

# Bank Capital in Italy

(The Impact of Inflation and Current Prospects)

by  
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1. — This paper is not concerned with the two preliminary questions relating to bank capital:

- a) the necessity and functions of bank capital;
- b) the advisability of State regulation.

Both the above problems have been thoroughly examined in banking doctrine and a fairly general agreement has been reached along the following lines:

a) a bank must have a capital of its own — even if the low ratio of its net worth to outside funds is a typical feature distinguishing it from other economic enterprises — not only to start business (« promotional » function), but above all to ensure (except in the case of a general depression) the capacity of absorbing extraordinary losses (1), in the direct interest of depositors (« guarantee » function).

b) In order to afford a proper degree of protection to depositors, the fixing of a bank's capital requires the intervention of a public supervisory authority. There is ample reason to believe that the composition of contrasting interests between bank « owners » and depositors cannot be left to market forces. In fact, « owners » are anxious to keep capital accounts at the lowest possible level so as to increase their profit rate, while depositors are interested in there being a large and adequate capital capable of meeting possible risks. Since, generally

(1) As is known, the process of the formation of bank income enlists among costs: insolvencies, the depreciation of any kind or form of assets, losses due to fluctuations in Stock Exchange quotations and exchange rates. These losses are considered part of ordinary business risks and should be sufficiently covered by current receipts. Consequently, the capital should only be required to cover:

- unpredictable and extraordinary risks;
- losses ordinarily experienced in day-to-day banking operations, when market conditions do not allow receipts sufficient to absorb them;
- losses due to liquidation sales, when a bank is being wound up and operating proceeds are no longer available.

On the other hand, when a general depression, whether national or international, occurs, the solvency of banks ceases as a rule to be a problem of « capital » and becomes a problem of « liquidity », the solution of which depends essentially on the action taken by the central monetary authorities,

speaking, the size of the capital is one of the elements on which the public's confidence in banks is based, one might assume that free competition should lead to balance « at a point in which capital would find a sufficient yield — as compared with the yield of any other form of investment — and creditors a sufficient guarantee » (2); but, as a matter of fact, market imperfections and the peculiarities of bank business might lead to very different results, to the detriment of depositors' claims. In particular, « it is not possible to neglect the fact that savers are nearly always incapable of assessing and estimating the relevant elements ... when facing the problem of deciding which bank to entrust their savings to; furthermore it is not difficult for bankers to find suitable substitutes for capital to offer to more or less gullible depositors » (3). Now, among the factors which, over and above capital, are likely to attract the public there is the volume of deposits; and this, in turn, is influenced by the credit policy carried out by the banks themselves. This process, as is well-known, enables credit Institutes, unlike all other economic enterprises, to increase their resources regardless of the amount of their net worth; and it is likely that the banks will be particularly inclined to avail themselves of this possibility during periods of business expansion and to postpone capital adjustments. For, while deposit expansion entails only a negligible increase in expenses, capital increases — quite apart from the charges involved — are usually beset with a number of difficulties both for State-owned banks and for private banks. The former are subject to the financial possibilities of the Treasury or to the accumulation of profits; the shares of the latter are usually less popular owing to their limited circulation, their comparatively low yield and the absence of opportunities for windfall profits. This is, in actual fact, the situation prevailing until recently in Italy, where the divergencies in average

(2) M. MAZZANTINI, *Trattato di tecnica bancaria*, Milan, 1940, p. 802.

(3) *Ibidem*, p. 803.

yield between bank shares and industrial shares are shown in *Table I*.

In the framework of these basic assumptions, our enquiry aims at discussing certain problems regarding a) the principles to be adopted in establishing

to establish simple and clear-cut principles so as to ensure the same standard for all banks, in actual fact considerable difficulties are encountered, both regarding the choice of the basis ratio and the modalities of enforcement, difficulties which it might be impossi-

PROFITS AND DIVIDENDS: COMPARISONS BETWEEN INDUSTRIAL AND BANKING CONCERNS TABLE I

Year	Number of firms		Paid-up capital and reserve funds (a) (millions of lire)		Profits (per cent)		Dividends (per cent)		Percent ratios of dividends to profits	
	Industrial	Banking	Industrial	Banking	Industrial	Banking	Industrial	Banking	Industrial	Banking
1938	1,138	66	33,164	3,082.70	7.56	5.09	6.22	3.33	82.32	65.13
1946	1,354	75	81,671	5,529.19	8.08	6.35	4.79	2.31	59.27	36.39
1947	1,515	80	172,743	8,770.21	10.13	6.18	7.00	2.47	69.19	37.40
1948	1,628	85	426,669	10,690.55	8.29	10.02	6.39	4.45	77.32	43.88

(a) The funds for monetary adjustment are included. End of year.

Source: *Notizie statistiche sulle Società Italiane per Azioni, 1949*, issued by the « Associazione tra le Società Italiane per Azioni ».

the size of bank capital, and b) the present capital structure of Italian banks and its practical implications.

## 1. - Capital-Deposit or Capital-Asset Ratio.

2. — As is known, current regulations concerning the size of bank capital generally vary according to whether they refer to the foundation or to the subsequent activity of a Bank.

Generally speaking, for the establishment of a new bank the presence of a certain capital is required. This initial minimum has necessarily to be fixed on the basis of factors quite extraneous to the future enterprise's activity; sometimes (as is today the case in Italy) they are left to the appraisal of the supervisory authorities in each separate case (4); sometimes reference is made to the population of the country or to the juridical form of the enterprise or to the territorial extension of its activity, etc.

Once the Bank has started operating, the adequacy of its capital to act as a guarantee should be proportionate to the expansion of its activity and, for this purpose, further and different control measures should be introduced. But, although it would seem advisable

(4) For the evolution of Italian legislative control (banking laws of 1926 and 1936) and for comparisons between the regulations in different countries, see: A. RENZI, *Difesa del risparmio ed esercizio del credito in regime corporativo*, Padua 1938; A. M. ALLEN and other Authors, *Commercial Banking Legislation and Control*, McMillan, London, 1939.

ble to overcome in periods of rapid economic dynamism. Hence it may become advisable or even necessary to waive precise formulas, preferring a flexible control and the pressure brought to bear by the supervisory authority.

3. — Regarding the selection of the term with which bank capital may be compared, there has been and still is a considerable divergency of opinions.

a) One line of thought, which in the past prevailed also in the United States, holds that capital should be in proportion to the total deposits and current accounts; and this as a consequence of the obvious relation existing between the risks inherent to credit operations and the total amount of alien funds.

b) A second line of thought — now strongly supported in the United States — considers total assets as the most reasonable basis for establishing the ratio of bank capital.

Undoubtedly the capital - total asset ratio presents an abstractly « logical » foundation, inasmuch as it refers the capital directly to credit items, including « loans and investments », the deterioration of which (owing to losses, devaluation, etc.) the capital is directed to absorb. However, in actual fact this abstract « logical » validity becomes irrelevant: on the one hand, total deposits differ from total assets according to rather homogeneous percentages; on the other hand, owing to the intrinsic characteristics of the assets, it

conceals incongruities and drawbacks not easily overcome.

Firstly, it should be remarked that the commonly accepted meaning of capital is an ideal, abstract accountancy value resulting from the algebraic total of assets and liabilities. Therefore, in an operating enterprise, its size is a function of the assessment criteria adopted to determine assets and liabilities. In particular, it is subject to asset evaluation since bank liabilities are easily ascertained. As there is a close connection between the evaluation of total assets and the size of capital, the latter has no value of its own that may be compared with the value of the assets.

Further, two other difficulties are to be considered: — some of the component parts of total assets, lacking a market value, have only nominal values; — the degree of risk varies considerably in the case of the majority of the credit items.

Consequently an unavoidable lack of precision and arbitrariness arises, which excludes a right of priority to total assets as a basis for establishing the size of bank capital.

The foregoing objections could not be overcome even if the ratios were calculated on the basis of assets exclusive of cash and investments in State securities (*i. e.*, limited to the so-called « risk assets »).

c) In order to give « real » meaning to the logicalness of the capital-asset ratio, the suggestion has been put forward in the United States to divide assets into groups with varying degrees of risk and to establish different capital (5) requirements for each group. This discriminating capital-asset ratio would overcome the drawbacks of which the capital-deposit ratio is accused, drawbacks which may be summed up as follows:

— in its uniformity, the capital-deposit ratio, although it is meant to cover any losses occurring in credit operations, does not make any allowance for the varying degrees of risk attending the different types of operation;

— it neglects the differences which may exist in asset structure from one bank to another and consequently applies the same standard to all enterprises, regardless of their business conduct;

— it ignores the changes which may occur in the pattern of bank assets in the course of time, modifying the estimate of the « adequacy » of capital as a guarantee.

Although the « logical » superiority of a multiple capital-asset ratio is undeniable, there are however serious reasons preventing it from being practicable.

(5) Some specify: « available » capital, that is to say capital account (capital+reserves and undistributed profits) less investments in immovable property (real estate, banking house fixtures, etc.).

Firstly, situations may develop which call for rapid changes in the composition of assets; in this case the adjustment of the several asset ratios might give rise to difficult problems or might even compel the banks to oppose legitimate business developments.

But, above all, the fact of establishing ratios for the different groups of assets would involve a complicated classification as regards the creation of homogeneous groups with respect to the degree of risk. Owing to the range of bank operations, no objective degree of risk can be applied to individual groups of credit operations, except in the case of cash assets and State securities. Very often, moreover, there is a considerable difference in risk between one operation and another within the same category — a difference which may actually be greater than the difference between one category and another.

To sum up, it appears that the traditional ratio of capital to total deposits is the most reasonable and simple in practice and not *a priori* surpassed as some American writers would contend (6).

It is based on a reliable and easily determined factor: the bank's liabilities, the amount of which may easily be ascertained and is not subject to evaluation principles of a subjective nature, so that it is possible to establish an amount of capital in keeping with the bank's debts and consequently with its credit capacity and presumable volume of risks.

## II. - The « Traditional » Capital-Deposit Ratio (1 to 10) and the Necessity of Adequate Remuneration for Bank Capital.

4. — As already stated, the adjustment of capital to deposits prevailed for a long time in practice as well as in theory and even now, despite the unavoidable arbitrariness involved, it may be satisfactorily applied as an empirical and general device to be adopted with suitable qualifications according to the different bank managements.

The best known of these ratios — it may be termed « traditional » since it represented the index of broad approximation for advanced banking systems in the first decades of our century — was the one

(6) For an extensive survey on this subject and for information regarding the tendency of the American supervisory authorities to replace the traditional ratio based on the volume of deposits with new systems referring to credit activity, see R. L. ROBINSON, *The Capital-Deposit Ratio in Banking Supervision*, in « The Journal of Political Economy », Feb. 1941; T. SMITH and R. E. HENGBEN, *Bank Capital: the Problem Restated*, in the same « Journal », Nov. 1947; R. L. ROBINSON, *A New Supervisory View of Bank Capital*, in « The Journal of Finance », March 1950.

which considered the necessary and sufficient amount of capital to be about one tenth of total deposits.

This amount — which referred to a period in which the capital of banks was well above this minimum — was actually contemplated by the articles of association of some banks (7), sanctioned by banking laws or recommended by the supervisory authorities (8) and also in Italy it was proposed with variations in some Bills referring to credit control (9).

As we shall specify later on, the ratio of 1 to 10 is now a memory of the past, except in a few countries (Switzerland and, to some extent, the United States). The expansion of currency circulation and inflationary developments in the last ten years have led to a great

broadly speaking, to the normal rate for investments on the market. Consequently the adjustment of bank capital to the expansion of deposits finds a natural obstacle in the level of bank capital yield: the faster the expansion of total deposits and the more limited the profits of bank business, the greater is the obstacle.

These conditions occurred in Italy during the past ten years of inflationary developments.

5. — On this aspect some statistical data may be interesting so as to bring up to date the calculations made by Prof. Mazzantini (10). The latter remarked that, between the first world war and the great depression, a ratio of about 1:10 between capital accounts and

PROFITS OF PUBLIC LAW CREDIT INSTITUTES AND BANKS OF NATIONAL INTEREST  
(millions of lire)

TABLE II

Year	Capital and reserves	Administered funds (a)	Net profit	Net profit, as a percentage		Ratio of capital accounts to liabilities	
				of capital accounts	of administered funds	%	Capital = 1
1938	3,582	35,924.92	200.75	5.60	0.558	11.07	9.03
1939	3,649	39,824.16	207.87	5.69	0.549	10.08	9.92
1940	4,082	46,929.40	221.19	5.41	0.509	9.52	10.50
1941	4,175	60,871.16	242.12	5.80	0.449	7.36	13.58
1942	4,377	74,882.69	262.27	5.99	0.386	6.20	16.14
1943	4,402	93,314.50	200.02	4.54	0.237	4.89	20.45
1944	4,491	175,065.49	172.65	3.84	0.128	2.63	38.02
1945	4,810	256,804.34	156.92	3.26	0.072	1.91	52.36
1946	5,557	471,317.30	174.08	3.13	0.048	1.19	84.03
1947	5,848	753,403.44	292.98	5.01	0.047	0.78	128.20
1948	6,422	1,096,101.11	650.60	10.13	0.073	0.58	172.41
1949	12,728	1,192,658.00	1,304.50	10.25	0.114	1.08	92.59

(a) Includes: paid-up capital, reserve funds, deposits and current accounts, circular cheques and sundry creditors.  
Source: *Notizie Statistiche sulle Società Italiane per Azioni*, 1949

divergency between the growth of bank deposits and the increase of bank capital, resulting sometimes (in Italy for instance) in a capital-deposit ratio much below 1:10. For a thorough appraisal, and a partial justification, of this trend, two sets of circumstances must be taken into account:

a) the complex variety of controls introduced during the last twenty years and the growing importance of public investments in bank assets have provided guarantee factors making up for and rendering acceptable considerably lower capital-deposit ratios;

b) further, as already stated, a ratio between capital and liabilities cannot ignore the necessity of ensuring a remuneration of bank capital corresponding,

(7) See MAZZANTINI, *op. cit.*, p. 804.

(8) See the articles already quoted in « The Journal of Political Economy », Feb. 1941 and Nov. 1947.

(9) See « Rapporto della Commissione economica presentato all'Assemblea Costituente »; Vol. IV, *Credito e Assicurazione*, p. 5, Rome, 1946.

the funds administered (including not only deposits and current accounts, but also net worth, circular cheques and sundry creditors) allowed a more than sufficient yield to paid-up capital (11). In fact, net profit fluctuated around 10-12 per cent per annum. The world crisis impaired this yield very considerably.

Continuing these calculations for the years after 1937, and until 1949, for « public law credit institutes » and « banks of national interest » on the one hand (Table II), and credit companies including « banks of national interest » on the other (Table III), we observe in contrast:

— a stationary average percentual yield during the first years of the war and its decline between 1942 and 1946;

— an uninterrupted lowering in the average ratio

(10) *Op. cit.*, p. 803 ff.

(11) As a general practice of Italian banks, « subscribed capital » and « paid-up capital » coincide.

between capital accounts and liabilities: from about 1:10 in 1938 to 1:20 in 1943 and 1:172 in 1948.

It may be inferred that the traditional ratio of 10 per cent showed a tendency to shift radically also because, under the conditions in which banking operations

seven-tenths. Once the reserve fund reached one tenth of total deposits, the aforesaid institutions were allowed to allocate a maximum of five-tenths of their net profits to charity and public utility purposes.

A real capital-deposit ratio, however, was only

PROFITS IN BANKING COMPANIES  
(millions of lire)

TABLE III

Year	Number of firms	Capital and reserves	Administered funds (a)	Net profit	Net profit, as a percentage		Ratio of capital accounts to liabilities	
					of capital accounts	of administered funds	%	Capital = 1
1938	66	3,082.70	30,873.57	157.13	5.09	0.51	11.09	9.02
1946	75	3,529.19	451,615.50	351.27	6.35	0.07	1.24	80.64
1947	80	8,870.21	670,046.40	548.00	6.18	0.09	1.34	74.62
1948	85	10,690.55	992,494.68	1,071.55	10.02	0.12	1.09	91.74

(a) Includes: paid-up capital, reserve funds, deposits and current accounts, circular cheques and sundry creditors.  
Source: *Notizie Statistiche sulle Società Italiane per Azioni*, 1949.

rations are performed today, it does not guarantee a « fair » remuneration for the capital invested, owing to the constant increase in bank costs (12).

### III. - Capital-Deposit Ratio in Law and Practice.

6. — The problem of a minimum initial capital will not be discussed in this paper; it has been suitably solved in Italy by granting the supervisory authority full power to take flexible decisions case by case according to circumstances (Art. 28 of the Banking Law 1936-37). Far more interesting and delicate is the problem of the capital-deposit ratio for operating enterprises. We will turn our attention to it, examining present Italian legislation and the changes which have occurred in the actual ratio for the whole Italian banking system as well as for the different groups of banks, posting up to date some international comparisons and discussing briefly the possibilities and the means for strengthening bank capital in our country.

7. — The first provision regarding the capital-deposit ratio in Italy is to be found in a law of 1888 on Saving Banks, which established that nine-tenths of the yearly net profit were to be set aside to form a reserve fund until the latter amounted to one tenth of total deposits. Subsequently, in 1929, Savings Banks and Pledge Banks were allowed to reduce the quota to be earmarked for the formation of a reserve fund to

(12) On the problem of bank costs in Italy, see: M. MAZZANTINI, *I costi di gestione delle banche italiane*, in « Moneta e Credito », edited by the Banca Nazionale del Lavoro, No. 7, 3rd quarter, 1949, pag. 288 ff.

enacted in 1926. On the basis of Art. 15 of Decree-Law No. 1830 of November 6, 1926, the ratio of bank deposits to capital plus reserves was not to exceed 20 to 1. Any amount in excess of this was to be invested in Government bonds or deposited or placed in a non-interest bearing current account with the Bank of Italy. This « legal » ratio of 1:20 was at that time — and remained until the second world war — far lower than the actual ratios of Italian banks which were generally about 1:10.

The 1936-7 Banking Law — recognizing the arbitrary nature of any inflexible and aprioristic formula, in view of the different banking managements and changing market conditions — refrained from formally enacting fixed ratios and preferred to grant the supervisory authorities power « to impart instructions of a general nature to banks or of a particular nature to groups of banks or to single banks, amendable after suitable notice » with regard to « the ratio between net worth and liabilities, and the possible types of investment authorized for such deposits as exceed the amount established by said ratio » (Arts. 32 and 33 (13)).

Nevertheless the ratio established by the 1926 Law was maintained as a standard by the supervisory authorities until 1945.

The « nominal » increase which had meanwhile taken place in the volume of deposits as a result of inflation — unaccompanied by even a nominal adjustment of bank capital — then made it imperative to change the ratio so as to ensure a suitable yield to the banks which were heavily burdened by increased

(13) The supervisory authorities have also the power to « regulate the ratio between bank capital and investments in real estate or industrial shares » (Art. 35).

operating costs. Consequently, as from March 1, 1946, the supervisory authority provided that capital accounts (capital and reserve funds) could not be less than one thirtieth of total deposits and that banks holding deposits equivalent to more than thirty times their capital accounts were to invest the surplus in State or State-guaranteed securities to be deposited with the Bank of

This measure was a temporary makeshift at a time when monetary devaluation reacted unfavourably on the yield of banking enterprises and the formation of savings. It was not implemented and had therefore to be abandoned.

Eventually the matter was regulated *ex novo* by the provision of July 17, 1947, wherein the Intermini-

DEPOSITS AND CURRENT ACCOUNTS IN ITALY, BY GROUPS OF BANKS (a)  
(millions of lire)

TABLE IV

End of year	Public Law Credit Institutes	Banks of National Interest	Ordinary Credit Banks	People's Co-operative Banks	Savings Banks and Pledge Banks of 1st category	Total
1938	8,843	13,888	8,163	5,722	18,916	55,532
1939	10,437	15,994	9,699	5,924	18,912	60,966
1940	14,701	19,251	11,543	7,210	19,753	72,458
1941	19,550	24,626	15,968	9,478	24,012	93,634
1942	24,701	29,622	21,500	12,840	29,283	117,946
1943	26,880	40,337	26,745	16,617	32,679	143,258
1944	56,648	73,562	45,175	27,122	46,278	248,785
1945	84,081	108,763	86,020	46,455	81,267	406,586
1946	142,540	192,063	154,783	78,500	130,169	698,055
1947	225,070	244,486	226,719	114,291	203,323	1,013,889
1948	333,333	364,717	328,249	169,279	324,700	1,520,278
1949	448,286	446,101	424,310	214,125	415,902	1,948,724
1950	518,506	517,089	487,033	238,400	473,878	2,234,906

(a) Interbank current accounts are excluded. The data refer to 365 banks (commercial and savings banks) which hold about 99% of the total deposits collected by all Italian banks.

Source: *Bollettino* of the Bank of Italy.

Italy or pay it into an interest-bearing current account also with the Bank of Italy (within six months from the ascertainment of the surplus).

TABLE V

NET WORTH OF ITALIAN BANKS (a)  
(millions of lire)

End of Year	Public Law Credit Institutes	Banks of National Interest	Ordinary Credit Banks	People's Co-operative Banks	Savings Banks and Pledge Banks of 1st category	Total
1938	1871	1711	1581	599	1582	7,344
1939	1930	1719	1574	592	1691	7,506
1940	2254	1828	1677	664	1716	8,139
1941	2329	1846	1745	716	1796	8,432
1942	2518	1859	2041	741	1947	9,106
1943	2530	1872	2148	927	2073	9,550
1944	2610	1881	2261	1080	2256	10,088
1945	2916	1894	2434	1217	2415	10,876
1946	3632	1925	3909	1748	2541	13,755
1947	3833	2015	6885	3123	2910	18,766
1948	4347	2075	8630	3901	3802	22,755
1949	6378	6350	13590	5567	5258	37,143
1950	9331	6625	17190	6666	6958	46,770

(a) « Net worth » includes capital and reserve funds.

Source: *Bollettino* of the Bank of Italy.

sterial Credit Committee introduced, as an anti-inflationary weapon, a system of compulsory reserves.

Banks other than Savings Banks had to deposit with the Bank of Italy, either in the form of cash or of Government Securities, 20% of such part of their deposits and current accounts as exceeded ten times their capital accounts (capital and reserve funds) at September 30, 1947 as well as 40% of any increase in deposits occurring after September 30, 1947 until the total ratio between « reserves » and alien funds reached 25%.

Although this provision has deprived banks of the possibility of granting credit to economy in proportion to the whole of the increase in the deposits, it has, on the other hand, strengthened the guarantee for depositors as far as liquidity and solvency are concerned making up for the heavy drop in the capital-deposit ratio.

8. — Tables IV-VII contain data regarding the increases which occurred between 1938 and 1950 in the face value of deposits and current accounts and in the capital accounts of the Italian banking system. According to the index numbers in Table VI deposits

and current accounts increased 40 times (14) between December 1938 and December 1950 as against an increase of only about six times for total capital accounts. The capital-deposit ratio consequently underwent considerable changes, declining from about 1:8 in 1938 to 1:15 in 1943 and 1:66 in 1948; the situation improved appreciably in 1949 and 1950 (1:48 in December 1950), but there is still a very marked divergency as compared with 1938. In actual fact the total capital accounts of the Italian banking system at present amount to 2 per cent of total deposits and current accounts, as against 13 per cent in 1938.

TABLE VI

RATIO OF NET WORTH TO DEPOSITS  
IN ITALIAN BANKING SYSTEM

End of year	Indexes (1938=100)		% ratio of net worth to deposits
	deposits and current accounts (a)	net worth (b)	
1938	100	100	13.22
1939	109	102	12.31
1940	130	110	11.23
1941	169	114	9.00
1942	212	124	7.72
1943	258	130	6.66
1944	448	137	4.05
1945	732	148	2.67
1946	1,257	187	1.97
1947	1,825	255	1.84
1948	2,737	309	1.49
1949	3,509	505	1.90
1950	4,021	637	2.09

(a) Interbank current accounts are excluded.

(b) « Net worth » includes capital and reserve funds.

The drop in the capital ratio differs from one group of banks to another, owing to the different rate of deposit expansion and to the different managerial conduct adopted to adjust capital to the new conditions.

As Table VII shows, the highest capital ratio is at present that of « ordinary credit banks » and of « people's cooperative banks », for which the respective ratio are 3.52 and 2.79 per cent of deposits and current accounts, while the « banks of national interest » show the lowest percentage of the whole credit system, namely 1.28 per cent. Between the two extremes there are the savings banks and « public law credit institutes ».

The fact that « ordinary credit banks » and « people's cooperative banks » have maintained the

(14) As is known, this increase is considerably lower than the increase in wholesale prices (54 times); hence the increase in « monetary » terms conceals a drop of about 32 per cent in the « real » value of total deposits and current accounts.

TABLE VII  
PERCENT RATIOS OF NET WORTH TO DEPOSITS  
BY GROUPS OF ITALIAN BANKS (a)

End of Year	Public Law Credit Institutes	Banks of National Interest	Ordinary Credit Banks	People's Co-operative Banks	Savings Banks and Pledge Banks of 1st category
1938	21.15	12.32	19.36	10.47	8.36
1939	18.49	10.74	16.23	10.00	8.94
1940	15.33	9.49	14.53	9.21	8.68
1941	11.01	7.49	10.93	7.55	7.48
1942	10.19	6.27	9.49	5.77	6.65
1943	9.41	4.64	8.03	5.58	6.34
1944	4.60	2.55	5.00	3.98	4.87
1945	3.46	1.74	2.83	2.62	2.97
1946	2.54	1.00	2.52	2.22	1.95
1947	1.70	0.82	3.03	2.73	1.43
1948	1.30	0.57	2.63	2.30	1.17
1949	1.42	1.42	3.20	2.60	1.26
1950	1.80	1.28	3.52	2.79	1.46

(a) « Net worth » includes capital and reserve funds. The term « deposits » includes deposits and current accounts. Interbank current accounts are excluded.

highest ratio is accounted for partly by the larger flow of deposits to « public law credit institutes » and « banks of national interest », and partly by the juridical nature of « ordinary banks » and « people's cooperative banks », whose private character has enabled or even obliged them to increase their capital, not only by converting hidden into manifest reserves, but also by resorting to the money market and to revaluation for monetary adjustment — measures which were not accessible to the « public law credit institutes » owing to their juridical nature, or to the « banks of national interest » owing to the difficult financial situation of I. R. I. (Istituto per la Ricostruzione Industriale - Industrial Recovery Institute) which holds the of their shares (15).

9. — It is not only during the last ten years that there has been a decline in the capital-deposit ratio. Inflationary movements have always been accompanied by a marked downward trend of the capital ratio (16).

(15) It must be remembered that also the capital-deposit ratios for each of the above-mentioned banking groups are only general averages, often concealing wide divergencies from one enterprise to another within the same group. Even for one and the same enterprise, the capital-deposit ratio may be misleading inasmuch as the capital accounts are the result of asset values depending on subjective appraisals and divergent business policies; consequently they acquire a real meaning only if they are considered in the light of the management's practices (provision of sinking funds for real estate and banking house fixtures, under-valuation of investment portfolios, writing-down of doubtful credits, etc.).

(16) See MAZZANTINI, *op. cit.*, p. 807; and the article *Zum Kapitel « Bank Kapital »* in « Zeitschrift für das gesamte Kreditwesen », Feb. 1950.

As compared with deposits and current accounts, the percentual capital ratio of Italian banks actually declined from 22.3 to 8 per cent between 1913 and 1921, rising to 13.3 per cent in 1926 (12% in 1937).

Nor is this only an Italian phenomenon. Also abroad the decline in the capital ratio, which had already started before World War II, increased considerably as a result of recent inflationary developments, dropping to levels never reached in the past. Table VIII is significant in this respect, since it sums up

DEPOSITS AND CURRENT ACCOUNTS, NET WORTH AND RELATED RATIOS  
IN AMERICAN, FRENCH, ENGLISH AND SWISS BANKS

TABLE VIII

GREAT BRITAIN: « BIG FIVE » (a)  
(millions of sterling)

End of period	Deposits and current accounts	Net worth	% Ratio
1938	1,950.09	116.11	5.95
1947	5,147.00	125.30	2.43
1948	5,354.00	128.3	2.40
1949	5,336.00	128.8	2.41
1950	5,473.89	129.62	2.36

(a) Barclays Bank, Midland Bank, Lloyds Bank, Westminster Bank, National Provincial Bank.

Source: Balance-sheets.

UNITED STATES: « COMMERCIAL BANKS »  
(millions of dollars)

End of period	Deposits and current accounts	Net worth	% Ratio
1939	57,718	6,885	11.9
1945	150,227	8,950	6.0
1946	139,033	9,557	6.9
1947	144,103	10,059	7.0
1948	142,843	10,480	7.3
1949	145,174	10,967	7.6
1950	153,870	11,620	7.5

Source: Federal Reserve Bulletin.

10. — As has already been remarked, a justification for the changed pattern of the capital-deposit ratio may be found in the far-reaching innovations (changes in asset structures, public controls, etc.) introduced in most countries after the Great Depression of 1930-33, which led to a considerable increase in the guarantees afforded to depositors. This is the case also in Italy, particularly since 1947 when the system of compulsory reserves was added to the network of legal obligations already in force (control relating to the opening of

FRANCE: WHOLE BANKING SYSTEM  
(billions of francs)

End of period	Deposits and current accounts	Net worth	% Ratio
1938	54.5	10.7	19.63
1946	443.1	19.3	4.35
1947	516.2	22	4.26
1948	816.3	24.5	3
1949	986	35.1	3.50
1950	1,131.9	39.4	3.48

Source: Commission de Contrôle des Banques, *Rapports Annuels*.

SWITZERLAND: WHOLE BANKING SYSTEM  
(millions of francs)

End of period	Alien funds	Net worth	% Ratio
1939	15,195.6	2,119.8	13.9
1945	18,339.1	2,182.5	11.9
1946	19,820.6	2,209.7	11.1
1947	21,012.8	2,261.2	10.8
1948	21,920.9	2,306.5	10.5
1949	23,018.8	2,371.3	10.3

Source: *Das Schweizerische Bankwesen im Jahr 1949*, issued by Swiss National Bank.

the data for the four money markets of greatest international importance: U.S.A., Great Britain, France and Switzerland. In Great Britain the capital-deposit ratio has dropped to a level slightly higher than in Italy (from 6% to 2.40%); the French ratio is somewhat higher (3.50%, but with a maximum decline from 19.6%); the ratios for the U.S.A. (7.6%) and especially for Switzerland (10.30%) are still high, but there has been a considerable shrinkage as compared with 1938, which in the case of Switzerland is as high as 30%.

new banks or banking branches, elimination of participations and medium and long term loans, credit control, etc.). In this legal framework, a policy aiming at guaranteeing bank creditors' claims by an increase in bank capital might to some extent at least, be substituted by an active manipulation of the complex variety of control weapons the monetary authorities now have at their disposal.

In any case, the process of strengthening bank capital has been under way since 1948 and, quite apart from the above-mentioned « compensatory » control

measures, should be pursued tenaciously beyond the modest level so far attained. Until what new ratios are reached? The answer — obviously only a broadly approximate one — involves a knowledge of the present revaluation possibilities for monetary adjustment. We will now examine this aspect.

#### IV. - Revaluation for Monetary Adjustment and Bank Capital Increases between 1946 and 1950.

11. — In recent years the problem of revaluation (17) for monetary adjustment has been of particular interest to non-financial business enterprises which, operating as they do on real goods in which almost all their capital is invested, have not suffered any substantial loss as a result of inflationary developments.

On the other hand, this problem is not of great importance for banks owing to the different structure of bank assets, which consist for the most part of monetary values and only for a small fraction of values incorporated in real property (real estate, furniture and equipment).

In fact, if we consider the distribution of bank assets we see that:

— for a first group of assets (cash, portfolio, discounts, advances, contangoes, letters of credit, etc.), which absorb most of a bank's resources, no problem of revaluation arises;

— for a second group (State securities, corporate debentures and shares), revaluation is equally impossible, since, while the accountancy value of some investments (State securities) remains unchanged, in the case of others (shares) stock exchange quotations already discount monetary devaluation. There is, however, a possibility of revaluation in the case both of the share portfolio and of industrial participations purchased in periods of currency stability, provided these securities are still entered at « face » value in the bank balance-sheets;

— it is for a third group of assets, consisting of immovable property and equipment, that revaluation can be of interest. Only a part of these assets are entered in bank balance-sheets in view of the usage of considering as operating expenses all payments made for the purchase of furniture and equipment and

(17) As is known, revaluation for monetary adjustment is regulated by Act No. 436 of May 27, 1946; Act No. 241 of Sept. 13, 1946; Act No. 49 of Feb. 14, 1948 and Act No. 94 of April 1, 1949.

On the problem of legal coefficients for monetary adjustment, see G. MANGINI, *Aspects and Problems of the Italian Stock Market*, in this Review, No. 5, April 1948, pag. 321 ff.

for works of adjustment and improvement to bank premises. Hence the existence of hidden reserves, the extent of which it is impossible for anyone outside the bank administrations to know — and the possibility of a revaluation, which, however, can never have the same importance as in the case of non-financial business enterprises.

The problem of the revaluation of these assets should be carefully studied by banks in an attempt to find a way of adjusting their capital to the new monetary standard and raising its ratio to the deposits and current accounts, with the threefold purpose: (a) of reducing the amount of the deposits to be tied up as compulsory reserves in State securities or current accounts with the Bank of Italy; (b) of increasing the line of credit that may be granted to a single enterprise (18); (c) of reducing the amount of the securities to be deposited with the Bank of Italy against the outstanding volume of circular cheques (*assegni circolari*) (19).

12. — The process of strengthening bank capital, which was started in 1946, developed in 1947 as a result of: a) asset revaluation for monetary adjustment (in compliance with Act No. 436 of May 27, 1946); b) cash payments occurring in the case of « ordinary credit banks » and « cooperative banks »; c) allocation to reserve funds of current profits. In this manner the net worth of the banks as a whole rose from 7,344 millions in 1938 to over 18,700 millions at the end of 1947. The same trend continued in 1948 (from 18,766 to 22,755 million lire). But the greatest capital and reserve increase — 14,388 million lire — was in 1949. It occurred in all sectors of the Italian credit system, and in particular in that of « banks of national interest » and « ordinary credit banks » which were able to effect revaluation for monetary adjust-

(18) Under present regulations, a bank is allowed to grant to a client a line of credit up to and not exceeding 20% of the amount of bank capital. For grants above this ratio the authorization of the Bank of Italy is required.

(19) The « *assegno circolare* » is an instrument of credit payable to order issued by a bank against payment of the equivalent in cash. The bank is responsible for the payment of the « *assegno circolare* ». This is the difference with a common cheque: in fact a bank is under no obligation to cash a cheque if no funds are available in the drawer's account. Owing to the guarantee of the issuing bank, the « *assegno circolare* » is an instrument of payment quite generally accepted. It may be issued only by some authorized banks, after they have deposited a special reserve fund with the Bank of Italy for an amount equivalent to 40% of the average circulation of drafts during every two-month period. If at the end of the period the circulation exceeds the « capital accounts » of the issuing bank, an additional « cover » must be deposited for an amount equivalent to 100% of the surplus (at present this reserve is only 60% of the surplus as compared with the amount which was in circulation at September 30, 1947).

ment, availing themselves of the provisions issued in Act No. 49 of Feb. 14, 1948.

A further strengthening of bank net worth — by 9,627 million lire — especially pertaining to « public law credit institutes » and « ordinary banks » took place during 1950 due, for the amount of 3,032 million lire to the increase in capital and for the amount of 6,595 million lire to the increase in reserve funds.

On the whole, the contribution brought by revaluation for monetary adjustment to the capital funds of the Italian banking system in the period 1946-1950 has been calculated to amount to 3,337 million lire: only 10% of the total increase (33,015 million lire) in banks' net worth occurred in the last four years (See Table IX).

TABLE IX

REVALUATIONS FOR MONETARY ADJUSTMENT  
(millions of lire)

Year	Number of banks	Revalued Items			Assignment of revalued items to			Total
		Real property	Securities	Previous revaluations	Capital	Reserves	Other purposes	
1947	18	502	284	—	71	124	591	786
1948	10	311	273	—	214	340	30	584
1949	28	418	941	182	735	515	291	1,541
1950	22	1,662	534	191	764	574	1,049	2,387
Total	78	2,893	2,032	373	1,784	1,553	1,961	5,298

Source: Report for 1950 by the Bank of Italy.

In December 1950 the total capital accounts of the Italian banking system — 44,770 million lire — reached an average of barely 6.37 times the 1938 level, whereas deposits and current accounts had increased 40.2 times; the comparative rate of increase for capital and deposits differed widely from one group of banks to another:

Banking Institutions	Increases in capital accounts (1938=1)	Increases in deposits and current accounts (1938=1)
Public law credit institutes	5.55	58.6
Banks of national interest	3.87	37.2
Ordinary credit banks	10.87	59.6
People's cooperative banks	11.12	41.6
Savings banks and pledge banks . . . . .	4.39	25.1

In short, despite the efforts made by the banks, the results on the whole are modest so far. The low coefficients for monetary adjustment established by the

law (20) and their limited application have not permitted the full revaluation of bank assets, nor has the flow of fresh capital (and the ploughing back of profits) been proportionate to the steady increase in deposits.

#### V. - Revaluation Possibilities of Bank Capital.

13. — What results might be obtained with a full revaluation of bank assets?

As has already been said, the assets to be considered for this purpose are:

- the share portfolio;
- participations;
- premises;
- furniture and equipment.

Let us examine these items for the several banking groups.

##### 14. — Share Portfolio.

The share portfolio, consisting mainly of assets not in the nature of participations, followed the trend shown in Table X between 1938 and 1950 in the five sectors of the Italian banking system.

As can be seen, the total nominal value of banks' share holdings remained practically unchanged between 1938 and 1946, subsequently starting to rise, in conformity with the revaluation process for monetary adjustment, until in 1950 they reached 9 times the 1938 level. Now, if we consider that the market value of said shares was about twice their face value in 1938 and about three times at the end of 1950, after having exceeded 10 times in 1947-48, it is permissible to assume that the share portfolio is not liable to appreciable revaluation. Undoubtedly the bank's share portfolios contain securities which, in view of the prudential standards of evaluation adopted, deserve to be revalued; but in any case these are values which, compared with total assets, are of little importance and would therefore give a very modest contribution.

##### 15. — Participations.

The Banking Law of 1936 forbade banks to have participations in commercial and industrial enterprises, so as to avoid risks of immobilization.

This ban, however, is not extended to some « public law credit institutes », which have continued to hold and acquire participations in some enterprises of an industrial nature or of public interest in Southern Italy. But, with this exception, all other banks now

(20) Maximum: 18 times the 1938 values, as against an increase of 54 times in wholesale prices (on Dec. 1950). Proposals for raising the revaluation coefficient now in force (to a maximum of 40 times?) are now pending in government circles.

possess only participations in other national or foreign credit Institutes.

The participations to be considered are therefore:

- a) bank participations;
- b) sundry participations;
- c) foreign participations.

Their trend during the past years is given, for the whole Italian banking system, in *Table X*. As can be seen, the most striking increases occurred in recent years; they may be attributed, at least partly, to the

TABLE X

SHARE PORTFOLIO, PARTICIPATIONS AND PREMISES  
OF ITALIAN BANKING SYSTEM  
(millions of lire)

End of year	Share portfolio (a)	Participations	Premises
1938	696	784	1,564
1939	603	761	1,509
1940	605	785	1,540
1941	613	1,644	1,497
1942	581	1,674	1,200
1943	795	1,797	1,544
1944	552	1,750	1,531
1945	507	1,797	1,664
1946	644	3,258	2,408
1947	1,374	4,145	3,963
1948	3,430	5,015	6,033
1949	5,288	7,445	8,979
1950	6,500	11,387	11,740

(a) Nominal value.

Source: *Bollettino* of the Bank of Italy.

capital increases carried out by controlled enterprises. The trend varied widely from one group of banks to another.

In the sector of « public law credit institutes » which, as we have seen, is the only one in which some banks hold industrial participations, a revaluation might be possible, particularly when the participations were acquired prior to the war and are still entered at their original values. It is impossible, however, to give reliable calculations on this matter, since it would be necessary to know the nature of each participation, the economic and capital situation of the enterprises controlled and their managements, etc.

As far as bank participations are concerned, revaluation may be considered in differing degrees, according to whether they refer to Italian or to foreign banks. We are of opinion that revaluation is not possible for the former since Italian banks, as we shall soon show, have no intrinsic revaluation possibilities with regard to their capital. For participations in foreign banks — which are still entered in the balance-

sheets of Italian banks at the old exchange rates — revaluation possibilities are greater owing to the changed rate of exchange, but not likely to be important.

16. — *Premises.*

The most suitable sector for full revaluation is that of banks' real estate — the item which has suffered least from the process of monetary devaluation. Revaluation possibilities are enhanced by the usage of considering all works of improvement, adjustment and embellishment as operating costs to be fully covered by current profits.

Limiting our considerations to the values indicated in bank balance-sheets, since it is obviously impossible to take hidden reserves into account, the immovable property of banks returned by the Bank of Italy followed the trend shown in *Table XII* between 1938 and today.

The increase recorded in recent years is mostly due to new purchases of immovable property, but for the two sectors of « ordinary credit banks » and « people's cooperative banks » it is partly due to revaluation for monetary adjustment carried out in compliance with the legal conversion coefficients.

Obviously the data given represent accountancy values which, as things are at present, owing to the changes in the purchasing power of money, do not give any precise indication of the real value of the banks' immovable property.

17. — A revaluation of bank premises might be carried out according to one or another of the following criteria, which lead to very different results:

a) a revaluation based on « legal coefficients » could only give very limited results. In fact, by revaluing the immovable property owned by Italian banks in 1920 (worth about 450 millions) and its subsequent increases up to September 1950 on the basis of the aforesaid coefficients (21), the following approximate credit balances are obtained:

(21) The coefficients for monetary revaluation calculated in compliance with legal provisions are the following:

Year 1920 - 36.3582544738	Year 1924 - 25.1626318632
» 1921 - 28.3411741626	» 1925 - 23.055065514
» 1922 - 27.3129568686	» 1926 - 22.3163343702
» 1923 - 26.5623917364	» 1927 - 29.509054848
from 1927 to October 1936 . . . 30.42	
from October 1936 to 1938 . . . 18	
Year 1939 . . . . . 15.66	
» 1940 . . . . . 13.50	
» 1941/42 . . . . . 11.34	
» 1943 . . . . . 9	
» 1944 . . . . . 6.75	average for investments North and South of the « Gothic Line »
» 1945 . . . . . 3.60	

Public law credit institutes . . .	12,015	millions
Banks of national interest . . .	9,663	»
Ordinary credit banks . . . . .	8,868	»
People's cooperative banks . . .	5,374	»
Savings banks and 1st cat. pledge banks . . . . .	10,644	»

Total . . . 46,564 millions

b) One might also conjecture a revaluation on the basis of the *general index numbers for wholesale prices* (at September 1950, 58.88 times the 1938 level).

Following this principle, the credit balances of revaluation would increase considerably, reaching the following amounts:

Public law credit institutes . . .	13,738	millions
Banks of national interest . . .	16,231	»
Ordinary credit banks . . . . .	19,589	»
People's cooperative banks . . .	9,260	»
Savings banks and pledge banks	20,759	»

Total . . . 79,577 millions

It should be remarked that, having taken the values of the 1938 balance-sheet set forth in *Table XII* as conversion basis in this case, we have not considered the revaluation indices for the years 1927 and 1936 and the process of amortization already under way in the preceding years, which might raise the figures we have obtained even higher.

c) Lastly, it is possible to conjecture a full revaluation on the basis of the *changes in the value of the lira resulting from*:

— the gold price between December 31, 1920 and December 21, 1927;

— the law relating to the stabilization of the lira (Act No. 2325 of December 21, 1927) for the period going from December 22, 1927 to October 4, 1936;

— the law relating to the « alignment » of the lira (Act No. 1745 of October 5, 1936) for the period going from October 5, 1936 to December 31, 1938;

— wholesale price indexes between January 1, 1939 and September 30, 1950.

If suitable computations were performed in compliance with the foregoing principles, the credit balances of revaluation might be the following:

Public law credit institutes . . .	36,749	millions
Banks of national interest . . .	28,018	»
Ordinary credit banks . . . . .	26,534	»
People's cooperative banks . . .	16,421	»
Savings banks and 1st cat. pledge banks . . . . .	31,998	»

Total . . . 139,720 millions

The conversion computations do not of course take into account certain phenomena of a truly economic nature reflecting the immovable property market and the process of amortization under way, which would probably modify the results we have obtained.

18. — *Furniture and Equipment.*

The praiseworthy administrative custom adopted by banks of considering purchases of furniture, calculating machines, mechanical equipment for accountancy, etc. as operating costs helps to form hidden reserves, the extent of which is unknown. But as said articles are subject to great wear and tear, the value of these reserves, as compared with total assets, could hardly be noteworthy. For this reason — quite apart from obvious principles of cautious management — they ought to be overlooked.

19. — *Hidden Reserves.*

The survey we have made so far of revaluable assets has not yet exhausted the possibilities of the reintegration of bank capital.

The integrity of the latter is further safeguarded by the formation of hidden reserves resulting from prudential evaluations of the several bank assets. But just because of their particular nature, it is not advisable to reveal them through revaluation. Moreover it would be a very difficult task to determine their extent, owing to the divergent evaluation principles — of a subjective nature — adopted by banks and their variability even within the same bank from one year to another. In any case, the possible margin of revaluation is necessarily low, as these reserves usually result from an under-estimation of security holdings, bearing for the most part a fixed income and having a market value about par.

Besides the case of reserves resulting from the under-estimation of asset items, mention must also be made of the hidden profits concealed among liability items. In the case of most banks, these too, however, are not of such magnitude as to render an equivalent and manifest revaluation of capital advisable.

VI. - *The Reconstitution of Staff Retirement Funds.*

20. — In order for the problem of the revaluation of bank capital to find a complete solution, not only the assets liable to monetary adjustment must be considered, but also the liabilities consisting of charges which have to be adjusted to the conditions existing at the moment of payment and which consequently are also affected by monetary vicissitudes.

Under this heading we find the indemnities due to bank employees when their employment comes to an

end, for the payment of which the banks have to constitute suitable retirement funds.

The formation of these funds without a corresponding investment in real estate — which was not allowed in the case of Italian banks — has had a detrimental effect on their real value. In fact, while the indemnities due to the staff have increased in proportion to the rise in salaries connected with inflationary developments, the value of the assets allocated has not followed the same trend owing to the fact that for their very nature they are not liable to revaluation for monetary adjustment. Consequently, as things are at present, the value of the retirement funds of the banking system as a whole is not in proportion to the amount of indemnities due to the staff on the basis of present salaries and seniority.

21. — Regarding the calculation of staff retirement funds, Prof. Saraceno remarked (22):

« supposing that each employee administers on an average a deposit quota equivalent to 15-20 times his yearly salary and taking the average seniority of the personnel to be 10-15 years, the staff retirement fund is equal to 3-5 per cent of the deposits ».

Following this principle and making allowance for the fact that the total amount of bank deposits is about 2,234 billion lire (Dec. 1950) it might be assumed that the staff liquidation fund for the whole Italian bank system should fluctuate between a minimum of 68 and a maximum of about 113 billion lire.

Perhaps this computation is optimistic. If, as it would appear, the number of bank employees amounts to 83,173 with an average seniority of from 5 to 10 years for one third, from 10 to 20 years for another third and over 20 years for the remainder and if the average retirement indemnity is at present about 1,500,000 lire per employee, the total volume of the retirement funds which should be indicated in the balance-sheets of Italian banks should be about 125 billion lire; instead bank returns showed a total of 24,611 million lire at December 31, 1950.

These figures, we repeat, are based mainly on suppositions and must therefore be considered only as broadly indicative. It is likely, however, that the Italian banking system as a whole would require further allocations not far from one hundred billion lire to reconstitute the retirement funds for the bank staff now in service. And, since, *rebus sic stantibus*, it would not be possible generally speaking, to cover this gap with current profits, any capital revaluation would have first of all to be allocated to this purpose.

Are the credit balances resulting from capital revaluation likely to be sufficient for the reconstitution

of staff retirement funds? The answer depends largely on the criteria followed in asset revaluation. If we assume that revaluation sources are provided exclusively by real estate items, the balances thus attainable would be completely absorbed by the reconstitution of staff retirement funds, should they be computed at a total amount of about 78 billion lire on the basis of the index number for wholesale prices (hypothesis b). On the other hand, in the case of a full revaluation such as was conjectured under hypothesis (c), a margin would very probably remain.

## VII. - Conclusions.

22. — If the latter alternative is excluded for reasons of extreme caution, one might affirm: a) that immovable property assets which may certainly be revalued are offset by liabilities which, adjusted to the present cost and the seniority of the staff, would probably absorb the whole of such revaluation balances; b) that bank capital, consequently, could not expect any conspicuous contribution from revaluation for monetary adjustment.

These remarks — which might be complicated by the previously mentioned divergencies in conditions between groups of banks and from one bank to another and the consequent necessity of adopting an appropriate minimum common denominator — show that any realistic possibility of rapid improvements in the present capital-deposit ratio is to be excluded. Therefore, the burden of strengthening capital accounts will fall largely on banks' current profits, which increased considerably in 1948, 1949 and 1950 and on which the capital adjustment efforts made by the banking system in recent years — with results that are favourable on the whole but vary from group to group and from bank to bank — were founded. It is undoubtedly necessary to persist in these efforts so as to attain capital endowments more in keeping with the importance and expansion of banking activities both at home and abroad. As things are at present, however, it is out of the question for banks to set themselves pre-war capital-deposit ratios as target, owing to the expansion which has occurred in deposits and current accounts and increased operating costs; furthermore said ratios would be unnecessary in a situation like the present when the interests of depositors are guaranteed by so many public controls.

Wishing to indicate a realistic and at the same time technically adequate proportion, one might consider an average capital-deposit ratio of from 3 to 6 per cent. However, since the Italian banking system as a whole is below these levels, it might be sufficient:

a) to reach an intermediary ratio between the « legal » pre-war ratio (5%) and the present average (2%);

b) to consider the latter as a « limit » ratio in view of the changed economic situation and use it for purposes of control, judging any departure from it as a sign that the bank in question is in a bad way.

No statement regarding this matter has so far been

made by the supervisory authorities. Nevertheless, although any comparison of capital to deposits is now outdated having been absorbed in practice by the new system of compulsory reserves, some term of comparison of the type mentioned above might integrate, and be satisfactorily conciliated with, said reserve system, if it were applied by the supervisory authorities as a term of orientation without rigid formalities.

(22) See P. SARACENO, *La banca di credito ordinario*, Milan, 1949, page 109.