

determining whether to buy municipals. These companies necessarily consider whether their insurance underwriting is at a profit (or loss) and the amount of their taxable portfolio income before seeking municipal securities that yield a tax-free income. When, as in recent years, underwriting losses are heavy, many of the companies have less need for tax-exempt income and their purchases of municipals have fallen off correspondingly.

In the case of personal trusts (and, as appropriate, individual investors), comparative yields as contrasted to marginal tax rates is the principal determination governing investments in municipal securities, after due allowance has been made for the expenditure requirements of the income beneficiary (or individual). The higher the tax bracket of the personal trust (or individual investor), the greater is the need for tax-exempt income. Many nonfinancial business corporations, after considering their cash flow requirements, invest a portion of their cash balances in municipals so long as the tax-exempt yield compares favorably to the after tax returns on alternative short-term investments.

For institutional investors such as life insurance companies or mutual savings banks (which have appreciably lower marginal tax rates than high income individuals, most nonfinancial corporations, commercial banks or fire and casualty insurance companies) the prime consideration is a comparison of tax-exempt municipal yields with taxable investment yields. Generally, these institutions have less immediate liquidity or expenditure requirements. In the case of life insurance companies, as detailed in chapter 23, investments in municipals take place if their yields are from 60 to 90 percent of taxable yields (mainly if the ratio is above 80 percent) or if the tax-exempt yield is 50 to 100 basis points lower than the taxable yield.

State and local public retirement funds and State and local governments, because of their tax-exempt status, have little reason to acquire municipal securities when their yields are lower than those on taxable securities. Since the restrictions on investments by these public funds are increasingly being relaxed, there has been a corresponding decrease in their holdings of municipal securities, with an even sharper fall off in new investments. So far, private noninsured pension funds, which, if qualified, are also tax-exempt, have not invested in tax-exempt municipal securities.

3. *Projected Municipal Security Financing: 1966-75*

According to the materials presented in volume 1, State and local public agency capital requirements for public facilities for the decade 1966-75 are estimated at \$327.8 billion, of which \$31.6 billion is estimated for 1970 and \$40.7 billion for 1975. With interpolations for the remaining years of the decade, assuming an annual rate of increase of about 5.5 percent, and assuming that the financing patterns during 1956-65 will continue in the following decade,²⁵ supplement B translates these capital requirements into estimated annual net changes in State and local government debt outstanding. Such annual net changes in debt are projected to rise from \$8.5 billion in 1966 to \$11.3

²⁵ Long-term borrowing will account for about 50 percent of capital outlays; long-term borrowing for capital outlays represents 92 percent of all long-term borrowing; and the rate of annual debt retirements will rise gradually each year at an incremental rate of 0.05 percent per year from an estimated level of 5.60 percent in 1965. Evaluation of these and other assumptions appear later in the text.