 per cent of the differential in finance charges could be traced to operating expenses and the cost of nonequity funds. The remaining 77 per cent was in the return on equity funds and provisions for income taxes. The high-charge banks earned an average of 8.4 per cent on their net worth, compared with only 5.5 per cent at the low-charge banks.

The profits of high-charge banks could not be attributed solely to their favorable earnings on consumer credit, however. They also showed a higher return on their other earning assets, more complete utilization of the resources, and greater leverage than the low-charge banks (Table 21).

TABLE 21

COMPARISON OF COMMERCIAL BANKS WITH HIGHEST AND LOWEST AVERAGE FINANCE CHARGES ON CONSUMER CREDIT, 1955-59[a]

Item	Two High-Charge Banks (1)	Two Low-Charge Banks (2)	Difference (col. 1 minus col. 2) (3)
DOLLARS PER $100 OF AVERAGE OUTSTANDING CONSUMER CREDIT			
Finance charges[b]	10.90	7.00	3.90
Operating expenses	3.80	3.40	.40
Salaries	2.20	2.00	.20
Occupancy costs	.30	.10	.20
Advertising	.20	.40	-.20
Provision for losses	.30	.20	.10
Actual losses	(.3)	(.2)	(.1)
Other	.80	.70	.10
Nonoperating expenses (lender's net operating income)	7.10	3.60	3.50
Cost of nonequity funds	1.90	1.40	.50
Income tax	1.70	.70	1.00
Cost of equity funds (lender's profit)	3.50	1.50	1.00
Dividends	2.50	1.10	1.40
Retained	1.00	.40	.60
SELECTED RATIOS (PER CENT)			
Total net operating income to earning assets	3.5	2.7	.8
Total net operating income to total assets	2.8	2.0	.8
Cost of nonequity funds to nonequity funds	1.6	1.2	.4
Nonequity to equity funds	12.6	8.5	4.1
Time deposit to total assets	30.0	10.0	20.0
Net profits to equity funds	8.4	5.5	2.9

[a] All data are averages of individual bank ratios for the five years 1955-59.

[b] Excludes dealer's share of gross finance charges.