Volume Title: The Share of Financial Intermediaries in National Wealth and National Assets, 1900-1949

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Nature and Limitations of this Report

This report is a by-product of, and in some directions a supplement to, a study of financial intermediaries which forms part of the investigation by the National Bureau of Economic Research into the trends of capital formation and financing in the American economy. The main study will attempt to describe statistically and to analyze trends in the growth of financial intermediaries and in their role in the American capital market since the turn of the century. One important aspect of the growth of financial intermediaries is the proportion of national wealth or assets administered by these institutions. Because this aspect is of interest not only to students of financial institutions but also to those concerned with changes in the economic structure of the United States, the findings in this field are made available before completion of the full study of financial intermediaries.

From the economists' point of view, the development of financial intermediaries and the trend of their share in national assets and wealth deserve attention as an indication of the extent and character of financial interrelations, which in turn help to determine how capital expenditures are financed and how existing assets are shifted among owners. Both are of importance in directing the flow of saving into investment and possibly even in influencing its size. They thus ultimately bear on the fundamental relationship between a country's financial organization and the rate and pattern of its economic growth.

This paper is part of a broader study yet to be published, and this imposes a few limitations. Probably the most important is that the derivation of the basic data used is not shown in detail. The complete study will provide full documentation, which would have lengthened this paper unduly. Thus many of the underlying figures will, for the time being, have to be taken on faith. It may be well to state by way of summary that the figures on the assets and liabilities of the different groups of financial intermediaries are derived as a rule from generally available and well-known statistics, particularly for the largest groups of intermediaries such as commercial banks, savings banks, life insurance companies, and government insurance and trust funds. Even in these cases, however, it has often been necessary to fill gaps in the original statistics and to provide additional breakdowns not given in the original data. For other groups of intermediaries the estimates had to be based, at least for the earlier part of the period, on samples of large companies, e.g. for property insurance companies or on the institutions operating in certain states, e.g. for savings and loan associations and credit unions. In some cases, finally, it proved necessary to develop entirely new estimates. Personal trust funds administered by banks and trust companies and self-administered private pension funds are the most important examples.[2]

In addition to the figures on assets and liabilities of different groups of financial intermediaries, we need estimates of national wealth and of national aggregates for specific assets and liabilities, particularly the amounts outstanding of real estate mortgages of different types, corporate and government bonds, preferred and common stock, and short-term credits to business and consumers. The estimates of national wealth used differ only slightly from those published in summary form[3] in *Volume Fourteen, Studies in Income and Wealth* (National Bureau of Economic Research, 1951), pp. 18-19. National totals for some of the specific intangible assets and liabilities were readily available, particularly for the period from 1929 on. For others, primarily corporate stock, new estimates had to be developed, and their derivation was sufficiently complicated to require description in an appendix of the full study.

[2] These new estimates will be described in appendixes to the main study and in R. W. Goldsmith, *A Study of Saving in the United States* to be published in 1954 by Princeton University Press.

[3] More detailed data, supplementary information, and description of sources and methods used will be included in Volume III of *A Study of Saving in the United States.*

Coverage

This report defines financial intermediaries broadly as institutions that receive funds from other economic units as creditors, stockholders, or trustees and use these funds to make loans to, or to buy securities of, other economic units which they do not control,[4] rather than to acquire tangible assets for operation as most nonfinancial enterprises do.

This definition encompasses about two dozen types of institutions now operating in the United States, which are listed below.

Institutions Included among Financial Intermediaries

I Banking System
- 1 Federal Reserve banks
- 2 Commercial banks
- 3 Mutual savings banks
- 4 Postal Savings System

II Insurance
- 1 Private life insurance companies
- 2 Fraternal insurance organizations
- 3 Private self-administered pension funds
- 4 Federal pension, retirement, and social security funds[a]
- 5 State and local pension and retirement funds[a]
- 6 Fire and marine insurance companies
- 7 Casualty and miscellaneous insurance companies
- 8 Mutual accident and health companies

III Miscellaneous Financial Intermediaries
- 1 Savings and loan associations
- 2 Credit unions
- 3 Management investment companies[b]
- 4 Investment and bank holding companies[c]
- 5 Investment installment companies[d]

[a] Includes all trust funds administered by federal, state, or local governments.
[b] Includes so-called "mutual funds."
[c] See Securities and Exchange Commission's report, *Investment Trusts and Investment Companies* (1939), Part I.
[d] On nature and operations of these companies see U.S. Securities and Exchange Commission's report *Companies Sponsoring Installment Investment Plans* (1940).

[4] This clause is necessary to exclude nonfinancial holding companies which are not regarded as financial intermediaries for the purpose of this study, primarily because the problems they raise are of an essentially different nature and are more like those of operating enterprises, at least for holding companies the subsidiaries of which are wholly or almost wholly owned.

6 Mortgage companies
7 Federal and joint-stock land banks
8 Government lending institutions
IV Personal Trust Funds Administered by Banks and Trust Companies

These institutions have been arranged into four main groups: (1) the banking system, (2) insurance, (3) miscellaneous financial intermediaries, and (4) corporate fiduciaries. The first three main groups may be regarded as financial intermediaries in the narrower and more usual sense of the word. Corporate fiduciaries, i.e. the personal trust departments of commercial banks and of trust companies, are included for three reasons: their large size and their importance for the capital market, the similarity of their investment practices to those of some other financial intermediaries, and the institutionalized nature of their relationship to the trustors.[5] For some purposes an alternative grouping has been found more useful, that of private and public financial intermediaries.

The delimitation and coverage of the groups actually used in the investigation is necessarily influenced by the availability and character of statistical material. For that reason figures for a few types of institutions are shown separately, although they are of small quantitative importance and might well have been amalgamated with larger similar groups; and a few types of institutions which certainly fall within the definition of financial intermediaries have been omitted altogether (e.g. life insurance departments of savings banks; common trust funds administered by banks and trust companies) because the preparation of adequate estimates would require an effort not regarded as warranted in view of the small magnitudes involved.

More significant and more debatable is the omission of investment banking institutions (including security brokers and dealers) and of finance companies[6] (primarily sales finance and per-

[5] It is the absence of the third characteristic that leads to exclusion of noncorporate fiduciaries from the definition of financial intermediaries. For most of the individuals who act as fiduciaries, this is not their main or permanent occupation.

[6] On the operations of these companies see the National Bureau of Economic Research series "Studies in Consumer Instalment Financing," particularly Volumes 1, 2, and 4.

sonal loan companies) from the main set of tables on which this paper is based. In both cases there are conceptual reasons that might justify the omission, but practical considerations have been decisive. Conceptually, the exclusion of investment banking institutions and finance companies may be based on the fact that, in contrast to the other groups included, most of the funds which they employ consist either of equity or are supplied by other financial intermediaries, primarily commercial banks. But more important is the practical consideration that no combined balance sheets are available for either of the two groups, and that it did not appear possible to obtain data of sufficient reliability or in detail comparable to that for most other groups. The material, however, is sufficient to indicate that the total assets of the two omitted groups are not likely to have exceeded 5 per cent of the assets of all financial intermediaries at any benchmark date except 1929 and were considerably smaller than that at most dates, hardly exceeding 2 per cent in 1949. Omissions of investment banking institutions and finance companies thus could not affect the major trends with which this paper deals. Table 2 permits a rough evaluation of the relative size of these two groups compared to the other groups of financial intermediaries included in the tabulations.

Selection of benchmark years

If data were freely available, and the costs of assembling them or readers' patience were of no consideration, it might be desirable to present figures for the assets and liabilities of financial intermediaries as well as for the relevant national totals for every single year. Actually, however, annual data are as yet unavailable for several groups of financial intermediaries, particularly personal trust departments. For others the preparation of detailed annual figures, while not impossible, would be extremely laborious. Even apart from these considerations, presentation of the entire statistical material on an annual basis would unduly swell the report and might obscure rather than clarify the main movements.

It was thus felt that the most important trends would be better developed and presentation greatly simplified by restricting the study to benchmark years at important turning points in the financial history of the country so located that the intervals between them constitute periods of relatively homogeneous economic character. On the basis of these considerations as well as of the availability of data, particularly the concentration of detailed national wealth estimates on a few dates, eight years – 1900, 1912, 1922, 1929, 1933, 1939, 1945, and 1949 – have been selected as benchmarks.

The first of the seven periods formed by these benchmarks, the years 1901 through 1912, is long enough to provide what may be regarded as a typical picture of the period preceding World War I, a period now possibly appearing as an example of quiet normalcy but in fact one of rapid expansion and changes in the field of finance. The second period, covering the years 1913 through 1922, is dominated by the effects of World War I and its aftermath on the American economy and its financial structure. The third – 1923 through 1929 – covers the high plateau of the late twenties, a period that indelibly marked the financial structure and habits of the country. The next, comprising the four years 1930 to 1933, is the shortest but one of the most dramatic, covering one of the longest and most severe depressions in American economic history. The benchmarks of 1933 and 1939 delimit another period of deep change in the financial structure of the country and bracket essentially the entire era of New Deal reforms. The sixth period, lasting from 1940 through 1945, is, of course, entirely dominated by World War II. The last period starts with 1946 and terminates with 1949, since sufficiently detailed data were not yet available for later years when most of the statistical work on this report was done. Although this period is influenced by the adjustment from war to peace, particularly during its first half, it is probably reasonably close to a typical situation at mid-century.

The draft of this paper was essentially completed by the end of 1952. As a result of further work on some of the material, the full study will show some differences in figures and interpretation, usually of a minor nature, and will include estimates for the end of 1952.

Terminology

Most terms used have the meaning generally assigned to them in financial or accounting terminology or are explained when first encountered in this paper. It may, however, be helpful for some readers to review the content of the main terms used.

Tangible (or real) assets include land, structures, equipment, inventories, livestock, gold, and silver.

Intangible (or financial) assets cover all balance sheet assets other than tangibles. They are divided into claims and equities.

Claims are limited to the creditor's side of relationships between economic units evidenced by debt instruments and by informal or imputed relations similar to them in character, and hence appear only on the asset side. They include accruals.

Equities (or equity securities), likewise used only as an asset item, include the shares of corporations, proprietors' interest in unincorporated business enterprises, and beneficiaries' interest (excess of assets over debt) in private financial nonprofit institutions and government corporations and trust funds.

Debt (or liabilities) is the counterpart, from the debtor's point of view, to claims. It therefore appears only on the right-hand side of balance sheets and includes accruals.

Net worth is the difference between total assets and total liabilities and is defined equally for all types of economic units. It is sometimes divided into earned net worth (cumulated saving), contributed net worth (payments by proprietors for shares or other equities), and unearned net worth (net realized and unrealized capital gains).

National wealth is the sum of tangible assets within the national boundaries and the difference between foreign assets (tangible assets located abroad owned by nationals plus equity of, and claims against, foreign units held by domestic units) and foreign investments (liabilities to foreigners plus foreign holdings of domestic tangible assets and of equities in domestic units).

National assets is the sum of the total assets — intangible as well as tangible — of all economic units within the nation as shown in their actual or constructed balance sheets. National claims and liabilities and national net worth are correspondingly defined.

Investing (or capital formation) is limited to expenditures (gross or net of capital consumption allowances) on durable tangible assets, i.e. assets having an expected life of three years or more. The term includes expenditures arising in change of hands of durable tangible and of intangible assets. The results of investing are called investments.

Saving is the difference between current income and current expenditure, i.e. expenditure on non-durable assets.