Volume Title: Comparative Operating Experience of Consumer Instalment Financing Agencies and Commercial Banks, 1929-41

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Volume Publisher: NBER

Volume ISBN: 0-870-14126-0

Volume URL: http://www.nber.org/books/daue44-1

Publication Date: 1944

Chapter Title: Net Profit and Cash Dividends: The Share of the Owners

Chapter Author: Ernst A. Dauer

Chapter URL: http://www.nber.org/chapters/c1781

Chapter pages in book: (p. 154 - 178)

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Net Profit and Cash Dividends: The Share of the Owners

THROUGHOUT the period 1929-41, net profit—the amount available to stockholders after all operating costs and interest payments have been met—was a high percentage of net worth for the consumer instalment financing agencies as compared with commercial banks or with other corporations generally. Likewise, their dividend payments to stockholders were higher percentages of net worth than those of banks or other corporations. However, as a result of the higher level of net profit among the specialized agencies, the amounts paid out in dividends generally represented a smaller proportion of net profit than they did for commercial banks or other corporations.

NET PROFIT

Rate of Net Profit

The average rate of net profit on the book value of ownership equity invested in the business declined sharply during the depression for the consumer instalment financing agencies, but in general it remained positive; after reaching pre-depression levels during the recovery in 1936 and 1937, it declined in 1938, rallied in the subsequent years and remained at a high level.[1] On the other hand, the average rate of net profit on net worth of commercial banks, although better than that of corporations in general, was lower than that of the consumer agencies in the good years, and in the depression was a negative figure. Figures are shown in Table 27.

Sales finance companies for the period as a whole showed almost

[1] A considerable variation was shown in the rates of net profit reported by individual companies in the income tax sample, but the distribution of individual companies, presented in Appendix Table B-14, confirms the inferences based on average rates of net profit.

TABLE 27

NET PROFIT OF SELECTED SAMPLES OF CONSUMER INSTALMENT FINANCING AGENCIES AND COMMERCIAL BANKS IN PERCENT OF NET WORTH, 1929–41[a]

Sample	*1929*	*1930*	*1931*	*1932*	*1933*	*1934*	*1935*	*1936*	*1937*	*1938*	*1939*	*1940*	*1941*
Sales finance companies													
2 to 3 national[b]	15.9%	11.4%	8.9%	5.8%	9.6%	15.3%	17.9%	20.2%	20.4%	14.1%	12.1%	12.3%	14.1%
2 to 4 regional[b]	16.4	13.0	11.5	3.6	6.4	11.8	18.5	19.2	15.6	9.6	10.1	10.7	8.9
9 to 32 local[b]	13.4	8.0	7.4	3.1	6.9	11.0	15.0	16.0	16.1	7.5	9.0	10.8	11.6
202 local[c]	11.9	..	..	..	4.7	..	..	12.1	..	..	..	..	..
Personal finance companies													
2 national[d]	..	16.3	14.1	12.2	12.0	11.3	13.5	14.9	16.6	14.4	13.8	13.5	11.8
2 to 5 regional[d]	20.6	16.4	12.8	−6.3	10.8	12.7	14.0	16.3	18.2	14.0	15.1	15.4	14.5
5 to 7 local[d]	..	..	..	..	..	9.2	10.4	13.7	13.8	10.2	11.4	14.5	12.8
153 local[e]	11.8	..	..	..	5.4	..	..	8.3	..	..	..	..	..
79 non-invest. type indust. bkg. cos.[e]	7.3	..	..	..	1.3	..	..	5.9	..	..	..	..	..
Invest. type indust. banks													
56 noninsured[e]	9.7	..	..	..	2.0	..	..	4.9	..	..	..	..	..
6 largest insured[e]	..	..	..	..	..	[h]	6.3	12.1	12.5	19.2	16.7	13.4	13.4
All other insured[e]	..	..	..	..	..	4.1	7.3	8.2	10.0	8.0	9.8	7.8	8.7
37 insured[e]	8.9	..	..	..	1.8	..	..	10.8	..	..	..	..	..
Credit unions													
All reporting federal credit unions[f]	..	..	..	..	..	..	2.6	4.3	5.1	5.0	4.9	4.9	4.3
Commercial banks													
All national banks[g]	7.8	4.0	−1.5	−5.0	−9.6	−5.2	5.1	10.0	7.1	6.1	7.4	7.0	7.5
All insured banks[e]	..	..	..	..	..	−5.5	3.4	8.4	6.0	4.7	6.0	6.1	6.7

(footnotes on following page)

as high a rate of net profit on net worth as personal finance companies, despite a relatively low rate of operating profit on total funds. Their net profit rate showed sharper fluctuations, however, with changes in the business cycle, falling during the depression and rising in the years immediately following 1933; and its year-to-year pattern diverged materially from the rate of operating profit on total assets. These relationships emphasize the importance, as factors in the rate of net profit, of the sales finance companies' high proportion of borrowed funds, and of the interest rate paid on them.

In 1929 the rate of interest paid by sales finance companies on borrowed funds was only slightly below the rate of operating profit; nevertheless, the high proportion of borrowed funds provided sufficient leverage to lift the rate of net profit on equity capital. When the rate of operating profit fell, from 1930 to 1933, the rate of interest paid on borrowed funds fell also, but less rapidly, so that the rate of net profit dropped more sharply than the rate of operating profit. From 1933 to 1936 the rate of net profit rose spectacularly, much more rapidly than the rate of operating profit, because of the continued sharp fall in the interest rate on borrowed funds, and the rise in the proportion of such funds. From 1938 to 1941, despite a decline in the rate of operating profit, the rate of net profit was fairly stable, thanks to the continued decline in the rate of interest on borrowings and in the proportion of equity capital.

FOOTNOTES TO TABLE 27

[a] The number of companies for each year may be found in Appendix Table B-1.

[b] Based on data from the National Credit Office, Inc. Some of these companies are included in the 202 local companies of the income tax sample. Here the denominator is average net worth at the beginning and end of year.

[c] Based on tabulations prepared by the Income Tax Study. The figures represent net profit in percent of year-end net worth.

[d] Based on data from the National Credit Office, Inc. Some of these companies are included in the 153 local companies of the income tax sample. Here the denominator is average net worth at the beginning and end of year.

[e] Based on data from Federal Deposit Insurance Corporation. Net worth is the average of figures for beginning, middle and end of year, except for industrial banks in 1934 and 1935, when year-end figures are used. Cash depositories and banks designated in this study as insured industrial banks are included with all insured commercial banks.

[f] Based on data from U. S. Farm Credit Administration, Division of Finance and Accounts. The figures represent net profits in percent of year-end net worth.

[g] Based on data in Annual Reports of the Comptroller of the Currency. Net worth is the average of figures for call dates during the year.

[h] Less than 0.05 percent.

In personal finance companies, whose proportion of borrowed funds was lower than that of sales finance companies, fluctuations in the rate of net profit on net worth followed those in the rate of operating profit on total assets more closely. In addition, as long as the rate of personal finance companies' operating profit was high, the decline in the interest rate paid on borrowed funds, and the increase in the proportion of such funds, had a less noticeable effect on the rate of net profit. By 1937, however, the rate of operating profit had decreased sufficiently to allow the influence of these factors to be reflected in the rate of net profit. After 1937, despite the continued decline in the rate of operating profit, the rate of net profit was relatively stable.

For industrial banking companies included in the income tax sample the average rate of net profit in 1929 was somewhat below that of sales finance and personal finance companies, and by 1933 it had dropped still further. This fall was sharper than that in the rate of operating profit, since the cost of borrowed capital had remained relatively constant. During the subsequent upturn, 1933-36, the rate of net profit of non-investment and of noninsured investment type industrial banking companies failed to reach 1929 levels, since the rate of operating profit did not show sufficient recovery nor the rate of interest on borrowed capital sufficient decline.

This was in sharp contrast to the experience of insured industrial banks, which exceeded their 1929 level in 1936 and subsequent years, as a result of the expansion in proportion of deposits to equity capital and the decrease in rate of interest paid on deposits.[2]

Since the proportion of borrowed capital in federal credit unions has always been insignificant, the rate of net profit—about 5 percent of year-end net worth—was only fractionally higher during the period under review than the rate of operating profit on year-end total assets. As in the case of all data covering federal

[2] Figures for a group of reporting Morris Plan banking companies—almost all of which are investment type companies, and a number of which are insured banks, included in the income tax sample—show a higher rate of net profit throughout the period than the other samples of industrial banks. In this series, the fluctuations from year to year, however, are in general agreement with those indicated by the other samples. See National Bureau of Economic Research (Financial Research Program), *Industrial Banking Companies and Their Credit Practices,* by Raymond J. Saulnier (New York 1940) Table 47, p. 164.

credit unions, the average rate of net profit of those units that have operated throughout the respective years was somewhat higher than indicated by reported figures, which are affected by the rapid growth in the number of federal credit unions during this period.

Over the period 1890-1929 national banks experienced an average rate of net profit of 7.8 percent of net worth,[3] the same as that shown in 1929. The fact that despite a substantially lower rate of operating profit, this net profit rate was almost as high as that of investment type industrial banking companies, and about two-thirds that of local sales finance and personal finance companies, may be attributed to the high proportion of demand deposits, on which no interest or a very low rate of interest was paid.[4]

The national banks' rate of net profit dropped sharply to a negative figure of almost 10 percent in 1933, as a result of continued payment of interest, which absorbed over one-quarter of total income at a time when the rate of operating profit had declined beyond the vanishing point. This drastic drop in rate of operating profit may be laid to the huge increase in the rate of gross and net charge-offs on loans and securities.[5]

With the subsequent recovery the rate of operating profit for national banks fluctuated around 1 percent of total assets, a level less than one-half that of the late twenties. At the same time, however, there was a further decline in the proportion of total funds represented by net worth,[6] a prohibition of interest payments on demand deposits, and a sharp decrease in the rate of interest paid on time and savings deposits.[7] In consequence, during the six-year period ending in 1941, the rate of net profit of all national banks averaged about 7.5 percent, only slightly below the rate for 1929 and the average for the years 1890-1929.[8]

[3] See Chart XV, below.

[4] The rate of operating profit was less than 3 percent of total assets, and the rate of interest paid on time and savings deposits was in excess of the rate of operating profit.

[5] See Chart IX, Chapter 5.

[6] See Chart III, Chapter 2.

[7] See Chapter 7, especially footnote 9.

[8] The only practical method of determining the *rate* of profitability (on net worth) is by the use of book figures of net worth. It should be noted that as a result of the disappearance of a substantial portion of the net worth of the entire banking system, through bank failures in the early thirties, the total *dollar amount* of net profit (and of dividends) of the banking system was lower, in relation to the previous decade, than the data on *rates* indicate.

Comparison with Other Industries

It is difficult, if not impossible, to obtain an adequate measure of the profitability of consumer instalment financing agencies and commercial banks in relation to that of other types of corporations. Figures are available, however, from income tax returns for the years 1930-39, covering the rate of net profit (book) to net worth for all active corporations and for banks and trust companies.[9] In Chart XIII these are juxtaposed to figures on the rate of net profit to net worth of the National Credit Office samples of sales finance and personal finance companies, and to figures covering insured industrial banks. Although the data are not entirely comparable, one set being prepared for published statements, supervisory authorities, or credit purposes, and the other for income tax purposes, the indicated levels of net profit rates reveal that throughout the period consumer agencies earned materially higher rates of net profit on owners' equity than banks or corporations in general.[10]

Figures prepared from income tax returns of banks and trust companies,[11] and of all corporations, are more readily comparable to each other than to the other series shown in the chart. The banks' rate of net profit on net worth appears to have been more favorable than that of all corporations except in 1933 and 1934, and for the period as a whole banks showed a net profit of 2.5 percent of net worth, as compared with 2.1 percent for all corporations.

Banks were able to continue profitable operations through 1931, one year longer than all corporations, and did not emerge from their unprofitable situation until after 1934, again a year later than all corporations. This supports the view that the effect of

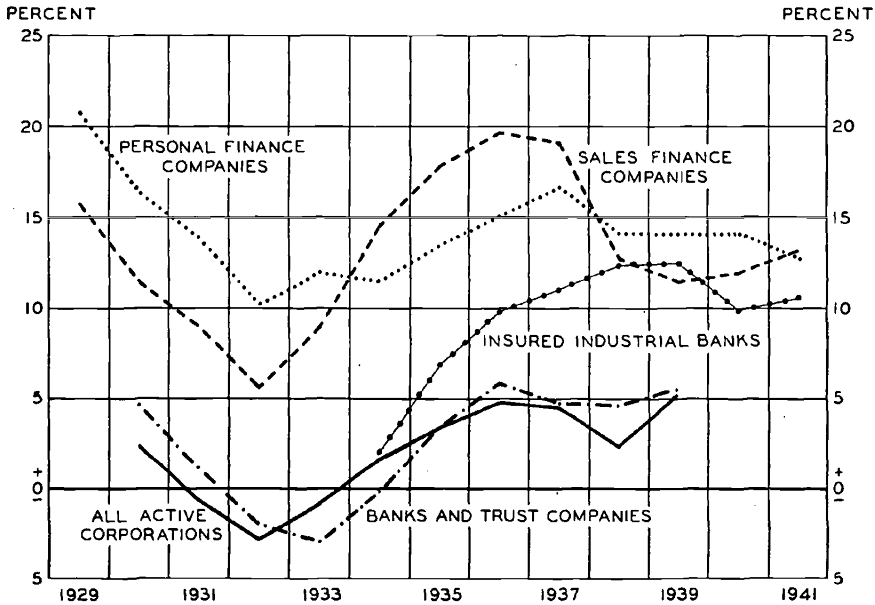
[9] In presenting figures from income tax returns the Internal Revenue Bureau separates returns of companies and banks into those with "net income" and those with "no net income." These have been combined here.

[10] In order to simplify the presentation the rates of national banks have not been included in the chart. They showed more extreme variation than the rates of all banks and trust companies filing income tax returns, being lower in 1930-34 and higher in subsequent years. The figures are available for comparison in Table 27.

[11] The classifications used were, for 1930-37, "national banks" and "state banks and trust companies," and, for 1938-39, "banks and trust companies." Although the categories used by the Internal Revenue Bureau include some enterprises not encompassed in our definition of commercial banks (and apparently exclude industrial banks), the differences are not sufficiently significant to affect our conclusions.

CHART XIII

RATES OF NET PROFIT OF CONSUMER INSTALMENT FINANCING AGENCIES, COMMERCIAL BANKS AND ALL CORPORATIONS, 1929–41[a]



[a] Represents net profit in percent of net worth. For sales finance and personal finance companies, based on data from the National Credit Office, Inc., combining national, regional and local companies; net worth is the average of figures for beginning and end of year. For industrial banks, based on data from Federal Deposit Insurance Corporation covering insured industrial banks; net worth is the average of figures for beginning, middle and end of year, except in 1934 and 1935, when year-end figures are used; banks that submitted reports covering less than the full year's operations or whose operations were materially affected by mergers during the year are not included. The number of the above companies for each year may be found in Appendix Table B-1.

For all active corporations filing income tax returns based on data in *Statistics of Income*. For active banks and trust companies filing income tax returns based on data in the *Source Book* of the Bureau of Internal Revenue. Returns were filed on a fiscal or calendar year basis. The comparability of these sets of data for the various years is discussed in *Statistics of Income, 1938,* Part 2, pp. 6-8, 241-83.

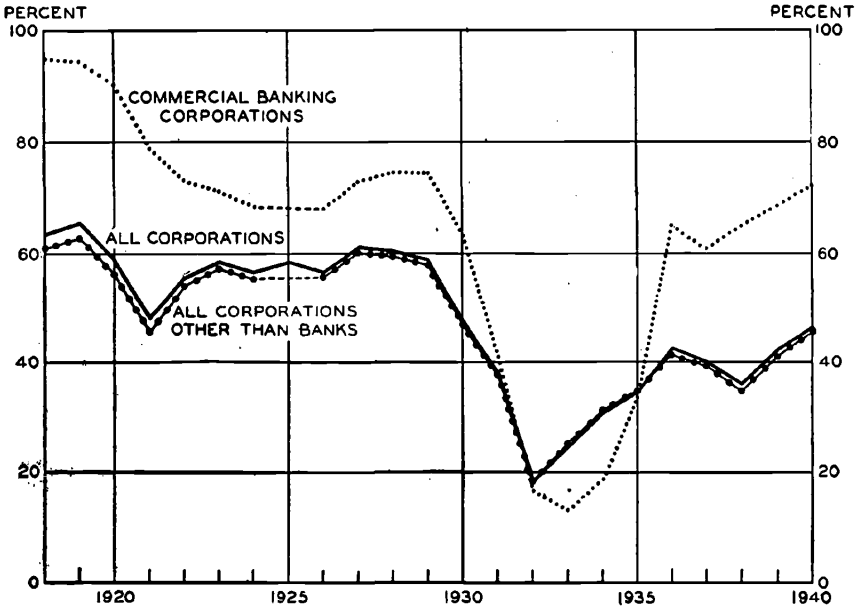
the business cycle on banks tends to come later than that on the national economy as a whole.

Further data from the income tax returns are presented in Chart XIV, which shows the proportion of corporations reporting taxable net income for each of the years 1918-40.[12] This chart reveals

[12] Taxable net income differs from net profit, as tabulated from income tax returns, by the amount of tax-exempt income and by the amount of income, excess profits taxes, and surtaxes.

CHART XIV

PERCENTAGE OF CORPORATIONS FILING RETURNS THAT REPORTED TAXABLE NET INCOME, 1918–40[a]



[a] Based on data in *Statistics of Income,* and in the *Source Book* of the Bureau of Internal Revenue covering income tax returns of all active corporations filed on a fiscal or calendar year basis. Prior to 1927, inactive corporations were included, their returns being compiled among those showing no taxable net income. Except for "all corporations" figures are not available for 1925. In 1938 there was a slight change in classification of "commercial banking corporations."

that during the first war a greater proportion of national and state banks and trust companies enjoyed profitable operations than all other corporations taken as a whole. Moreover, the proportion of banks whose operations were profitable is probably understated, primarily because in banks interest from tax-exempt securities is an important component of total income.[13]

[13] The importance to banks of income from tax-exempt securities is indicated by the following percentages of income on government obligations in 1938 (both wholly and partially tax-exempt) to total income ("total compiled receipts"):

	All Corps.	*Banks*	*All Corps. Other Than Banks*
All corporations	0.6%	23.2%	0.2%
Corporations with taxable net income	0.5	24.1	0.1
Corporations with no taxable net income	0.8	20.6	0.6

While the advantage of banks over other corporations diminished materially after 1920, under the pressure of agricultural difficulties on many small country banks, it lasted nevertheless until 1930. In 1931 and 1932 the proportion of enterprises showing net income rapidly became smaller, reaching a low point for all corporations in 1932 and for banks in 1933, when only one bank in eight reported taxable net income. From 1932 through 1935 the proportion of enterprises showing taxable net income continued lower among banks than among other corporations, but this relationship was reversed in 1936, and from that year through 1940 the differential in favor of banks was greater than it had been during the twenties.

From data on the proportion of companies reporting taxable net income for the period 1918-40, and on rates of net profit on net worth for the shorter period 1930-39, it appears that the profitability of capital invested in banking is higher than that of corporate enterprises in general. However, there is no doubt that in some specific industrial groups a higher proportion of corporations enjoyed profitable operations, or that certain industrial groups as a whole had higher average rates of net profit on net worth.[14]

Profitability and Size of Institution

There is little indication of a direct relationship between size of enterprise and rate of net profit among the specialized companies included in the income tax sample.

Since the relation of size of company to rate of operating profit on total assets was slight,[15] any relationship existing between size of company and rate of net profit must be attributed to variation in the rate of interest paid on borrowings, or to variation in the relationship between borrowed and owners' capital.

We have seen that there was little connection between size of company and rate of interest paid on borrowed capital among the companies included in the income tax sample,[16] but that for both

[14] Six-year averages of rates of return for industrial groups, over the period 1931-36, presented in William Leonard Crum, *Corporate Size and Earning Power* (Cambridge, Mass., 1939) p. 25, lead to the conclusion that the public utility, food, liquor, tobacco, leather, rubber, paper, printing, chemical, and metal groups had higher rates of net profit than commercial banks during this period.

[15] See the concluding section of Chapter 6.

[16] See Chapter 7.

sales finance and personal finance companies included in the smaller samples, the degree of variation among companies engaged in nation-wide, regional and local operations differed considerably from year to year during the period 1929-41.[17]

It appears, therefore, that any correspondence between size of enterprise and rate of net profit on net worth shown by these companies would be due almost entirely to variations in the proportion of total funds represented by owners' equity. But although the relationship between size of institution and proportion of net worth was marked,[18] the influence of the latter upon rate of net profit (to net worth) was largely dissipated by the counter-influence of rate of operating profit and rate of interest on borrowings, both of which bore an irregular relationship to size of institution. The influence of size on the rate of net profit was thus negligible.

National bank data collected by the Federal Reserve Committee on Branch, Group, and Chain Banking for the years 1926-30, inclusive, show a rate of net profit on net worth markedly higher for the larger than for the smaller banks, when banks are grouped according to size, as measured by loans and investments.[19] These data have been widely interpreted and quoted as proving a causal relationship between size of institution and rate of profit.[20] There is every indication, however, as pointed out in a later study,[21] that

[17] See Chapter 7, especially Table 24.

[18] See Chapter 2, especially Chart II.

[19] *Banking Profits, 1890-1930* (material prepared for the information of the Federal Reserve System by the Federal Reserve Committee on Branch, Group, and Chain Banking): *Documents, Vol. 22, 73rd Congress, 1933-34.*

[20] See, for example, Twentieth Century Fund, *How Profitable is Big Business?* (New York 1937) pp. 160-61, which concludes as follows: "A study of banking profits shows clearly that the larger institutions had more favorable operating results than the smaller ones. . . . " "The comparison between the profitableness of large and small banks leaves little doubt that the advantage is with the former. Nevertheless, the largest banks are by no means always the most profitable. Neither should it be assumed that operation on a small scale cannot be made fairly profitable. Many of the smallest institutions must be looked upon, however, as uneconomic units and as constituting weak links in the banking system." See also Chapter 9 and pp. 150-53.

[21] See Donald S. Thompson, "Trends of Bank Earnings and Expenses," *Journal of the American Statistical Association,* vol. 33 (June 1938) pp. 327-33. This study shows that the figures on profits of small banks were dominated by figures of banks in agricultural and rural regions, particularly in the midwest and south, and that the figures on large banks were dominated by the results of banks in industrial and financial centers, particularly in the north and east. During the period covered by the study, banks in agricultural regions were still subject to the effects of postwar adjustments in agriculture; many of their loans were in default and the banks were taking substantial charge-offs on assets. Industry and finance, on the other hand, were active and prosperous. "The loss experience of the larger banks was charac-

the figures not only reflect the economic circumstances in which banks operated during that period, but are greatly influenced by variations in the proportion of total funds represented by net worth.

Among insured commercial banks in the years 1939-41 the relation of total net worth to total assets was much more important in determining the rate of net profit on net worth than was size of bank. This is evident from Table 28, which presents average net profit in percent of total net worth of insured commercial banks, grouped by amount of deposits and percentage of net worth, for the calendar year 1939.

When the percentage of net worth is held constant (reading down in the table) there is a tendency for smaller banks to show higher rates of net profit than larger banks, exactly the reverse of the conclusions attributed to the Federal Reserve Committee study. Differences between rates of net profit in any one group of banks with the same net worth proportion are not nearly so marked, however, as are differences between rates of net profit in any one size group (reading across the table) with varying net worth proportions.

Influence of Character of Loans on the Rate of Net Profit

We have seen in Chapter 6 that in consumer instalment financing companies included in the income tax sample there was a close relationship between rate of operating profit on total assets and rate of total income on loans—the rough measure of the character of the paper held; and that this was true also of commercial banks, where the relationship was computed between rate of net earnings on total assets and rate of income on loans.

This influence of character of paper on rate of operating profit (or net earnings) was sufficiently strong to carry over to the rate of net profit on net worth. True, the relationship between character of paper and rate of net profit was subject to a number of irregularities, due to the intervening influence of lower rates of interest on borrowed capital in low-rate companies, and of their higher proportion of borrowed funds. Nevertheless, in general, the greater

teristic of a period of prosperity; that of the small banks appeared to be characteristic of a period of depression. It seems, certainly in retrospect, that the situation was not at all a characteristic one and was of such a nature as to result in an unfavorable showing of small banks as compared with large banks."

TABLE 28

RATES OF NET PROFIT OF INSURED COMMERCIAL BANKS, 1939, BY NET WORTH PROPORTIONS AND AMOUNT OF DEPOSITS[a]

Deposits	All Banks	Net Worth in Percent of Total Assets: Under 5%	5–7½%	7½–10%	10–12½%	12½–15%	15–20%	20–25%	25–30%	30% or Over
$100,000 or less	3.4%	..	..	..	(–.9)%	7.0%	4.3%	3.8%	3.7%	1.6%
100,000–250,000	6.0	..	(8.5)%	8.4%	7.7	6.8	6.1	5.2	3.7	2.7
250,000–500,000	7.6	(15.6)%	6.0	10.2	8.9	7.6	6.1	5.2	5.3	2.5
500,000–1,000,000	7.6	(16.9)	10.8	10.1	8.7	7.2	5.7	3.8	.6	–.8
1,000,000–2,000,000	7.2	(26.9)	10.8	9.5	7.7	6.1	5.2	3.6	3.2	.3
2,000,000–5,000,000	6.4	(13.9)	9.4	7.9	7.1	5.2	4.5	2.8	3.2	(4.8)
5,000,000–10,000,000	6.4	(7.2)	8.5	8.2	6.1	6.0	3.7	2.1	(1.6)	(4.6)
10,000,000–50,000,000	7.4	(6.4)	10.3	8.5	6.6	6.7	3.5	(4.2)	(–12.4)	(4.0)
Over 50,000,000	6.4	..	6.8	7.2	5.6	4.8	(1.8)	(5.3)	(6.3)	..
ALL BANKS	6.9%	11.9%	9.5%	9.3%	8.0%	6.8%	5.6%	4.6%	3.4%	1.9%

[a] Based on data from Federal Deposit Insurance Corporation. Rates of net profit represent net profit in percent of net worth; figures are averages of rates of individual banks. In regard to banks that were members of the Federal Reserve System net worth, total assets and deposits are averages of figures for call dates during the year, and in regard to non-member banks they are averages of figures for the beginning, middle and end of the year. Cash depositories, banks designated in this study as insured industrial banks, and banks that submitted reports covering less than the full year's operations or whose operations were materially affected by mergers during the year are not included. Net-worth rate groups are inclusive of the lower limit and exclusive of the upper; deposits groups are exclusive of the lower limit and inclusive of the upper. Parentheses indicate groups containing 10 banks or fewer.

degree of trading on equity in low-rate companies did not offset the higher rate of operating profit in high-rate companies, which showed higher rates of net profit on net worth.

PAYMENT OF CASH DIVIDENDS

Rate of Dividends

The rate of cash dividends paid by consumer agencies during the period 1929-41 was subject to much less severe fluctuation than the rate of net profit. It did decline, however, from 1929 to 1933, spurted upward in the subsequent recovery and was reasonably stable from 1938 to 1941, at a level generally above that recorded at the beginning of the period. For the most part, those groups of companies whose net profit showed greater fluctuation displayed greater variation in dividend rates than those whose profits were more stable.

Amounts of cash dividends in percent of net worth for the period 1929-41, covering selected samples of consumer instalment financing agencies and commercial banks, and, for 1934-39, all corporations and banks and trust companies filing income tax returns, are presented in Table 29.[22] The figures based on income tax returns for 1934-39, while not entirely comparable to the other series, indicate that "banks and trust companies" paid rates of dividends somewhat lower than "all corporations," and much lower than sales finance and personal finance companies.

In fact, dividends of sales finance and personal finance companies were at higher average levels than those of any of the other groups studied. Sales finance companies, however, showed materially greater variation than personal finance companies; their more noticeable decline during the depression and their subsequent skyrocketing coincided with greater fluctuations in their net profits.

Among industrial banking companies in the income tax sample average rates of dividends paid dropped sharply during the depression, but by 1936, like those of the other specialized agencies, exceeded on the whole their 1929 level. After 1936 insured indus-

[22] Throughout this section the terms "dividends paid" and "dividend payments" are used for simplicity and brevity. They generally refer, however, to cash dividend declarations (or authorizations, in the case of credit unions) within the calendar or fiscal year; ordinarily the dividend payment occurs within a month after the dividend declaration.

TABLE 29

CASH DIVIDENDS OF SELECTED SAMPLES OF CONSUMER INSTALMENT FINANCING AGENCIES AND COMMERCIAL BANKS IN PERCENT OF NET WORTH, 1929–41[a]

Sample	*1929*	*1930*	*1931*	*1932*	*1933*	*1934*	*1935*	*1936*	*1937*	*1938*	*1939*	*1940*	*1941*
Sales finance companies													
3 national[b]	8.4%	10.2%	7.3%	6.6%	6.3%	8.1%	14.3%	17.7%	17.3%	13.2%	12.4%	11.9%	12.0%
3 to 4 regional[b]	5.3	5.2	4.0	4.5	3.5	4.6	5.6	10.8	9.7	6.1	6.6	7.3	6.2
10 to 32 local[b]	6.9	6.3	6.3	4.3	4.3	6.2	7.5	10.9	10.6	6.6	6.4	6.9	7.2
202 local[c]	5.2	..	..	..	3.1	..	..	8.4	..	..	..	..	..
Personal finance companies													
1 to 2 national[d]	8.8	10.8	10.7	10.9	10.2	10.0	10.7	12.2	12.4	10.5	10.6	10.3	9.6
2 to 5 regional[d]	7.2	9.7	8.4	9.0	7.9	8.2	9.1	11.9	16.4	13.7	12.9	12.8	12.4
2 to 7 local[d]	..	..	..	5.8	5.1	11.6	7.5	7.4	10.3	10.7	7.2	7.2	8.0
153 local[c]	5.5	..	..	..	4.9	..	..	7.2	..	..	..	..	..
79 non-invest. type indust. bkg. cos.[c]	4.4	..	..	..	2.1	..	..	5.8	..	..	..	..	..
Invest. type indust. banks													
56 noninsured[c]	5.1	..	..	..	2.7	..	..	6.3	..	..	..	..	..
6 largest insured[e]	..	..	..	..	..	1.1	2.9	4.1	4.8	6.3	6.2	7.0	6.7
All other insured[e]	..	..	..	..	..	3.3	3.4	4.2	4.4	4.5	4.5	4.5	4.3
37 insured[c]	4.8	..	..	..	2.0	..	..	4.5	..	..	..	..	..
Credit unions													
All reporting federal credit unions[f]	..	..	..	..	..	..	1.0	2.0	2.6	2.9	2.9	3.0	2.6
Commercial banks													
All national banks[g]	6.0	5.4	5.1	4.1	2.4	3.1	3.7	3.8	3.8	3.7	3.9	3.8	3.7
All insured banks[e]	..	..	..	..	..	3.0	3.4	3.6	3.5	3.5	3.6	3.6	3.5
Banks and trust companies[h]	..	..	..	..	..	3.1	3.1	3.1	2.9	2.9	2.9	..	..
All corporations[h]	..	..	..	..	..	3.4	4.2	5.4	5.1	3.5	4.1	..	..

(footnotes on following page)

trial banks, except for the six largest, reported an almost constant rate of dividends on net worth, at about 4.5 percent. That of the six largest increased steadily between 1934 and 1940, but showed a slight decline in 1941.

The rate of dividends authorized by federal credit unions rose throughout the period 1935-41 except, again, for a slight decline in the latter year; but it was lower in percent of net worth than that of any agency, or of banks or corporations. Although credit union

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FOOTNOTES TO TABLE 29

[a] Represents total cash dividends declared or authorized during year (whether or not paid in same year or based on earnings of same year) of companies paying dividends, in percent of average or year-end total net worth of all companies. The number of companies for each year may be found in Appendix Table B-1, except as noted in footnotes below.

[b] Based on data from the National Credit Office, Inc. Net worth is the average of figures for the beginning and end of year. These samples differ from those used in other tables because, in order to increase the coverage, all companies that reported on dividends are here included, regardless of whether complete statements of income, expenses, interest and profits were available. In 1929 one national company, and in 1929-32 one regional company, reported on dividends, though not otherwise reporting a complete statement. The sample of local companies differs in each year, the numbers in the sample for each year being as follows: 1929, 10; 1930, 10; 1931, 13; 1932, 15; 1933, 18; 1934, 25; 1935, 28; 1936, 30; 1937, 32; 1938, 31; 1939, 29; 1940, 29; 1941, 29. Some of the local companies are included in the 202 local companies of the income tax sample.

[c] Based on tabulations prepared by the Income Tax Study. Net worth is the year-end figure.

[d] Based on data from the National Credit Office, Inc. Net worth is the average of figures for the beginning and end of year. These samples differ from those used in other tables for reasons given in footnote b above. Companies that reported on dividends, though not otherwise reporting a complete statement, were as follows: in 1929 one national; in 1930-31 and 1935-36 one regional; in 1932-34 two regionals; in 1932-33 two locals; and in 1934-35 one local. Some of these companies are included in the 153 local companies of the income tax sample.

[e] Based on data from Federal Deposit Insurance Corporation. Net worth is the average of figures for the beginning, middle and end of year, except for industrial banks in 1934 and 1935, when year-end figures are used. Cash depositories and banks designated in this study as insured industrial banks are included with all insured commercial banks.

[f] Based on data from U. S. Farm Credit Administration, Division of Finance and Accounts. Represents dividends authorized in percent of year-end net worth of all reporting federal credit unions.

[g] Based on data in Annual Reports of the Comptroller of the Currency. Net worth is the average of figures for call dates during the year.

[h] For all corporations, and for banks in 1938-39, based on data in *Statistics of Income*; for banks in 1934-37, based on data in the *Source Book* of the Bureau of Internal Revenue. The classifications for banks were, for 1930-37, "national banks" and "state banks and trust companies," and, for 1938-39, "banks and trust companies." Except for 1938-39 data on dividends pertain to all banks filing income tax returns—a slightly larger number than those filing net worth figures. Data on dividends include only dividends paid on common capital.

dividends may legally be, and generally are, as high as 6 percent of members' shares, three-quarters of the reporting federal credit unions at the beginning of the period, and one-quarter at the end, did not authorize dividends.

The dividend record of national banks over the forty years ending in 1929 reveals that during the last twenty-five years of that period the rate of return on total net worth had attained a degree of regularity reminiscent of contractual interest (Chart XV).[23] In *each* year from 1905 to 1929 dividends were paid at a rate of from 5.2 to 6.2 percent of total net worth. This high degree of regularity is explained by the fact that the amount of dividends paid from year to year increased at about the same rate as total net worth.

In 1932 and 1933 the dollar amount of dividends decreased sharply, as a result of the heavy charge-offs of the depression years, and by 1933 the rate on total net worth had declined to less than half its previous level. As the subsequent revival failed to restore the rate to its earlier level, it fluctuated from 1936 to 1941 within narrow limits—slightly below 4 percent of total net worth, or at about two-thirds of the average rate maintained over the earlier period.

In contrast to the regularity of rate of dividends on total net worth, the rate of dividends paid on capital stock exhibited a constant growth, with but minor fluctuations, from a low of 6.8 percent of capital stock in 1894 to a high of 13.7 percent in 1929 (Chart XV). The growth in rate of dividends paid on common capital, in contrast to the regularity in the rate on total net worth, may be attributed to the growing share of total net worth represented by surplus and undivided profits—or, conversely, to the diminution in the share represented by the par value of capital stock outstanding.

[23] Cash dividends averaged 5.5 percent of total net worth over the forty years. In eleven of the earlier years the rate was less than 5 percent but during the balance of the period 1890-1929 it showed little variation from year to year, as is evident from the following tabulation of the number of years in which rates were at various stipulated levels:

	1890–99	*1900–09*	*1910–19*	*1920–29*	*1930–39*	*1940–41*
Under 4½%	1	..	..	..	8	2
4½–5	7	3	..	..	..	..
5–5½	2	2	1	5	2	..
5½–6	..	4	8	3	..	..
6 or over	..	1	1	2	..	..

From 1910 through 1931 the rate of dividends was never less than 10 percent of capital stock; it exceeded 11 percent in all but two of those years, and was more than 12 percent in seven years.[24] During the early thirties the average rate dropped sharply, but it exceeded 4.5 percent of stock even at the low in 1933; in subsequent years the rate of common dividends recovered quickly, and from 1937 to 1941 averaged over 9 percent of common stock.[25]

Net Profit Paid Out in Dividends

In most years for which data are available, dividends of sales finance and personal finance companies amounted to between 50 and 100 percent of net profit, averaging about 80 percent; in only a few of the years did dividends exceed net profit.

Although industrial banking companies in 1929 and 1933 paid out the highest proportion of net profit in dividends, the dividends paid by insured industrial banks since 1934 have generally been less than half of net profit, probably reflecting the conservatism attendant upon the acquisition by these institutions of the status of banks.

The proportion of net profit authorized by federal credit unions to be paid out in dividends increased steadily throughout the period for which data are available, rising from 40 percent in 1935 to 61 percent in 1941. The latter level was still comparatively low, however, largely because of the relative youth of these enterprises. There is, besides, a stipulation in federal credit union law which requires the retention of 20 percent of net profit. In a new institution the added incentive to build up a backlog of reserves serves to curtail the authorization of dividends.

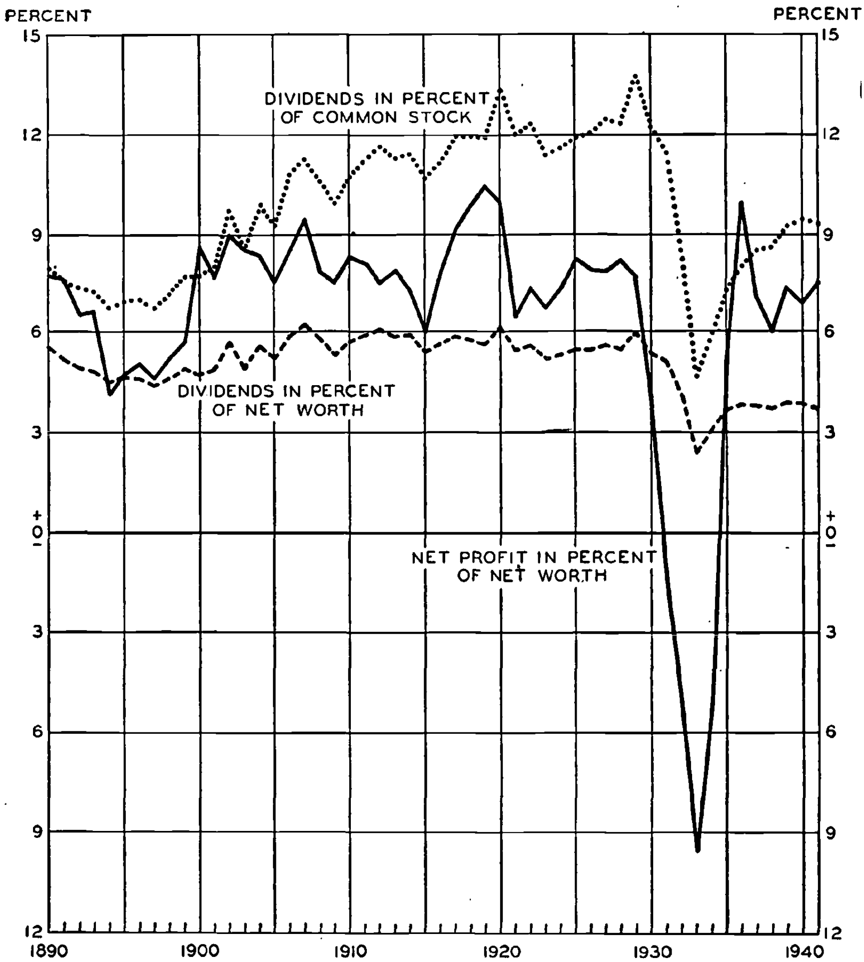
[24] Dividends averaged 10.7 percent of capital stock for the period 1890-1929, and 10.1 percent for the entire fifty-two years. The pattern of rates clearly elucidates the growth trend, as is evident from the following tabulation of the number of years in which rates were at various stipulated levels:

	1890–99	*1900–09*	*1910–19*	*1920–29*	*1930–39*	*1940–41*
Under 7%	4	..	..	..	2	..
7–8	6	1	..	..	1	..
8–9	..	2	..	..	4	..
9–10	..	4	..	..	1	2
10–11	..	2	2	..	..	..
11–12	..	1	8	4	1	..
12–13	..	..	..	4	1	..
13 or over	..	..	..	2	..	..

[25] Beginning in 1933, the rate of dividends on total net worth includes declarations on both preferred and common shares. The rate on common capital stock represents common dividends throughout.

CHART XV

RATES OF CASH DIVIDENDS AND NET PROFIT OF NATIONAL BANKS, 1890–1941[a]



[a] Based on Annual Reports of the Comptroller of the Currency. For 1890-1915 the numerator (dividends or net profit) pertains to the years ending August 31, 1890-1906, the ten months from September 1, 1906 to June 30, 1907, and the years ending June 30, 1907-15; and the denominator (common stock or net worth) pertains to June 30 or approximately that date. For 1916 the numerator pertains to the eighteen months ending December 31, 1916, adjusted to an annual basis; and the denominator is the average of figures for June 30, 1915, June 30, 1916, and December 31, 1916. For 1917-41 the numerator pertains to the years ending December 31, 1917-41; and the denominator is the average of figures for call dates during the respective years. Common stock represents par value.

For the forty-year period prior to 1930, dividends of national banks averaged about 70 percent of net profit; thus, on the average, about 30 percent of net profit was retained and added to net worth. Reference to Chart XV reveals that the relation of dividends to total net worth was much more regular than that of net profit to total net worth, and it is therefore not surprising to find that the proportion of net profit paid out in dividends fluctuated considerably from year to year.

Nevertheless, dividends exceeded 80 percent of net profit in only ten of the forty years prior to 1930, stood between 60 and 80 percent in twenty-six years, and were less than 60 percent in four years. Heavy net charge-offs resulted in a sharp drop in net profit in 1930, and in net losses in 1931-34, yet the payment of dividends was curtailed much less drastically.[26] Thus, although a reasonable average margin of net profit above dividends had been maintained from year to year, the heavy charge-offs of five bad years, combined with the continuance of dividend payments, wiped out a large percentage of the retained net profit accumulated over the preceding forty years.

Dividends paid by national banks over the entire period, 1890-1941, amounted to 82 percent of net profit. Over the years 1929-41, slightly more than the total net profit earned during that period was paid out in dividends.

Variation Among Individual Companies

The dividend record of individual consumer instalment financing companies included in the income tax sample is characteristic of an industry growing to maturity. In 1929, when practically all the companies reported profitable operations, one-third of the personal finance companies, and about one-fourth of the sales finance and non-investment type industrial banking companies retained

[26] The computation of rates of dividends on net profit is meaningless for the years 1931-34, when there were net losses. For the rest of the period 1890-1941 the number of years in which rates were at various stipulated levels is as follows:

	1890–99	*1900–09*	*1910–19*	*1920–29*	*1930–39*	*1940–41*
Under 50%	..	..	..	..	1	1
50–60	..	2	2	..	2	1
60–70	1	5	2	4	1	..
70–80	3	3	3	5	1	..
80–90	2	..	3	1	..	..
90–100	3	..	..	..	..	..
100 or over	1	..	..	..	1	..

all of their net profit to retire borrowings or to provide additional funds for working capital. Only among investment type industrial banking companies did an exception occur: in that group less than 10 percent of the companies with profitable operations retained all net profits.

In 1936 practically all the companies that showed profitable operations, and a few that sustained net losses, paid dividends.[27] In the interim their worth as potential borrowers had become more generally recognized, the rates of interest paid on borrowed funds had been reduced, and they were therefore no longer so dependent upon retained funds for expansion.

In addition, there was a pronounced tendency for the companies that did pay dividends to pay out higher proportions of net profit in 1936 than in 1929.[28] This, too, indicates less urge to provide for the possibility of expansion, temporary or permanent, through the retention of net profit. In 1936 fewer of the insured industrial banks than of any other type of company paid out a relatively large proportion of net profit in dividends—an indication that these banks had become more conservative with respect to the retention of net profit, at a time when other types of companies had become less conservative.

Also, companies that paid dividends paid higher rates on net worth in 1936 than in 1929.[29] In each type of company the proportion paying dividends of more than 8 percent of net worth increased between those two years, while the proportion paying dividends of 4 to 6 percent decreased materially. In almost all cases this rate represented a somewhat higher percentage on the par, or stated, value of the outstanding stock.

Companies paying a rate of more than 8 percent in 1936 accounted for nearly half of the sales finance group, one-third of the personal finance, and one-fifth of the industrial banking companies, except the insured industrial banks (where they constituted scarcely more than one-twentieth).

In each of the types, the smaller the company, the greater the

[27] This may have been in part the result of the surtax on undistributed profits in 1936 and 1937 upon the dividend payments of these companies. Since, however, the proportion of net profits paid out in dividends by the companies included in the National Credit Office sample was not out of line in those years, it is believed that the tax was not a major factor.

[28] See Appendix Table B-15.

[29] See Appendix Table B-16.

likelihood that it will retain all of its net profit in the business and not pay dividends, a tendency particularly noticeable among institutions showing profitable operations. In larger companies, especially those in which stock is widely held, there is considerable reluctance to withhold payment of a dividend, for fear of the effect of such action upon the marketability of the stock; in a small company, in which stock is generally closely held, this factor is not operative.

Among the specialized companies that did pay dividends, it appears from the income tax data that there was no marked relationship between size of company and either rate of dividends on net worth or proportion of net profit paid out in dividends. However, national and regional sales finance and personal finance companies, on the average, showed a higher rate of dividends than the locals, and a higher proportion of net profit paid out in dividends;[30] and the six largest insured industrial banks showed higher averages than the smaller institutions.

National sales finance companies consistently paid higher rates of dividends than the regionals or locals, and paid out the highest proportion of net profit of any of the consumer instalment financing agencies over the period. Their dividend rates were particularly high during the years 1935-37, when their level of profit was correspondingly high.

During the last few years a substantial, but decreasing, proportion of banks have refrained from paying dividends.[31] Among all the various measurable factors affecting payment or nonpayment of dividends size of bank was most important. It is true that the higher the rate of net profit (on net worth) the higher was the proportion of banks paying dividends, but the differences were much more striking when banks were arranged according to size. This greater influence of size persisted even when the influence of other factors, such as rate of net profit, rate of net earnings, and proportion of net worth (to total assets), was held constant.

These size differences reflect the greater willingness of the man-

[30] These averages are based on the net worth or net profit of all companies, whether or not they paid dividends. Very few, however, of the larger companies included in the National Credit Office sample reported nonpayment of dividends—among the sales finance companies, no nationals; 1 regional, in 1933; 4 locals in 1932-33, 3 in 1935, and 1 each in 1934, 1936 and 1938; among the personal finance companies, only 1 regional, in 1929.

[31] See Appendix Table B-17.

agement in a small bank, where the stock is usually closely held, to withhold dividend payments; and, conversely, the reluctance of the management in a large bank, where the stock is widely held, to withhold a dividend and thereby adversely influence the market value of the stock. With but one exception in 1939 and one in 1941 every bank with average deposits in excess of 50 million dollars reported that it had declared a dividend in the years 1939-41.

TABLE 30

RATES OF CASH DIVIDENDS PAID BY INSURED COMMERCIAL BANKS, 1939, BY NET WORTH PROPORTIONS AND RATES OF NET PROFIT[a]

Net Profit in Percent of Net Worth	*All Banks*	*Net Worth in Percent of Total Assets* Under 5%	5–10%	10–15%	15–20%	20% or Over
Minus (net loss)	1.9%	..	2.0%	2.0%	1.8%	1.9%
Under 5%	2.3	(1.7)%	2.3	2.3	2.2	2.3
5–10	3.2	(2.7)	3.0	3.1	3.3	3.4
10–15	4.1	(5.7)	4.0	4.1	4.3	4.4
15–20	5.2	..	4.8	5.2	6.1	6.6
20 or over	7.9	(8.8)	6.9	8.7	7.4	(6.9)
ALL BANKS	3.4%	5.0%	3.6%	3.5%	3.2%	3.0%

[a] Based on data from Federal Deposit Insurance Corporation. Rates of cash dividends represent cash dividend payments in percent of net worth of banks paying dividends; figures are averages of rates of individual banks. In regard to banks that were members of the Federal Reserve System net worth and total assets are averages of figures for call dates during the year, and in regard to non-member banks they are averages of figures for the beginning, middle and end of year. Cash depositories, banks designated in this study as insured industrial banks, and banks that submitted reports covering less than the full year's operations or whose operations were materially affected by mergers during the year are not included. Net-worth and net-profit rate groups are inclusive of the lower limit and exclusive of the upper. Parentheses indicate groups containing 10 banks or fewer.

Although there was a greater likelihood that a dividend payment would be made among larger than among smaller banks, there was no regular difference in the *rate* of dividends paid by the large banks as compared with the small.[32] The rate was highest for the largest banks, but it was almost as high for smaller banks, and much lower for medium-sized banks. In fact, the rate of dividend payments on net worth appears to have been most closely

[32] See Appendix Table B-18.

related to the rate of net profit on net worth, as can be seen from Table 30.

Irrespective of the net worth ratio, the higher the rate of net profit the higher was the dividend rate, and this tendency was both consistent and marked. Also, as can be deduced from Table 30, the proportion of net profit paid out in dividends was larger, on the average, among banks with a low than among those with a high rate of net profit.

Among banks with approximately the same rate of net profit the larger the net worth ratio the higher, in general, was the rate of dividends paid, but the relationship was not marked. Among banks with losses or with low rates of net profit the institutions with a low capital cushion paid as high a rate of dividends (representing a higher proportion of net current operating earnings) as those with adequate or high capital cushions. This tendency may well give the supervisory authorities cause for concern, when they recall how rapidly the retained net profits of the banking system—accumulated slowly over decades—were wiped out by the unusual charge-offs of a few years of depression.

Notes on the Character of the Data