7. MAKING MUNICIPALS MORE ATTRACTIVE

A further question was asked in the survey regarding the alternatives, if any, that might increase the attractiveness of municipal securities if tax exemption were removed. Although it was made quite clear by the respondents that nothing could adequately replace the attractiveness of tax exemption, and that if the exemption feature were removed there would be an increase in yields, numerous suggestions were put forward that (according to the respondents) would partially offset removal of tax exemption. A Federal guarantee of municipals was by far the most often quoted suggestion with a State guarantee of the issues of political subdivisions following close behind.

Among the ideas put forward was one suggesting that the Federal Reserve System liberalize its regulations in order to permit banks to use municipal bonds to secure advances without the payment of a penalty discount rate. Other suggestions related to improvement in the municipal secondary market and the setting up of sinking funds. Some other recommendations that were mentioned include—

(*a*) Codification of the laws governing the issuance of municipal securities so that it will be easier to determine both the legality and the financial status of such issues.

(*b*) Uniform municipal accounting and financing reporting in order to have better standards for comparing various issues.

(*c*) Elimination of advance refundings which have been largely motivated by opportunities arising from the ability to obtain higher yields by short-term investment of the proceeds from the sale of such securities.

(*d*) Financing of the neediest State and local governments by some type of specialized Federal program.

(*e*) Use of municipal securities held by commercial banks to meet part of their reserve requirements.

C. Present and Future Municipal Bond Holdings

The past 20 years show clear evidence of a continuous municipal bond buildup by commercial banks, with such holdings rising from \$3.5 billion in 1944 to \$33.6 billion in 1964, an increase of nearly 10 times. Viewed as a percentage of total loans and investments, State and local government securities of commercial banks have gone from 3.3 percent in 1944 to 12.1 percent in 1964. Table 14 shows the growth of both loans and investments and State and local government securities of commercial banks during the 1944–64 period. Table 15 indicates that over the 1944–64 period, total loans and investments increased by \$172.6 billion, or 162.8 percent, while municipal securities climbed \$30.1 billion, or 860 percent. During the 1944–54 period a \$50.8 billion increase for total loans and investments, or 47.9 percent, was accompanied by a \$9.1 billion, or 260 percent increase, for municipals. Taking the 1954–64 period only we see that loans and investments increased by \$121.8 billion, or 77.7 percent, while municipals rose \$21 billion, or 166.6 percent.