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THE INVESTIGATION OF FACTORS INFLUENCING THE FORM IN WHICH FUNDS ARE MADE AVAILABLE FOR BUSINESS INVESTMENT

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Federal Reserve System

I Debt and Equity

Concern has been expressed intermittently in various quarters regarding the form in which funds are made available for business investment and particularly regarding the availability of equity funds. The sharp collapse of 1929-30 was in part ascribed to the overindebtedness of the economy, and as the decade of the thirties progressed, the failure to achieve complete recovery was attributed in part to the unwillingness of investors to take risks. Again at the end of World War II, when fears were expressed over the adequacy of the demand for investable funds, much significance was attached to the forms in which savings would become available for investment.

The premise underlying this concern is that the savings habits of individuals and their investment preferences are in some way directly related to the effective operation of the economic system. The question to which an answer must be sought, therefore, is: Has the manner in which individuals save and the form in which they hold their assets become inimical to the best operation of the economy? Clearly an enterprise system cannot operate successfully if all savings take the form of debt, that is, if all owners of wealth insist on holding fixed dollar obligations. While this extreme situation has not prevailed in the past, it is still true that by far the greatest proportion of the equity investment in business has come from retained earnings and from inflation of asset values, while a relatively small amount has been derived from the savings of individuals.

Nevertheless the demand for equity funds over the past half century has in general been adequately met by the three principal sources of capital supply. Certainly in the first two decades of the century, as well as in the forties, two of the sources — inflation and retained earnings — have been important factors in maintaining a satisfactory debt-equity ratio. Any case for attributing depression to the unwillingness of individuals to invest savings in equities must rest on the experience of the twenties and thirties. It may be argued that the prosperity levels of activity during the 1920's in residential construction, commercial building, public utility and municipal construction were heavily dependent on a volume of debt financing which could not be maintained indefinitely under a stable or declining price level, though this was probably true only to a limited extent of capital formation in the manufacturing, trade and extractive industries.

It may also be argued that the depression of the 1930's was deepened by the great volume of debt then outstanding and that rapid recovery was impeded, in consequence, by a lowering of the ratio of equity to debt through losses and deflation of asset values and by the public's increasing preference for fixed dollar investments.

The view that inadequate equity funds have contributed to depression has been explored elsewhere at greater length,[1] and while it cannot be claimed that these investigations have been exhaustive, they provide reasonable grounds for believing that a more restrained use of the debt instrument in some sectors of the economy in the 1920's would have prevented some of the malformations of that period and the prolongation of the ensuing depression of the 1930's.

The record of history is inconclusive as to whether debt, or the propensity of individuals to put their saving into debt forms, has been inimical to high level employment. Fears were often expressed that this might be the case in the years immediately following World War II but the threat of an inappropriate relation of debt to equity was overcome in those years by retention of earnings and the inflation of asset values. Nevertheless it is worthwhile to consider whether such a condition might arise in the future. The stability of an expanding economy might be jeopardized if prices were to be held stable, if through public policy or other means a greater than customary proportion of business earnings were to be distributed to owners, and if the propensities of individuals to hold fixed dollar media of investment, strengthened by the expectation of falling prices, were to be subject to secular increase.

[1] See Irving Fisher, *Booms and Depressions* (Adelphi, New York, 1932); and Homer Jones, "The Flow of Savings," Part I, *Journal of Finance,* October 1948, pp. 1-26; Part II, *Journal of Finance,* March 1949, pp. 28-46.

If inadequate equity in relation to debt in the financial structure of business should be judged a serious likelihood for the future, now is the time to consider means for its correction. One possible solution would be gradual inflation, which, other things equal, would steadily increase equity in relation to debt. Furthermore, individuals and institutional investors might be expected to adapt themselves to such a policy by putting more of their funds into equities and less into fixed dollar media. We shall proceed, however, on the assumption that a policy of chronic inflation, which is noted here without discussion of its demerits, is impracticable and will not be adopted.

A second possibility needing exploration is that retained earnings will be sufficient to permit business to absorb personal savings in the form of debt at a high enough level to ensure full employment. While we have inadequate comprehension of the force of the various influences which determine the volume of retained earnings relative to other savings, the possibility exists that stockholder demands and public policy may compel greater distributions of earnings in the future and force business to go to the public to a greater extent than formerly for equity funds. Should this potential need for new capital sources become real, individuals will have to increase their willingness to make equity investments and businesses will have to take positive steps to acquire equity money directly or through institutional intermediaries.

If public policy is to contribute to the encouragement of equity investment by individuals we need to know more about what individuals do with their savings, and why they make such disposition of them as they do. The literature on investment is full of hypotheses on this subject, but short on factual material. Suggestions for overcoming this factual deficiency through sample surveys of the saving and investing habits of individuals will be dealt with in the following section.

II Surveys of Consumer Finances

1 *General*

Two types of information may be obtained from sample surveys of consumer finances: 1) objective facts on various characteristics of individuals – age, sex, marital status, occupation, place of residence, source of wealth (e.g., inheritance), education, amount and pattern of assets, liabilities, income, family size, etc. – that may be associated with certain saving and investing patterns, and 2) responses to questions concerning the reasons why people hold their present assets and how they account for any changes that have occurred in recent years in the pattern of their assets and liabilities. Information of both types can best be obtained through intensive personal interviews of a relatively small and carefully selected sample.

2 *Sampling Special Categories of Investors*

It is by studying a great many special cases of large-scale individual investors that we can expect to gain the clearest insight into the factors that influence the extent of their savings and the character of their investment. To round out the investment picture, the factors influencing the availability of internal funds for business must be determined, and this can be done most accurately by interviewing a sample of businessmen.

Considerable work has already been undertaken along these lines, but if further progress is to be made special techniques of interrogation will be needed. A survey of consumer finances such as that of the Federal Reserve System — covering a sample of only about 3,500 spending units — suffers from the disadvantage that only a few of the consumers interviewed account for a large portion of the reported saving and of the accumulated wealth. One way of obtaining a larger sample of relatively wealthy individuals, though a very costly method, is to have an extremely large sample of the entire population. Another way is to oversample in certain respects — for example, tenants in high rent areas, residents of dwelling units of high value, or owners of expensive first-owner automobiles. Thus far, however, no reliable measure of correspondence has been established between such commonly supposed indicators of wealth and levels either of income or investment. A third possibility is to follow up an extensive mail questionnaire with the selection of high-income respondents for personal interviews.

Difficulties other than that of obtaining a satisfactory sample also stand in the way of any survey intended to reveal something of the behavior of wealthy investors. Many such individuals are more or less constantly on the move, living in hotels, or abroad and seldom at home. Once a sample of high income individuals has been identified, however, there is the additional difficulty of getting their cooperation. Unlike the lower income person, who generally responds without hesitation, the wealthy tend to be reluctant respondents. This makes little difference in many kinds of consumer surveys, but as we develop studies concerning savings, net worth and asset patterns, the problem becomes more acute.

The best approach to the very wealthy may possibly be through the good offices of a local banker. These persons need to be assured that there is no tax aspect to the interview. Perhaps they can be convinced, regardless of their political beliefs, that social benefit may accrue from such study; or perhaps there are other means whereby cooperation can be more readily obtained. The surmounting of this difficulty is one of the most important tasks to be faced if the quality of our factual information on the saving and investing habits of individuals is to be substantially improved.

3 *Miscellaneous Problems*

By singling out for examination certain of the hypotheses most commonly advanced in the past concerning savings and investment patterns we may throw some light on the factual materials that should be sought in surveys of consumer finances. Assertions are common that self-employment is conducive to equity investment. Thus, the farmer's savings are said to be invested largely in farm improvements; the owner of a closely held business is said to have a similarly convenient use for his savings. Also, the circumstances prevailing in small, closely knit communities, where personal relations are close, are considered more conducive to the provision of equity funds than those typical of urban centers. If this is true then the increasing numbers and influence of urban salaried workers may make the provision of equity capital even more problematical.

The supply of equity capital is thought to be further jeopardized by the concentration of wealth in the hands of certain groups of individuals, such as economically inactive women and the aged. We must discover to what extent persons like these, and the urban salaried worker, have distinctive patterns of asset holdings and saving.

Another common hypothesis alleges a general tendency to avoid investment risks, usually regarded as a result of the public's unfavorable experience with equities in the period following 1929. Study may well reveal changes in this attitude as a result of improved investment conditions and the general tendency in recent years toward inflationary price changes.

Although the tax rates of the twenties are not thought to have inhibited equity investment, the rates of the thirties and forties are generally pointed to as having effectively influenced individual investment decisions. To what extent do people react to the fact that income taxes reduce the average returns from risk investments relative to those from safer ventures? Would some type of averaging taxable returns over a period of years encourage venture undertakings? Are many important savers conscious of the double taxation of income from corporate stock, first as corporate income, then as personal income? Will this knowledge seriously affect their investment plans?

Obviously, high income tax rates greatly increase the attractiveness of tax-exempt securities to well-to-do investors. But what amounts are invested in tax-exempts in order to offset rises in personal income taxes?

And what yield differential, as between tax-exempt and nonexempt securities, is consistent with this type of investment preference? Would subjecting income from state and local securities to the same rates as income from other sources increase the willingness of individuals in the higher income brackets to invest in equities? These questions, which merely frame the problem, are all too often stated in the form of flat assertions.

Other closely related objectives are: 1) to discover how individuals evaluate their own ability relative to that of financial institutions to choose wisely among investment options, and 2) to determine the extent to which the final distribution of savings between debt and equity investment reflects the individual's calculations concerning quite different problems. In any event, the attitudes and preferences of individuals may be related closely to their age, sex, urban or rural location, income and occupational experience.

A survey which attempts to determine both the direct causes of an individual's choice as between equity and debt, and the nature of an individual's estimate of his investment abilities, should probably focus its inquiries on specific forms of investment, such as insurance, government bonds, state and local bonds, savings and loan accounts, savings bank accounts, retirement funds, rental real estate, marketable common stocks and closely held businesses. The past experience of individuals with these forms of investment must be determined. In the case of insurance policyholding and common stock ownership, it would be particularly important to learn something of the effects of advertising and salesmanship. Perhaps this line of inquiry will furnish a clue to the prevalence of higher priced policies despite the emphasis usually placed by individuals on the contingency aspect of their insurance plans. It may also help to determine the extent to which people are conscious of diversification of holdings by institutions. In addition to the information obtained through an improved survey technique, case studies of the investment of large fortunes should throw much light on this range of problems.

III Some Tentative Results

While the Survey of Consumer Finances periodically sponsored by the Federal Reserve System and conducted by the Survey Research Center of the University of Michigan has not been specifically designed to answer such questions as those detailed above, it has touched on a number of matters of interest in this connection. Among them is the finding that entrepreneurial types of persons — self-employed businessmen or farm operators — have had an influence on total consumer saving quite out of proportion to their numbers or their incomes. In each year from 1947 to 1949 these groups accounted for from 60 to 75 percent of total personal net saving, though they constituted only 21 to 22 percent of all consumer spending units and received only 28 to 30 percent of total consumer money income. This indicates that the problem of finding sufficient outlets for personal saving at high levels of economic activity may not be as great as has been thought in some quarters. Entrepreneurs have the best opportunity and the greatest incentive to invest, i.e., in their own businesses; also, they are probably the best informed group with respect to other business investments, including investment in new enterprises.

On the question of people's attitudes toward investing in fixed value savings bonds or bank deposits as against common stock or real estate, it was found in early 1949 that one in every ten consumer units with incomes of $3,000 or more rated savings bonds or bank deposits as their first choice for the investment of current savings. The most frequent reason given was safety. As for common stock, most consumer units in this income bracket did not favor such investment because they were either not familiar with it or believed it to be too risky. Consumer units at the level of $5,000 or more stressed the element of risk while those at the lower income level cited lack of familiarity as the chief deterrent. Preference for investment in common stock, and actual ownership of stock, increased quite sharply with income. Fewer than 5 percent of the consumer units with incomes of less than $3,000 owned any common stock while more than 35 percent of those with incomes of $7,500 or more reported such ownership.

Even the consumer units owning corporate stock tended to have more resources in liquid assets – i.e., in U. S. government securities and savings and checking accounts – than in stock. In early 1949 approximately two-thirds of the consumer units with $5,000 or more in liquid assets owned no corporate stock and of the one-third who did own stock roughly three-fifths held securities valued at less than $5,000. The same tendency to favor "safe" investment outlets was apparent among consumers with smaller amounts of liquid assets.

These data indicate no lack of funds potentially available for investment in corporate equities, either among individuals who owned no corporate stock or among those already participating directly in the capital markets. Fear of the risks involved and lack of familiarity with the market were apparently the basis of the limited corporate stock ownership.[2]

[2] For a fuller exposition, see "1949 Survey of Consumer Finances: Part VI. Ownership of Automobiles, Stocks and Bonds, and Other Non-Liquid Assets," *Federal Reserve Bulletin*, October 1949, p. 1186.

IV Role of Financial Institutions

In addition to surveys directed to individuals, it will be necessary to examine the investment holdings and attitudes of financial institutions. Our first concern should be to substantiate or to disprove the statement that there has been a tendency for individuals to place a larger proportion of their savings with institutions, a subject which is being exhaustively examined by Raymond Goldsmith. Such a rise in the importance of institutional investment may pose two problems: one, the relation of individuals to these institutions, and the other, the investment practices of the institutions themselves. Interviewing of personnel at financial institutions presents unique problems which may perhaps be most effectively conducted by means of case studies, but care must be taken so that the individual studies cumulate to a total which will provide a basis for framing useful generalizations.

The salient point to be established by these studies is the extent to which the shift to institutional investment inherently necessitates the choice of debt rather than of equity securities. If the investment policies of insurance companies, savings banks, trust funds and investment companies merely reflect the desires and attitudes of the persons placing their savings with them, then increased institutional investment will create no additional problems. However, to the extent that such institutions independently determine the relative proportions of their investment portfolios, as well as provide channels for the flow of funds from savers to production units, their growth may pose problems beyond that of the absorption of a given volume of saving.

Referring, for example, specifically to insurance companies, do their doubts concerning the liquidity of equities rest exclusively on their view of their functions? They are not likely to experience any net loss of funds; yet, even in those states in which they are permitted to acquire equities, insurance companies take less than full advantage of this provision. Does this suggest inherent limitations on equity investment by insurance companies or can it be explained on such grounds as the national nature of their business and the inhibiting effect of the New York law? A requirement that equity holdings be valued at current market prices, and informed opinion as to what is sound — as evidenced by state prohibitions and regulations on common stock investment by institutions — may operate to deter equity investment.

We must also examine, possibly on a sample basis, the cumulation and management of personal trusts. Why do people place funds in trust accounts? What role in trust formation may be assigned to the desire to avoid various taxes? Among what groups is the use of the trust most common? Do the circumstances surrounding the placement of funds dictate the trustees' choice of investments or is this due mainly to trust law and custom?

All transfers of funds to investing institutions raise questions as to the amount of personal saving involved relative to current expense. Insurance is, of course, the prime example but it has so far been very difficult to determine from individuals the value of their policies and the rate of saving which these impose. It may be possible to obtain more concrete information on this subject by identifying the policies of interviewees and consulting the insurance companies for relevant basic data contained in them.

V Business Saving

Finally, the saving patterns of business must be studied. Primary emphasis should probably be placed on the determinants of the magnitude of retained business earnings. However, the volume of savings made by businesses does not in itself offer any assurance of the amounts that will be invested. Corporations may retain earnings in liquid form with no transference into real investment. Questions paralleling those asked of individuals should be designed to ascertain the characteristics of business investment.

In considering the amount of saving by business units, we shall again want to verify common assertions concerning the relative extent of business and nonbusiness saving. The fact is that we are very deficient in factual information bearing on this problem. The data for the years before 1920 are fragmentary and difficult to compare with later data. The 1930's and the 1940's constitute such a distorted period of prolonged depression and of war that they throw but limited light on what we might expect the sources and the volume of saving to be in a period of comparative economic stability.

Despite the limitations of historical data, more knowledge concerning the interaction of business saving and general economic fluctuations in the past may be obtained from surveys and case studies. We can expect to encounter great difficulty at the level of small-scale, closely held enterprise. Questions of the definition of saving and consumption will arise in the case of family firms and enterprises in which certain assets are used both for business and consumption. The paucity of business records for such units may also constitute an additional obstacle. The survey methods suggested should be used to probe the possibility that for various forms of enterprise saving results simply because the entrepreneur has not found it desirable or practical to alter his level of living radically to conform to fluctuations in profits.

The determination of dividend policy is another area that merits very careful examination. An appreciable increase in the distribution of dividends might well alter the proportions of entrepreneurial and nonentrepreneurial savings. With respect to corporate saving, we should want to find out if retention of yearly earnings to permit constant dividends poses a different problem from conscious retention for expansion. These are only a very few of the problems needing further investigation; many others are raised in the paper by Messrs. Jacoby and Weston.

In conclusion, my chief thought is that the major facts regarding the sources and the availability of funds for business investment are yet to be ascertained. The motives that determine who saves, and how much, are still largely unevaluated. The factors governing the way in which savers tend to hold their current savings — thus influencing the redisposition of accumulated assets — are not well known. Also the influences operating to determine portfolio policy for institutional investors need further evaluation. Public policy in these areas cannot be held in abeyance pending accumulation of further knowledge; but if we are to validate — or reject — the many hypotheses which encumber this field, and make progress toward a more informed public policy, research might be directed to the areas designated.

Discussion and Comment

Discussion:

RAYMOND W. GOLDSMITH

As I see it, Mr. Jones's paper consists of two fairly independent parts. The first is a brief summary of what I might call the "devil theory" of debt which the author has developed in much more detail in some other studies, the most substantial of which is as yet unpublished. The second consists of a call for more and better survey data on saving and asset holding.

To start with the second part, I wholeheartedly agree with Mr. Jones's basic thesis that more survey type data on the motives determining individual, business and institutional decisions on saving and asset holding are urgently needed, and that we now know woefully little about these matters. I am particularly glad to notice his emphasis on the importance of studying changes in asset holdings which do not involve net saving or dissaving but rather rearrangements of the balance sheet. There are just a few points on which I would put more emphasis than Mr. Jones does or go a little further than he appears to go.

First, it seems to me that what we need is not only more emphasis on saving and asset holdings in the current income and expenditure surveys, but a fairly elaborate survey devoted exclusively to these matters. This immediately raises the problem of financing.

Second, I suggest that in such surveys we devote much more attention to what individuals themselves regard as saving and dissaving, instead of imposing on them our own definition and classification of saving. If we do this we may well find that individuals' definitions of saving and dissaving are very difficult to fit into a national system of social accounts. This would be only one more argument for the separation of measurements best fitting a system of social accounts from those having the highest motivational significance.

Third, financial life histories of individuals, as well as businesses, are about as important as information on their current saving activities and their current asset holdings. The stratification of results by respondents' age is only a partial substitute for the collection of information on assets and liabilities of the same individuals over a protracted period of time.

Fourth, I submit that the survey data will acquire their full value only if analyzed together with the historical material, particularly in the form of time series we already have or which we could accumulate with a not unreasonable amount of effort and expense. There seems to have developed in recent years an overemphasis, by no means limited to or even particularly pronounced in this paper, on current surveys, as compared to comparative historical analysis. We need both, if only to check the results of the two approaches. We need the historical record to find out, even if imperfectly, whether respondents actually do or did what they say or think they will do or did. We need, in particular, a comparison of time series and survey results because for the past we virtually have no surveys, and we want to know to what extent we can trust whatever time series material we possess or can work up.

This certainly is not the place for an extensive discussion of the theories Mr. Jones has developed about debt and equity funds, some aspects of which he has compressed into the pages which form the first part of his paper. The few remarks I am going to make on this section are quite preliminary, and may be based at some points on a misunderstanding of the real arguments of the author, or on ignorance of the actual data which have led him to his conclusions.

1) I am worried about the disregard in the paper, although possibly not in the full study, of the point of view of the individual supplier of funds, i.e., the refusal implied in much that is said in the paper to take savers' wishes as expressed in their decisions regarding asset holdings as final.

The apparent preference of savers for claims compared to equities may not be to our liking, but why should we regard it as less valid than, for instance, the high position that many consumers reserve for tobacco and liquor in their scale of preferences? Arguments against the high propensity to save in the form of claims, which apparently underlie the paper, seem to me incompatible with an approach based on the premise that the economic machine is steered by the decisions of consumers and savers.

In other words, the position taken by Mr. Jones seems to call for a fully developed theory of welfare economics, and I do not find in the paper reason to assume that such a theory is being developed or is accepted by the author. This criticism would be valid even if the apparent preference of savers, particularly small savers, for claims were as irrational as so many economists assume it to be when they discuss the equity problem. While this is a matter calling for much further study, I should at least like to venture some doubt whether individual savers' attitudes on this point are so irrational from their point of view.

Investment in equity securities, particularly of enterprises about which the saver knows little and on whose policies he has no influence whatever, is from his point of view a very risky venture — and generally the riskier the smaller the enterprise – unless the amount is limited to a small fraction of his total assets. We need not be astonished that such risks are not often taken by small savers unless they are unusually well informed about equity investments or unless their speculative proclivities are strong. This argument, of course, will lose strength and the one underlying Mr. Jones's paper will gain, as forms of equity investment reducing risk, e.g., by diversification through the use of investment companies, become more common.

2) I miss in the paper a clarification of the question whether the purported undue emphasis on debt is a recent phenomenon. In other words, would the desired increased emphasis on equity financing represent a return to the good old days, or would it constitute an advance into a promised but unfamiliar land? A clear stand on this point would also call for a decision as to whether the core of the problem is a supposed tendency toward excessive debt financing or the dance of the dollar.

3) I should like to take exception to an impression given by the paper which again may be due to the extremely compressed nature of the argument, *viz.*, that investment is good *per se*. We certainly do not have to be Keynesian to recognize that there may be situations in which a shift from investment to consumption expenditures, or at least a change in the distribution of the increase in national income between investment and consumption, is called for in the interest of stable growth.

4) Finally, so far as the empirical verification or illustration goes, it is not sufficient to start with 1929, although I realize that it has become a rather general habit to date our economic history from that unlamented starting point, or what is worse, to make the twenties our standard of comparison. To give sufficient generality to such conclusions it is necessary to go back at least as far as 1910.

Discussion:

DONALD B. WOODWARD, *Mutual Life Insurance Company of New York*

We in the United States are indeed very much more fortunate than the rest of the world. The paper by Homer Jones and indeed most of the conference papers can be taken to emphasize the difference between this country and others. The problem to which these papers are devoted is what form the investment of saving should take – as between debt, equity, etc. But if we were abroad in almost any country, we should be concerned about a much more difficult question, i.e., whether there would be any or a sufficient volume of saving at all. I cannot feel that such a vast difference is unimportant and it should not pass unnoted.

Homer Jones has done a most interesting job, as he always does. He has long felt very strongly that debt is an adverse influence in the economy. He argues cogently on the subject. He is doing a very great service to keep this question prominent in economic discussion. I say this in order to avoid any possible misunderstanding in the several questions I wish to raise about his paper.

First, the relationship between debt and depression needs more analysis and exploration in my opinion. There is no significant evidence of which I am aware demonstrating that debt has in fact contributed to general economic instability. Of course, debt is adverse in individual cases where trouble has come, but this is quite different from proof of a general influence. The point may be pressed still further. Are there not meritorious aspects of some debt on some occasions? Have the vast proportion of business institutions and individuals who have utilized debt over time been so extremely wrong-minded? I suspect that in fact a considerable catalogue of advantages of debt could be made. Probably if there were no such thing as debt, then debt would have to be invented. The question of its dangers belongs in economic discussion; but there would be merit in a development of the other side of the case as well.

Second, I want to suggest that the meaning of debt has somewhat changed during the last decade or two. To a degree the form has changed in many significant aspects in some areas and, even more broadly, the substance of debt has undergone a considerable change. Debt is no longer, if it ever was preponderantly, the instrument by which the poor widow is thrown out of her home and compelled to sacrifice herself for bread for her children. Indeed the hard, sharp line between debt and equity, which at least seemed to exist in the past, has become very much blurred and inexact.

Some examples may suffice. In the development of consumer debt in the past three decades a very great amount of flexibility has been introduced. In nearly all institutions doing consumer financing, the terms of the obligation are altered rather freely to meet the changing circumstances of any individual who is making any reasonable effort to fulfill his obligation. Installments due are waived, maturity is altered, and additional funds are advanced in need to care for emergencies and to reconstitute the financial position of the individual. Substantially the same development has come in agricultural indebtedness. The farmer who will exert any reasonable effort and who has any reasonable prospects can have his indebtedness adjusted and readjusted to suit his altered circumstances. In the debt of corporations the same developments have occurred as well as some additional ones. The income bond has attained some prominence, requiring charges to be paid only if earned. The subordinated debenture has come to have considerable use. A growing part of corporate debt is directly negotiated and held by only one or a few creditors; this permits easy renegotiation to fit changing circumstances, instead of inescapable appeal to the bankruptcy court, when creditors are exceedingly numerous and rigidity is, therefore, inevitable. In actual fact, alteration of terms of indentures has become quite frequent and simple in this form of obligation. Finally, in urban mortgage debt the same flexibility which marks consumer, farm and corporate debt has become general. In addition, a considerable proportion of the debt on housing involves government provisions, whereby the property in difficulty will pass to a federal agency. This means that the demoralization of markets through necessitous liquidation, which has been so distressing in some past periods, should not reoccur at least in such violent form.

I do not mean to suggest that creditors have become philanthropists. It is simply that standards have changed and probably still are changing. The best way to protect assets by a creditor is no longer believed to be the way of greatest harshness. This alteration has not, so far as I know, been anywhere explored and explained. It has in all probability quite considerable importance. Analysis dealing with debt should be careful not to rest on concepts that may have been true three or four or more decades ago but have since considerably changed. And there seems to be an important job for someone to do in analyzing and describing the alteration in the form and substance of debt.

Third, I should like to register some doubt about the thesis of a super premium on debt available for financial institutions. Obviously, the development of a super premium is hypothetically possible. It is the actuality of its existence at present which I question. There are many markets in which institutional investors and noninstitutional investors meet. In addition, individuals always have the free choice of placing their funds directly or through institutions. I suggest merely that the point deserves further study and should admit at the same time that some of my associates do not share the doubts I have on this subject.

Fourth, the market place is almost wholly ignored in this discussion. A number of suggestions are made by Mr. Jones to stimulate the flow of savings into equity but nowhere is it suggested that this might be done or might come about through the operation of the market place by providing it a little more freedom. Actually I think the market place is a more influential mechanism than the discussions by Mr. Jones and others suggest. A very large number of people are at work constantly seeking to maximize return on investment and very far-reaching investment decisions are made by these people on the basis of market conditions. The market deserves far more attention and emphasis in discussion of business finance than it has received at this conference. I know that much has happened to modify and alter the functioning of the market place since 1929 and since the *General Theory* was published in 1936. Nevertheless, it is still functioning and is still a highly significant institution.

Comment:

JAMES S. EARLEY, *University of Wisconsin*

Mr. Jones has properly stressed the importance, and the difficulty, of securing reliable representative samples of investors in the higher income groups. In this connection a project we are now conducting at Wisconsin should be of interest to members of the conference.

This project, financed jointly by the National Bureau of Economic Research and the University, is a study of investment holdings of individuals, related to their income and other relevant characteristics, based upon Wisconsin individual income tax returns. As you may know, Wisconsin income tax returns are open to public inspection. Moreover, the taxpayer is required to list, by amount and specific source, each item of his investment income, from all sources other than U. S. government securities.

We are obtaining a sample of some 4,000 returns (embracing both spouses in the case of married persons) who received investment income in 1949. Although our sample extends throughout the whole income range, we are heavily over-sampling the upper income groups where most individual investment holdings are found. The sample has been built upon a much larger one taken for a study currently being conducted by the State Legislative Council. We believe we shall have a reasonably representative sample of investment income recipients at all levels of income and in different parts of the state.

We shall try to construct the pattern of investment holdings of the persons in our sample by valuing the investments from which their income was derived. We will analyze each listed source of dividend income from stocks to determine the number of shares held, and ascertain their average value in 1949. Stocks on closely held corporations will be valued at book value. Interest received from savings accounts and notes and mortgages, and dividends from savings and loan associations, will be capitalized at appropriate rates. The par value of corporate and other bonds held will be calculated on the basis of the interest received and the coupon rate, and then changed to average market price in 1949.

Each of these steps entails special difficulties, but we have done enough preliminary work to indicate that the difficulties are not insuperable.

The result of our study will be a snapshot picture of individual investment holdings (other than U. S. government securities) in Wisconsin as of the end of 1949, together with data concerning securities sold during the year. We believe this information will in itself be of considerable value in showing the investment attitudes and practices of persons in different income strata. It would be possible, of course, to carry on a similar study over time, using an identical sample of returns. Furthermore, it would be possible to apply the interview technique to such a sample as ours.

Naturally, the individual identity of the persons in our sample is not being divulged. However, it might be possible to provide subsequent investigators with a representative list of names and locations of persons in our sample for independent interview investigation, without divulging financial information concerning these individuals.

After this sample had been interviewed, it would be possible to go to the income tax returns to check on the accuracy of responses and to secure supplemental information. Under proper safeguards, it might be possible to arrange for checkbacks to the data in our present study.