

TABLE 7.—*Tax-exempt yields and equivalent taxable yields*

Tax-exempt yield in percent	Federal income tax brackets		
	30 percent	50 percent	70 percent
1.00	1.42	2.00	3.33
1.50	2.14	3.00	5.00
2.00	2.85	4.00	6.66
2.50	3.57	5.00	8.33
3.00	4.28	6.00	10.00
3.50	5.00	7.00	11.67
4.00	5.71	8.00	13.33

Source: Adapted from a table published by Bache & Co., Inc., New York.

3. TAX EXEMPTION AND FEDERAL GUARANTEES

It cannot be stated at what interest rate levels, as compared with the interest rates on taxable loans and investments, municipal securities become attractive as investments. The key factor is the marginal tax rate of the beneficiary. When yields on State and municipal securities are low—for example, at 1.65 percent—and the yields on corporate bonds are at 2.66 percent, those taxpayers with marginal income tax rates above 38 percent would benefit by tax-exempt securities. However, when tax-exempt bonds yield 3.27 percent and corporate bonds yield 4.35 percent, those taxpayers with marginal income tax rates above 24.8 percent would fare better with tax-exempt securities. Obviously, there are more taxpayers with the lower marginal income tax rates than with the higher marginal rates. At almost any given spread between yields on municipals and yields on corporates, there would be some taxpayers who would benefit from tax-exempt income. As the marginal income tax rate that would equalize the yield on municipals with the yield on corporate bonds declines, the number of potential investors who could profit from tax-exempt income will increase. Since 1952 this marginal rate has not been above 30 percent.

Despite the value of the income tax exemption, there are some situations in which State and local government securities are attractive for other reasons. Thus, in Pennsylvania a personal property tax virtually eliminates corporate bonds from a trust account subject to the tax. Such accounts are invested in Pennsylvania tax-exempt securities regardless of the income tax bracket involved.

There doesn't seem to be anything needed at the present time to make municipal securities more attractive for trust account investment, except possibly a subsidence of inflation which would benefit all fixed-income investments in relation to other investments. A Federal Government guarantee of municipal securities would eliminate the discipline of the marketplace. The relatively high credit rated borrowers would be left on about the same basis as the relatively poorer credit risks and there would be the possibility that less desirable local projects, from an economic point of view, would be undertaken. If the tax-exempt feature of municipal securities were removed in exchange for a Federal Government guarantee, municipal securities would thereby lose their chief attraction. Clearly, it is the tax-exempt feature that attracts most investors to State and local government securities, rather than their quality, because those seeking safety pri-