

BANK CAPITAL AND DEPOSIT PROTECTION

Bank earnings are now relatively high and promise to be even higher in the future. Since dividend disbursements have been held relatively constant there has been a sizeable expansion of bank capital in the last few years. The growth of bank deposits, however, has been so much more rapid that the traditional capital-deposit ratio has fallen steadily. There are those who argue that present high bank earnings or even larger ones are needed to buttress the falling capital-deposit ratio.

This conclusion does not necessarily follow. The capital-deposit ratio is no longer a dependable measure of the need for bank capital in view of the large growth of riskless bank assets, cash and U. S. Government securities. Capital is needed by banks to absorb the market losses taken on assets when they are converted into cash to meet sudden deposit shifts or the losses on loans and investments which go sour and are collected only in part or not at all.

On the basis of real banking risks, the capital position of the banking system is now probably better off than ever before. In the following table there is presented a capital-risk ratio which compares net capital (i.e., after deduction of banking house, furniture and fixtures, and other real estate) with deposits after deduction of cash and U. S. Government securities. This ratio is an approximation of real banking risk. For comparative purposes, the conventional capital-deposit ratio is also shown below:

All Commercial Banks

	Adjusted Capital-risk ratio	Conventional Capital-deposit ratio
1914	28.6	23.3
1921	21.0	17.8
1929	19.4	18.0
1934	29.5	17.8
1939	28.9	12.8
1943	35.7	7.3
1944 (est.)	37½	6½

Even this calculation does not measure fully the improvement in bank capital protection. Bank loans and holdings of non-U. S. Government securities have never before been of as high quality or as liquid as now.

Under existing circumstances banks have adequate capital to fulfill their function in the financial community without jeopardizing the position of depositors.