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Member Bank Earnings and Expenses

Eighth District member banks' net profits were less in 1951 than in 1950, despite the fact that gross earnings were at an all-time peak. Expenses too reached a new high, but did not rise proportionately as much as income. While the banks had more net current earnings (and other incoming funds) to work with than ever before, a larger share went for losses and charge-offs, nearly as much went to reserves for future losses, and a much bigger slice went for income taxes. Thus the amount available for dividends and additions to capital (net profit after taxes) declined sharply in 1951 and, because dividends were increased slightly in dollar amount, the smallest remainder in years was added to capital accounts.

Over the years the pattern of distribution of net earnings and other incoming funds has changed. Relative to earnings, losses and charge-offs have fluctuated, dividends have remained fairly steady, income taxes have risen and district member banks have retained less.

The 1952 Deposit Ownership Survey

The 1952 Survey of Deposit Ownership showed an increase in total volume of deposits with areas outside metropolitan centers claiming the bulk of the increase. Distribution of the increase among owner groups was different than in the preceding Survey year and in 1952 favored noncorporate businesses, farmers and individuals.

The relatively greater growth in these favored groups reflects primarily the increased rate of consumer saving in 1951 and to some extent, preparation for heavier tax payments.

Eighth District member banks' net profits were less in 1951 than in 1950, . . .

Net profits of Eighth District member banks in 1951 totaled $29 million, $2 million less than in 1950. This decline in net profits occurred despite the fact that gross earnings (and other incoming funds) reached an all-time high in 1951. After all obligations had been met, the amount available to strengthen capital accounts was the smallest in all but one of the past seven years. Between this year's high earnings (before taxes) and low level of capital account additions lay the biggest income tax bill ever paid.

. . . despite the fact that gross earnings were at an all-time peak.

In 1951, earnings of Eighth District member banks climbed to an all-time high of $137 million, about 10 per cent above the 1950 earnings of $125 million. Two factors caused this rise: (1) an increase in earning assets with most of the increase being in loans and, (2) a slight increase in the average rate of return on loans.

Total assets in 1951 reached the largest volume in district banking history, $5.5 billion. The expansion over 1950 was $317 million. Of this amount, $104 million reflected a growth in loans. Loans equaled 27.8 per cent of total assets in 1951, as compared with 27.0 per cent in 1950. District member banks earned a somewhat higher average rate of return on loans in 1951 than in 1950, 5.6 per cent instead of 5.5 per cent. Enlarged loan volume and higher rate of return raised earnings on loans from 53.4 per cent of total earnings to 56.0 per cent.[1]

A part of the expansion in bank assets ($87 million) took the form of investments in United States Government securities. Emphasis on loan expansion reduced the proportion of total assets invested in Government securities from 41.5 per cent in 1950 to 38.8 per cent in 1951. Income from Government securities accounted for only 27.4 per cent of total income in 1951, a 2 percentage point drop from 1950.

Early in 1951 the Federal Reserve System increased reserve requirements of member banks 2 per cent on net demand deposits and 1 per cent on time deposits. This increase made it necessary for district member banks to carry an additional $80 million in reserves, and the percentage of cash assets to total assets rose from 23.5 to 25.4 during the year.

[1]Ratios used in this article are from the annual study of operating ratios made by this Bank. In computing the ratios, averages were taken of asset and liability items in the December 30, 1950, June 30, 1951, and October 10, 1951 reports of condition. Earnings and expense items were for the calendar year 1951. Ratios are arithmetic averages of individual ratios of 492 member banks. Ratios computed in this way differ in some instances from ratios computed from aggregate dollar amounts. Copies of the operating ratio report may be obtained from the Research Department of the Federal Reserve Bank of St. Louis.

Expenses too reached a new high, but did not rise proportionately as much as income.

The cost of doing business also rose to a new high in 1951 with total operating expenses amounting to $81 million, about $7 million more than in 1950. As a percentage of total incoming funds, however, expenses were smaller than in 1950, or to put it another way, the percentage increase in expenses was smaller than the percentage increase in gross earnings. Higher salary costs were mainly responsible for the higher expenses and required 31.2 per cent of total earnings in 1951 as compared with 30.2 per cent in 1950. Interest on time deposits dropped from 7.3 per cent of total earnings in 1950 to 7.1 per cent. These percentage figures are, of course, ratios of interest paid on time deposits to total earnings in each year. During 1951 the rate of interest paid on time deposits was increased at a number of banks and time deposit volume moved up as well so that on both counts the outlay by district banks for interest on time deposits increased. However, the more rapid increase in total earnings resulted in a slight decline in the percentage cost of time deposit interest paid. All other expenses, as a group, continued to claim about the same proportion of total earnings as in 1950.

While the banks had more net current earnings (and other incoming funds) to work with than ever before, . . .

Since the rise in expenses in 1951 was at a lesser rate than the increase in earnings, district member banks enjoyed the highest net current earnings of all time, $56.1 million. By way of comparison these banks had net current earnings in 1950 of $50.2 million.

Table I presents a fairly complete picture of the funds at the disposal of bank management and the use made of these funds. The more conventional approach omits, except as memoranda, the disposition of some current losses (charged to reserves previously set up) and accounting for some current recoveries (credited to established reserve accounts). In other words, the more conventional presentation fails to show in balancing form all incoming funds and all dispositions. In point of fact, both net current earnings and previously established reserve accounts are factors in the determination of the use of funds and both should be included in any accounting of sources and uses of bank funds.

Items 3 through 8 of Table I show the sources and total amount of incoming funds that banks had to work with each year in the period 1948 through

1951. In addition to net current earnings, district member banks in 1951 had recoveries (on losses previously charged off) and profits on securities of $3.6 million. They also had reserves of $825,000 which were no longer needed and were, therefore, transferred to income. The banks also called into use during the year $2.3 million from established reserves and returned $540,000 in recoveries to these reserves. Total funds that district member banks had to work with in 1951 amounted to $63.3 million, well above the $56.8 million available in 1950.

. . . a larger share went for losses and charge-offs, . . .

Losses on loans and securities are charged against income, or against previously established reserves for losses on loans and securities. As shown in Table I, district member banks in 1951 had losses and charge-offs against income of $8.7 million, as compared with $5.1 million in 1950. In 1951 these losses and charge-offs amounted to 14 per cent of the total amount that banks had to work with, whereas in 1950 they were only 9 per cent. In 1948 and 1949 they were 11 per cent and 12 per cent respectively.

District member banks in 1951 also charged $2.8 million to reserves previously set aside for losses on loans and securities. Proportionately, charges made directly to reserves have been small in the four-year period ranging from 2 per cent to 5 per cent of incoming funds.

. . . nearly as much went to reserves for future losses, . . .

Federal tax law allows certain tax benefits to banks for reserves set up to take care of bad debt losses on loans based upon an average loss experience of previous years. Following clarification of the law in 1947 banks began setting up such reserves in 1948. In Table I reserves for bad debt losses on loans are combined with other valuation reserves on loans and securities. The largest total transferred to reserves for losses on loans and securities by district member banks was just under $10 million in 1948. In the three following years the totals transferred to these reserves were $6.7 million, $5.5 million and $5.2 million in that order. When calculated as a percentage of total incoming funds, the amount transferred in 1948 was 20 per cent. Since then the proportion has dropped to 13 per cent in 1949, 10 per cent in 1950 and 8 per cent in 1951.

. . . and a much bigger slice went for income taxes.

Any accounting of bank earnings and expenses will quickly emphasize income taxes. District member banks in 1951 paid the largest income taxes in history—$17.9 million, a larger amount than was added to capital accounts. The amount of income taxes paid in 1951 was substantially above the $13.7 million paid in 1950, and was more than double the $8.5 million paid in 1948. In the three years 1948-51, shown in Table I, income taxes rose $9.4 million although the total amount of funds that district member banks had to work with expanded only $12.5 million. Of the increase in earnings and incoming funds over the period, 75 per cent went for income taxes.

Thus the amount available for dividends and additions to capital (net profit after taxes) declined sharply in 1951 and, because dividends were increased slightly in dollar amount, . . .

Holders of stock of district member banks received $11.8 million in dividends in 1951, a slight increase over 1950. Compared with 1948, dividends in 1951 were up $1.5 million although the amount of incoming funds increased, as noted, $12.5 million.

TABLE I

BANK MANAGEMENT OF NET CURRENT EARNINGS PLUS OTHER INCOMING FUNDS AND PREVIOUSLY SET-ASIDE RESERVES *

(Eighth District Member Banks)

(Thousands of Dollars)	1948	1949	1950	1951
Sources of Incoming Funds				
1. Earnings	$106,703	$113,500	$124,528	$137,126
2. Less Expenses	66,041	69,109	74,339	81,052
3. Net Current Earnings	40,662	44,391	50,189	56,074
4. Recoveries and Profits Credited to Income	5,992	5,160	4,374	3,601
5. Recoveries Credited to Reserves	296	632	556	540
6. Transfers from Reserves to Income (Release of reserves previously set aside to cover possible losses)	1,442	1,200	678	825
7. Portion of Reserves Called into Use during Year (Net reduction in previously set-aside reserves: line 10 minus line 5)	2,433	1,217	979	2,271
8. Total Incoming Funds	$ 50,825	$ 52,600	$ 56,776	$ 63,311
Uses of Funds				
9. Losses and Charge-offs Made against Income	$ 5,699	$ 6,010	$ 5,103	$ 8,733
10. Losses Charged to Reserves	2,729	1,849	1,535	2,811
11. Additions to Reserves from Income	9,993	6,755	5,484	5,202
12. Additions to Capital Accounts	13,513	17,256	19,658	16,816
13. Dividends	10,419	10,703	11,275	11,850
14. Taxes on Net Income	8,472	10,027	13,721	17,899
Total Uses of Funds	$ 50,825	$ 52,600	$ 56,776	$ 63,311

* Includes only reserves for bad debt losses on loans, and valuation reserves on loans and securities.

The dividend rate in 1951 was 3.1 per cent of total capital accounts. In the period 1939-51, the rate has ranged from 2.9 per cent to 3.2 per cent.

. . . the smallest remainder in years was added to capital accounts.

Deposits increased during the war and postwar years at a much faster rate than banks added to capital accounts. The ratio of capital accounts to total deposits, one factor in measuring the adequacy of bank capital, declined from 15.5 per cent in 1939 to a low of 6.0 per cent in 1946. By the close of 1951 district member banks had strengthened their capital account-total deposit ratio to 8.0 per cent despite an increase in deposits. The dollar total transferred by district member banks to capital accounts in 1951 was $16.8 million. This, however, was the smallest amount to be transferred to capital accounts since 1944 with the exception of 1948 when substantial reserves for bad debt losses on loans were established.

Over the years the pattern of distribution of net earnings and other incoming funds has changed.

Table II shows in percentage form how district member banks distributed total incoming funds. The thirteen years covered in the table fall roughly into three periods. In the early period from 1939 through 1943, income taxes were not reported separately but were combined with other taxes as an expense item. The proportions shown in Table II for this period are estimates. In the middle period (1944 through 1947) income taxes became a more important factor and absorbed an increasing part of total incoming funds. In the last period (1948 through 1951) another factor changed the pattern of distribution: the banks set up substantial reserves for bad debt losses on loans.

Relative to earnings, losses and charge-offs have fluctuated, . . .

In the pre-war years of 1939 and 1940 losses and charge-offs were heavy as a portion of total net current earnings and other incoming funds of district member banks. The percentage allocated to losses and charge-offs declined steadily until by 1943 it was at the lowest point in the early period, 23 per cent of total funds. During the middle period (1944-1948), losses and charge-offs required between 17 per cent and 20 per cent of funds.

In the last period the percentage figure increased, ranging from 21 to 36 per cent. In this period, however, the percentage figure includes with the losses and charge-offs, the losses charged to reserves and the funds used to build up these reserve accounts. The combined percentage figure is heavily influenced each year by the additions to reserves and is not strictly comparable with the percentage figures on losses and charge-offs used in the two preceding periods. Excluding the percentage representing the addition to reserves, the share of incoming funds set aside to meet losses and charge-offs was below that of the earlier periods.

. . . dividends have remained fairly steady, . . .

The proportion of total incoming funds that went to pay dividends has remained fairly steady although the dollar amount has risen due to the expansion of capital accounts. Fluctuations in the percentage of funds distributed as dividends range from a low of 18 per cent to a high of 26 per cent. In the early period from 23 per cent to 26 per cent of funds went for dividends. In the middle period the level was somewhat lower ranging from 18 per cent to 23 per cent. In the last period the percentage was fairly steady at 19 per cent and 20 per cent.

. . . income taxes have risen and district member banks have retained less.

Income taxes have risen almost steadily. In 1943 and 1947 the proportion of funds paid out as

TABLE II
BANK USE OF FUNDS
Percentage Distribution of Total Incoming Funds
(Eighth District Member Banks)

	'39	'40	'41	'42	'43	'44	'45	'46	'47	'48	'49	'50	'51
1. Losses and Charge-offs Made Against Income	43%	44%	31%	31%	23%	17%	18%	18%	20%	11%	12%	9%	14%
2. Losses Charged to Reserves	....	....	....	....	....	....	....	....	....	5	3	2	4
3. Additions to Reserves From Income	....	....	....	....	....	....	....	....	....	20	13	10	8
4. Additions to Capital Accounts	26	20	30	28	38	46	44	43	38	27	33	35	27
5. Dividends	23	25	25	26	24	23	20	18	21	20	20	20	19
6. Taxes On Net Income *	8	11	14	15	15	14	18	21	21	17	19	24	28
	100%	100%	100%	100%	100%	100%	100%	100%	100%	100%	100%	100%	100%

* Estimates for years 1939-1943—Federal Reserve Bank of St. Louis.

income taxes showed no change from the preceding years' levels and in 1944 and 1948 the percentages decreased. With these exceptions, the percentage of earnings and other incoming funds paid out for income taxes increased from 8 per cent in 1939 to an all-time high of 28 per cent in 1951.

Larger losses and charge-offs, more dividends or greater income taxes make themselves felt in the amount of funds remaining with which to strengthen capital structures. Over the years, however, the amount of net earnings and other incoming funds put back into the business has averaged one-third, with the annual percentages varying from 20 to 46 per cent. After a peak of 46 per cent in 1944, the percentage declined irregularly to 27 per cent in 1951. Broadly speaking, as the percentage of funds paid out as income taxes increased from 1944 through 1951, the percentage added to capital has declined.

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The 1952 Deposit Ownership Survey

The 1952 Survey of Deposit Ownership . . .

Once each year the Federal Reserve System with the cooperation of member and nonmember banks conducts a survey of deposit ownership. The 1952 Survey, as usual, reports on the volume of individual, partnership and corporation demand deposits as of the close of the preceding year. Time deposits are not covered by the Survey, nor are demand deposits standing to the credit of the United States Government, states, political subdivisions of states, or banks. Deposits covered by the Survey accounted for well over half of total deposits and for three-fourths of all demand deposits at the beginning of 1951. Also, as usual, the 1952 Survey shows the pattern of ownership, as of January 31, of the demand deposits of individuals, partnerships and corporations. These patterns of ownership show the demand deposit holdings of eleven economic groups, the first six of which are further divided into corporate and noncorporate segments.

Survey results throw additional light on the character and trend of deposits, an important question for banks in the management of their assets and for those interested in the flow of funds and business conditions in the economy.[1]

Analysis of Survey results in this article will be restricted to movement of funds, changes in ownership patterns, and the probable influence of major business developments during 1951 on changes in the volume of demand deposits held in certain areas. Fuller treatment of changes in ownership of funds, a "Sources and Uses of Funds" analysis similar to the report on the 1951 Survey published in this Review in April 1951, will follow in a succeeding issue.

. . . showed an increase in total volume of deposits . . .

The first important measurement established by the Survey was the total of demand deposits of individuals, partnerships and corporations at all banks in the Eighth District as of December 31, 1951. This total was nearly $5 billion, an increase of $300 million, nearly 7 per cent, over that of a year earlier.[2] The growth in 1951 was approximately the same as the increase in these deposits in 1950.

The similarity between the two years in terms of deposit growth is noteworthy in view of the difference in the degree of inflationary pressure on prices in the two periods. An analysis of the relation between changes in the money supply and prices should consider not only changes in aggregate money volume, but changes in where and by whom it is held and for what purposes. The 1952 Survey sheds some light directly or by inference on these questions.

. . . with areas outside metropolitan centers claiming the bulk of the increase.

In terms of geographic distribution of the 1951 changes in deposit-money volumes, each of the deposit survey areas (see map), reported more deposits on December 30, 1951, than a year earlier. But the growth during 1951 was more pronounced, in absolute amounts and percentagewise, outside the metropolitan centers. The largest per cent growth occurred in Area XIII, southern Indiana

[1] "The character and trend of a bank's deposits are probably the most important determinant of liquidity requirements. A thorough analysis of the bank's deposits should be undertaken annually in order to determine, as far as possible, their relative stability . . ." *Commercial Bank Investment Policy*, Bank Management Commission Publication No. 126, American Bankers Association, New York, 1951, p. 10.

[2] Table I, showing demand deposits of individuals, partnerships and corporations for all banks in the Eighth Federal Reserve District by areas, is based on deposit volumes at the close of each year. Table II, showing these deposits in terms of ownership, uses a different time: January 31 of each year. In this district individual and business deposits customarily decline in the month of January but, of course, not always by the same amount. Thus comparisons on a year-to-year basis as of January 31 will be somewhat different from those on a December 31 basis. The differences, however, are small.

nearly uniform rate of growth for metropolitan and rural areas is in contrast with the change over the full seven-year period from 1945 to 1952. Over the longer period, as Table III and the small insert charts in connection with the map show, growth in deposit volume has been considerably faster at the metropolitan areas than at the rural ones, measuring the return flow of funds to the cities after the scattering that took place during World War II years. The nearly uniform growth during 1952 suggests that this war-time geographical disturbance of deposit holdings has been adjusted.

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Member Bank Earnings and Expenses

1952 was a year of all-time highs for Eighth District member banks in earnings . . .

INCOME of Eighth District member banks moved up in 1952 to the highest level in history. The growth in income resulted from enlarged resources and higher rates of return.

Resources continued to expand in 1952 and at the end of the year amounted to $6.3 billion. Compared with the $5.9 billion of total resources at the close of 1951, this was an increase of almost 6 per cent. In the use of these funds district member bankers followed rather closely the pattern of the previous year. They invested 38.8 per cent of total assets in United States Government securities and 7.3 per cent in other securities, the same percentages as in 1951. They made loans equalling 27.7 per cent of total assets, just a shade less than last year.[1]

In addition to enlarged resources, higher rates obtained on both investments and loans were an important factor in the increase in earnings. The average interest rate rose on Government securities from 1.79 per cent in 1951 to 1.92 per cent in 1952, on other securities from 2.49 per cent to 2.60 per cent, and on loans from 5.64 to 5.82 per cent.

The larger dollar volume of earning assets, coupled with higher rates of return, brought district member bankers the largest earnings of record, $153 million. This total topped by $16 million the previous high reached in 1951.

[1] Ratios used in this article are from the annual study of operating ratios made by this Bank. Asset and liability volumes used as bases or denominators in computing the ratios are averages of items reported in the December 31, 1951, June 30, 1952, and September 5, 1952, reports of condition. Earnings and expense items were for the calendar year 1952. Ratios are arithmetic averages of individual ratios of 489 member banks. Ratios computed in this way differ in some instances from ratios computed from aggregate dollar amounts. Averages of individual ratios are useful primarily to those interested in studying the financial results of operations of individual banks. Copies of the operating ratio report may be obtained from the Research Department of the Federal Reserve Bank of St. Louis.

. . . expenses, . . .

At the same time, rising operating costs pushed expenses to a new peak of $90 million in 1952, an increase of $9 million over the year before. Thus, over half of the $16 million gain in operating earnings went to pay mounting expenses.

Interest paid on time deposits during 1952 absorbed a larger percentage of earnings than in 1951, while salaries and other expenses accounted for a smaller share. The average interest rate paid to depositors of time money was increased from the .98 per cent paid in 1951 to 1.02 per cent.

. . . and net current earnings from operations.

As a result of the expansion of earnings and the lesser increase in expenses, net current earnings for 1952 also increased, reaching $63 million—the highest of record. Net current earnings represented 1.11 per cent of total assets of district member banks in 1952 compared with 1.06 per cent in the previous year. Measured against capital accounts these earnings were 15.7 per cent in 1952 and 15.0 per cent the year before.

Total incoming funds subject to disposition by bank management (net current earnings plus recoveries and reserve adjustments) reached $70.5 million.

Analysis of bank earnings and expenses over a year period is not complete with consideration of the factors affecting net current earnings alone. Certain charge-offs and recoveries, as well as additions to reserve accounts and withdrawals from previously established reserves, should be taken into account in determining the amount of funds that bank managements had at their disposal. A picture of the gross sources and uses of district member bank funds for the years 1949 through 1952 is presented in the table on the next page.

BANK MANAGEMENT OF NET CURRENT EARNINGS PLUS OTHER INCOMING FUNDS AND PREVIOUSLY SET-ASIDE RESERVES*

(Eighth District Member Banks)

	(Thousands of Dollars)	1949	1950	1951	1952
	Sources of Incoming Funds				
1.	Earnings	$113,500	$124,528	$137,126	$152,900
2.	Less Expenses	69,109	74,339	81,052	89,919
3.	Net Current Earnings	44,391	50,189	56,074	63,081
4.	Recoveries and Profits Credited to Income	5,160	4,374	3,601	3,255
5.	Recoveries Credited to Reserves	632	556	540	974
6.	Transfers from Reserves to Income (Release of reserves previously set aside to cover possible losses)	1,200	678	825	806
7.	Portion of Reserves called into Use during Year (Net reduction in previously set-aside reserves: line 10 minus line 5	1,217	979	2,271	2,444
8.	Total Incoming Funds	$ 52,600	$ 56,776	$ 63,311	$ 70,560
	Uses of Funds				
9.	Losses and Charge-offs Made against Income	$ 6,010	$ 5,103	$ 8,733	$ 9,446
10.	Losses Charged to Reserves	1,849	1,535	2,811	3,418
11.	Additions to Reserves from Income	6,755	5,484	5,202	4,928
12.	Additions to Capital Accounts	17,256	19,658	16,816	17,809
13.	Dividends	10,703	11,275	11,850	12,942
14.	Taxes on Net Income	10,027	13,721	17,899	22,017
15.	Total Uses of Funds	$ 52,600	$ 56,776	$ 63,311	$ 70,560

* Includes only reserves for bad debt losses on loans, and valuation reserves on loans and securities.

Item 3 of the table shows net current earnings, and items 4 through 7 the additional sources of income.

As indicated in items 4 and 5, profits and recoveries of previous losses and charge-offs were $4.2 million. Of this amount, $3.3 million was credited to income (item 4), and less than $1 million was credited directly to reserves (item 5). Transfers of $800,000 were made from reserves to income (item 6) and there was a net reduction in previously set-aside reserves of $2.4 million (item 7). With these additions incoming funds totaled $70.5 million in 1952, about 10 per cent more than in the year before.

Income taxes took the biggest share of these incoming funds.

Income taxes paid by district member banks took the biggest share of incoming funds in 1952. This was also true in 1951, but was not the case in prior years. In 1949 income taxes of $10 million (item 14) were smaller than the amounts of either dividends or additions to capital. In 1950 income taxes of $13.7 million exceeded dividends but were still less than the amount added to capital accounts. By 1951 income taxes of $17.9 million exceeded by $1 million the additions made to capital, surpassing by $6 million the amount of cash dividends. In 1952 the $22 million tax bill was $4.2 million more than the amount added to capital and $9.1 million above dividends.

When 1952 totals are compared with those of the prewar year of 1939, the increase in income taxes stands out even more. Additions to capital in 1952 were two and one-half times those of 1939, dividends were just over two times, but income taxes were more than ten times their prewar amount.

Stockholders received a lesser proportion . . .

There has been a steady though small decline in the percentage of total funds going to stockholders as cash dividends. In 1949 and 1950, cash dividends were 20 per cent of total incoming funds, in 1951 they were 19 per cent, and in 1952 they were 18 per cent. While dividends were losing ground percentagewise, they were increasing in dollar amount. Stockholders received $12.9 million in cash dividends in 1952, an increase of $1 million over 1951, and a gain of $2 million over 1949 (item 13). Dividends computed against total capital accounts reflected an earning rate of 3.0 per cent in 1952, down slightly from the 3.1 per cent in 1951.

. . . and a smaller amount remained to strengthen capital accounts.

As deposits increase, good banking practice requires that capital structures backing these deposits be increased also. Capital structures were increased in 1952 by $17.8 million (item 12). This amount just maintained relative proportions. Capital accounts were 7.3 per cent of total assets in both 1952 and 1951, and 8.0 per cent of total deposits in both years.

Losses and charge-offs were high in dollar amount.

Two other uses of funds are shown in the table, actual losses and charge-offs, and additions to reserves to cover potential bad debt losses. Actual losses and charge-offs are made against income or against previously established reserves. In 1952 district member banks charged the largest dollar volume of losses in the four-year period directly against income—$9.4 million (item 9). Losses charged against reserves were $3.4 million, also the highest in the period shown in the table (item 10).

As a protection against potential losses and for income tax purposes district member banks transferred $4.9 million to reserves (item 11).[1]

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[1] The building in reserves for potential losses has been most marked since the income tax law was clarified in 1947. Under the law banks are allowed for tax purposes to use an average experience factor for the determination of the ratio of losses to outstanding loans. The ratios of losses (or recoveries) for each of the last twenty years, including the taxable year, are averaged to obtain the experience factor. The percentage so obtained, applied to loans outstanding at the close of the taxable year, determines the amount which may be taken as a deduction in the bank's income tax return for that year. Continued deductions from taxable income will be allowed only in such amounts as will bring the accumulated total of the reserve account at the close of any taxable year to an amount not exceeding three times the moving average loss-ratio applied to outstanding loans.

For all member banks in the Eighth District the twenty-year average loss-ratio (1931-1950, the latest dates for which all-bank experience is available) was 0.51 per cent of outstanding loans. On this basis and excluding certain recovery credits, the maximum amount of reserves that district banks could carry would be 1.53 per cent (three times 0.51 per cent) of outstanding loans. This percentage is larger than the loss-ratio in 18 of the 20 years. In 1933 the ratio was 3.17 per cent and in 1934 it was 2.60 per cent.