

movement of capital to limit balance-of-payments deficits. Although it may be argued that foreign investment is too risky for pension fund assets, growth in pension systems can release other assets for international development.

There is the further evidence of capital shortage in the secular rise in long-term interest rates over the last two decades. It is hardly necessary to point out the tremendous capital needed in the future for the profitable development of space, underwater technology, urban renewal, and transportation and communication facilities, to mention just a few capital intensive areas of the American economy.

The question remains as to whether or not the funding of pension plans will lead to more efficient allocation of capital than would occur with a pension system financed primarily on a pay-as-you-go basis with reinsurance. The funding of pension plans places retirement savings in the hands of financial institutions whereas in nonfunded plans the savings are invested by the sponsoring corporations.⁶ Since financial institutions are free to invest in a full range of alternatives, aggregate productivity of capital should be greater than if funds were invested solely in the assets of the company sponsoring the plan. Tax-deductible pension contributions and tax exemption for fund earnings foster the establishment of funded plans and thereby improve the capital allocation process.

The argument that national economic goals are fostered through financial intermediary channels rather than through direct corporate savings can only be supported if the investment managers do a good job of allocating capital. Some indication of this is given in table 1 which shows the portfolio composition of various types of pension funds at the end of 1966. Corporate noninsured funds have been most aggressive in terms of common stock investments while multi-employer and union plans have been more aggressive in the mortgage market. State and municipal funds historically invested primarily in various Government obligations. Thus their record in terms of aggressive capital investment has been poorest of all. Insured pension funds are heavily committed to corporate bonds and mortgages due to legal restrictions, but have been turning more to equities as these restrictions are liberalized.⁷ If there is to be an indictment of pension fund investment, it is that too much emphasis has been placed on fixed-income obligations whereas investment objectives indicate very little need for fund liquidity. However, the record has been improving and, as will be pointed out in the section on investment management, will continue to improve if properly fostered.

Further evidence concerning the quality of investment management and the productivity of pension fund assets is found in a preliminary report of a research study of pension fund investment management by the Financial Executives Research Foundation.⁸ This re-

⁶ We are not arguing that corporations bear the cost of pensions. Under various circumstances, the costs may be shifted to employees, customers, stockholders, or the taxpaying public. We are concerned here with who holds the assets from which future benefits will be drawn. It seems unlikely that a company with an unfunded plan would pay higher wages or charge lower prices than if it had a funded plan. Thus, no matter who ultimately bears the cost of the benefits, the company with an unfunded plan should end up with more resources to invest.

⁷ Insured pension funds are not shown in table since investments are not reported separately from other insurance company assets.

⁸ Dietz, Peter O., "Measuring Rate of Return on Pension Funds," *Financial Executive*, July 1966.