

A recent innovation in municipal security financing has been the development of municipal bond investment funds. These are registered investment companies, the assets of which are invested in municipal securities.²³ The tax exemption of the interest income on the municipal securities is "passed through" to the holders of the shares in these bond funds, which by the end of 1965 aggregated \$249 million.

While personal trust funds have expanded their holdings of municipal securities over the past two decades, municipal securities as a percentage of assets have varied but little, rising from 10.4 percent in 1946 to 13.2 percent in 1955 and to 13.7 percent in 1965. However, in recent years many of the commercial banks (that administer these personal trusts) have established common trust funds for investments in municipal securities, with the number of such "tax-exempt" funds rising from 24 in 1962 to 104 in 1965. Analysis of personal trust holdings of municipal securities²⁴ finds (a) an increasing trend in revenue bond investments, (b) considerable investments in maturities of 10 to 20 years, with some investments in maturities over 20 years, (c) while there is some reliance upon bond ratings, most trust departments prefer to do their own credit analysis, and (d) neither intended use of proceeds nor geographical location of borrower have much influence on municipal security investment decisions.

To round out the picture, chapters 29 and 30 present materials on "nonfinancial corporations" and "individuals" as sources of funds for investments in municipal securities. As shown in table C4, "other corporations" have expanded their holdings of municipal securities (mainly short term) from \$0.3 billion in 1946 to \$1.2 billion in 1955, and to \$3.6 billion in 1965. "Individuals and others" (a residual calculated by subtracting all identifiable investor groups from total holdings shown in column 1 of table C4) have grown from \$3.4 billion in 1946 to \$10.6 billion in 1955 and to \$20 billion in 1965.

(b) *Portfolio Considerations*

Most of the foregoing investor groups buy municipal securities because they find the tax-exempt yields more attractive than the "after tax" yields obtainable on investments where the income is taxable. These comparative yield considerations come into play after appropriate allowance has been made for what may be called "portfolio considerations."

Commercial banks must necessarily consider their liquidity requirements, the demand for loans from business and consumer borrowers and their legal needs to hold Government securities as collateral for Government accounts. Funds that remain after these needs have been accommodated are then invested in "bonds," with municipal security investments depending upon a comparison of the tax-exempt yields with the bank's particular tax situation (income subject to tax). During periods of credit tightness, since commercial banks generally seek to accommodate their business and consumer customers first, their net expansion in municipal security investments tends to diminish.

Fire and casualty insurance companies similarly have to review their cash flows and income picture as well as comparative yields in

²³ See ch. 27 for a description of these funds.

²⁴ See ch. 28.