

CHAPTER 30

Individuals as a Source of Loan Funds*

INTRODUCTION

Most of the financial savings in the United States are owned by households either in the form of claims on financial institutions or in the form of securities and mortgages issued by businesses, governments, and other households. Savings by households that are deposited with financial institutions give rise to a demand for financial assets by these institutions, a process which is called financial intermediation. Individuals thus contribute to State and local debt financing both by direct ownership of State and local securities and as holders of claims on financial institutions which, in turn, may be investors in State and local obligations. Individuals also supply funds to State and local obligations as owners of personal trust funds.

As of the end of 1965, individuals—including personal trust funds and nonprofit institutions—are estimated to have held directly \$40.5 billion of State and local obligations representing 40 percent of the total amount of this type of debt. This compares to other marketable bond holdings by individuals amounting to \$31.1 billion; these consisted of marketable U.S. Government securities and corporate and foreign bonds. At the same time, however, individuals' holdings of corporate stocks were much larger, amounting to about \$670 billion at current market prices, and their holdings of cash, time deposits, and savings bonds totaled \$421 billion. Individuals' direct holdings of mortgages were relatively small, but the exact amount is difficult to estimate. When all these categories of financial assets are taken together as a measure of the individuals' portfolio of financial assets, it appears that State and local obligations accounted for 3.5 percent of the total portfolio.

The above data are taken from the Federal Reserve flow-of-funds accounts where individuals' financial assets are estimated as residuals by deducting institutional holdings from debt and asset aggregates. Direct information on the type of household that owned State and local debt is available from the 1962 Federal Reserve Survey of Financial Characteristics of Consumers. Estimates from this survey do not include the holdings by personal trust funds and by nonprofit institutions. Of the 57.9 million families or unrelated individuals in the United States at the end of 1962, it appears that only 3 percent had direct holdings of marketable bonds of any type and less than 1 percent were holders of State and local obligations. The combination of a relatively low yield and tax-exempt status of income from State and local debt, makes this type of investment attractive to consumer units in high income tax brackets, but not to those in lower brackets.

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