

the portfolio management decision to be made in relation to the long-time horizon of pension commitments. Despite competitive pressures to show good performance, the outcome of decisions is still to be judged over an extended period of time. If the illiquidity of a financial asset carries a premium in yield, pension funds are in about the best position to capture it. Hence the evolution of portfolio management has been steadily in the direction of holding less liquid assets, even in State and local government retirement systems.

The stability of lending and investing in the capital markets obscures some variability in the pace of forward commitments for directly placed corporate obligations and mortgage loans. The tendency to enlarge forward commitments in periods of strong demand for funds may have the effect of contributing to a situation in which idle balances are being activated and velocity is rising. However, there can be no important shift into claims on pension funds and pension fund managers have little capacity or inclination to supply liquid assets, such as Government securities, to holders of idle balances.⁵ The important role of these funds, therefore, is as a rather neutral financial intermediary between savers and investors, with little impact on income velocity or the money markets.

We have observed that both State and local government and private plans, as suppliers of loanable funds, have shown a strong preference for corporate securities. Our projections for the future show a continuation of the growth of participation in the area of real estate finance. Slow but steady progress has been made in solving the administrative and expense problems of handling mortgages. It is now possible for a pension fund to secure most of the services normally encompassed in home-office administration from organizations which economically perform these functions. A mortgage portfolio can be handled with almost the ease and economy of a bond portfolio. If net yields after allocated expenses are competitive, risk factors considered, there will undoubtedly be a substantial growth in pension fund mortgage lending across the Nation in conventional as well as FHA-insured and VA-guaranteed loans. By the late 1970's, the volume could easily be comparable to the average net acquisitions of mutual savings banks in recent years.

The ownership of real estate equities would appear to be a natural avenue of investment. Sale and leaseback financing has been, in fact, a growing outlet. The tax-exempt status of a private pension plan, however, can be impaired by engaging in an unrelated business. The operation of income-producing property, especially if the purchase is financed with borrowed funds and only an equity position is retained, is susceptible to being considered such an unrelated business. The tax benefits from accelerated depreciation to a real estate operator, and his ability to introduce substantial financial leverage, usually justify his paying a higher price for property than a pension fund is prepared to pay without these possibilities. Hence, pension fund ownership of true real estate equities is not likely to grow rapidly in the years ahead.

⁵For a full discussion of these points, see Victor L. Andrews, "Noninsured Corporate and State and Local Government Retirement Funds in the Financial Structure," in *Private Capital Markets*, Englewood Cliffs, N.J., 1964, especially pp. 463-481.