Personal saving and financial investment: 1951-65

This article traces the main patterns in the personal sector's finances over the past fifteen years. It is concerned with saving and investment by the personal sector as a whole, and not with the distribution of saving between different groups within the sector. A study of the sector's finances is not only of considerable interest in itself, but it also provides a background against which current developments in the personal sector may be seen more clearly. Some of the estimates for the earlier years are rather uncertain,(1) but the general story is well founded.

The personal sector is one of the main sectors distinguished in the annual articles on sector financing(2) and in the quarterly analysis of financial statistics (page 221). This sector includes not only individuals—for whom separate figures are not available—but also unincorporated businesses and private non-profit-making bodies. Figures for the fifteen years are given in the tables at the end of this article.

Saving The figures for personal saving, taken from the national income accounts, are the residual differences between independent estimates of personal disposable income (income after deducting tax, national insurance and health contributions, and net remittances abroad) and of consumers' expenditure. Both these estimates are subject to error, so that the error in the difference between them may be substantial; but the figures are the best available.

It is often convenient to look at the proportion of personal disposable income which is saved, rather than at the level of saving. This proportion, or savings ratio, has fluctuated from year to year, but its longer-term trend has been upward; in 1960-65 it was around 8%, compared with less than 4% in the early 1950's (Table I). With incomes rising too, the amount saved in 1962-65 was four times as much as a decade earlier, and, even after allowing for a fall in value because of the 30% rise in consumer prices, it was three times as great.

There are many reasons for the increase in saving. One is the rise in general prosperity—as people become richer they are able to save a greater proportion of their incomes. The growth of pension schemes, particularly occupational schemes, has also had a big influence; in fact, the growth in life assurance and pension funds accounted for about half the increase in personal saving between the two periods.(3) The spread of owner-occupation and the associated growth in saving through building societies has been another important factor.

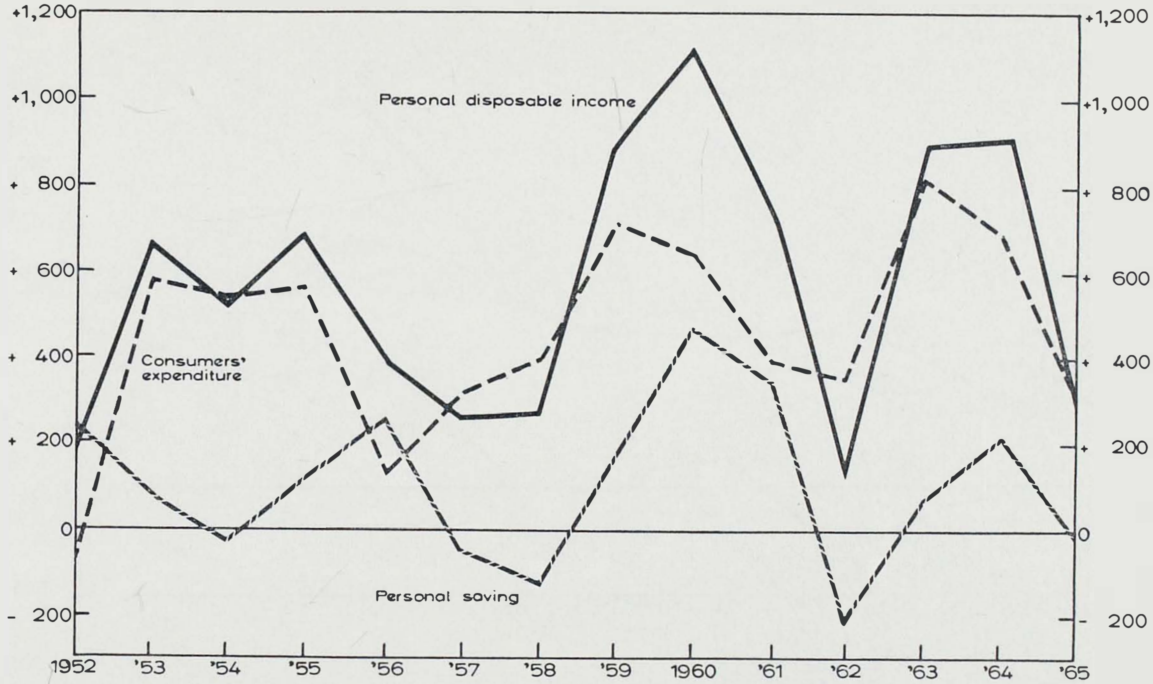
The personal sector's share of total domestic saving rose from 17% in 1952-55 to 31% in 1962-65. This increase was largely at the expense of companies, whose share fell from 57% to 48%. These changes were related to an increase in the proportion of profits

(1) Notably those for borrowing from banks and through hire purchase, and for investment in bank deposits and local authority debt.

(2) The latest appeared in the June *Bulletin*, page 128.

(3) Life funds of insurance companies and assets of pension schemes (other than National Insurance Funds) are regarded as the collective property of policyholders and contributors. So personal saving in the national income accounts includes the increase in these funds—arising from the excess of contributions (including employers' contributions), premiums and income from investments and property over pensions, other benefits and administrative costs.

Annual changes *£ millions at constant (1958) prices*



distributed as interest and dividends. The public sector's share of saving (that is, the public sector's excess of current receipts over current expenditure) changed little over the period; it was 24% in the early 1960's, against 23% ten years earlier.(1)

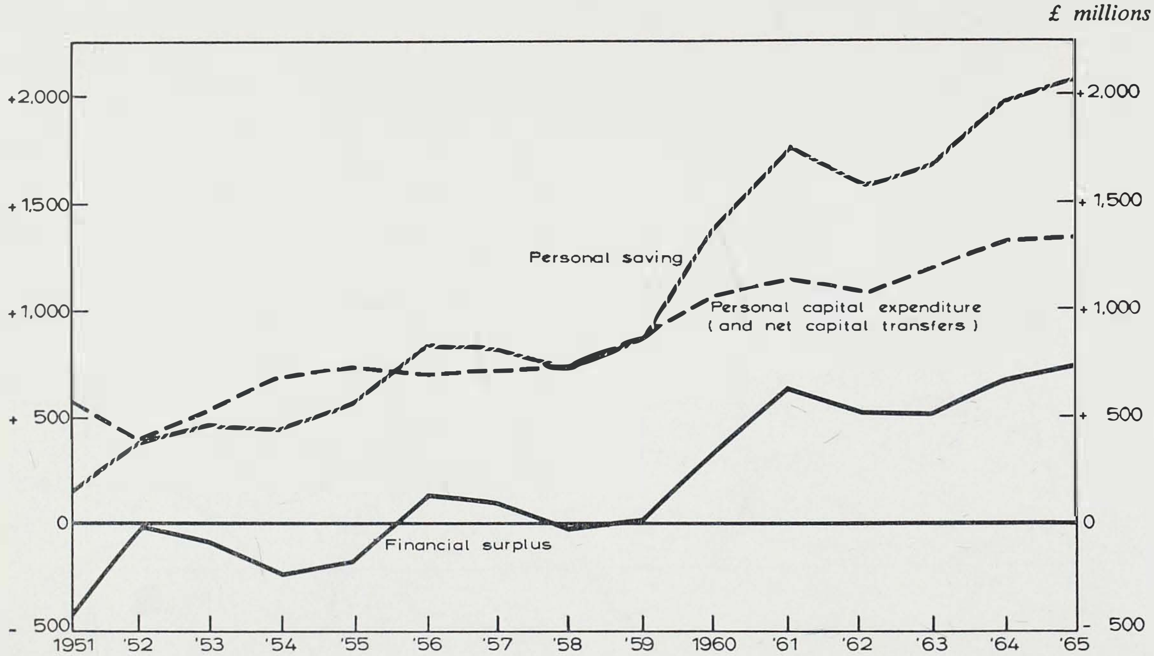
Short-term fluctuations in personal saving have taken place because of variations in the rate of increase of real incomes (that is, increases in value after taking account of movements in consumer prices) and of real consumption; they have been associated with changes in fiscal and monetary policies and in the economy generally. In the latter half of the period, real saving improved rapidly when real incomes grew rapidly—in 1959-61 and in 1963-64. It rose relatively slowly or fell when real disposable incomes grew slowly—in the years 1954, 1957, 1958, 1962 and 1965.

The peaks in the savings ratio usually followed periods in which real disposable incomes were rising fast; they occurred in years in which action was taken to correct inflationary conditions present or seemingly imminent and when growth in real consumption fell. Measures taken to control the growth of incomes after the rapid increases of 1955, 1960 and 1963 curbed consumers' expenditure and led to peaks in the savings ratio in 1956, 1961 and 1964. On the other hand, in the years when the savings ratio was low, measures were taken to stimulate demand—in 1954, 1958 and 1962.

Financial surplus

Out of its saving the personal sector makes net transfers of capital to the public sector; acquires physical assets, in the form of fixed investment and stocks of goods and work in progress; and, in recent years, has still had large amounts available for investing in financial assets. These amounts are known as its financial surplus.

(1) It will be noted that there is a discrepancy between the increases in the personal and public sectors' shares of saving and the fall in companies' share. This is because the two independent estimates of gross domestic product, obtained from income and expenditure data respectively, differ. The discrepancy, known as the residual error, indicates that in the 1950's income was generally underestimated or expenditure overestimated, while in the 1960's the position was reversed. This suggests that the rise in personal saving might have been exaggerated; but the suggestion is not supported by statistics of financial transactions: this is discussed later in the section on the unidentified item.



Capital transfers to the public sector comprise payment of death duties, less capital grants received from local authorities and the central government, such as those to universities (which form part of the personal sector). Net transfers averaged £120 million a year in the early 1950's and £190 million ten years later. The sector's capital expenditure is of two main kinds: expenditure by persons on new dwellings and by unincorporated businesses on fixed investment and stockbuilding—and is calculated net of sales of land and existing buildings to other sectors. Capital expenditure rose from an average of some £460 million per annum in 1952-55 to £1,030 million in 1962-65, a rise of 120%: the increase in real terms was about 80%. Most of the increase was due to investment in new dwellings, which rose by 220% (160% in real terms).

Growth in saving over the fifteen years was very much greater than that in capital expenditure and transfers, so that the personal sector's financial position swung from a deficit in the early 1950's to a surplus by 1956. It has remained in surplus in nearly all the subsequent years—from 1961 onwards, on average, by over £600 million a year (Table I).

There were, of course, considerable short-term variations in the sector's financial position. Capital transfers did not grow steadily, and capital expenditure fluctuated cyclically; it was noticeably high in 1955 and 1961, and low in 1952, 1956-58 and 1962. But the fluctuations in these items were small in relation to those in personal saving, and changes in the financial deficit or surplus generally tended to move in line with those in saving. Saving was relatively high and the financial surplus was relatively large (or the financial deficit was relatively small) in 1952-53, 1956-57, 1961 and 1964-65. When saving was low—in 1954, 1958 and 1962-63—the financial position was relatively weak.

The personal sector's financial position can also be looked at in terms of movements in financial assets and liabilities. In fact, the sector customarily not only invests in financial assets, but also borrows on a large scale. There is, however, a sizable discrepancy (the unidentified item) between the deficit or surplus derived from national income figures and the net identified changes in financial assets and liabilities. These aspects are now examined.

Identified borrowing

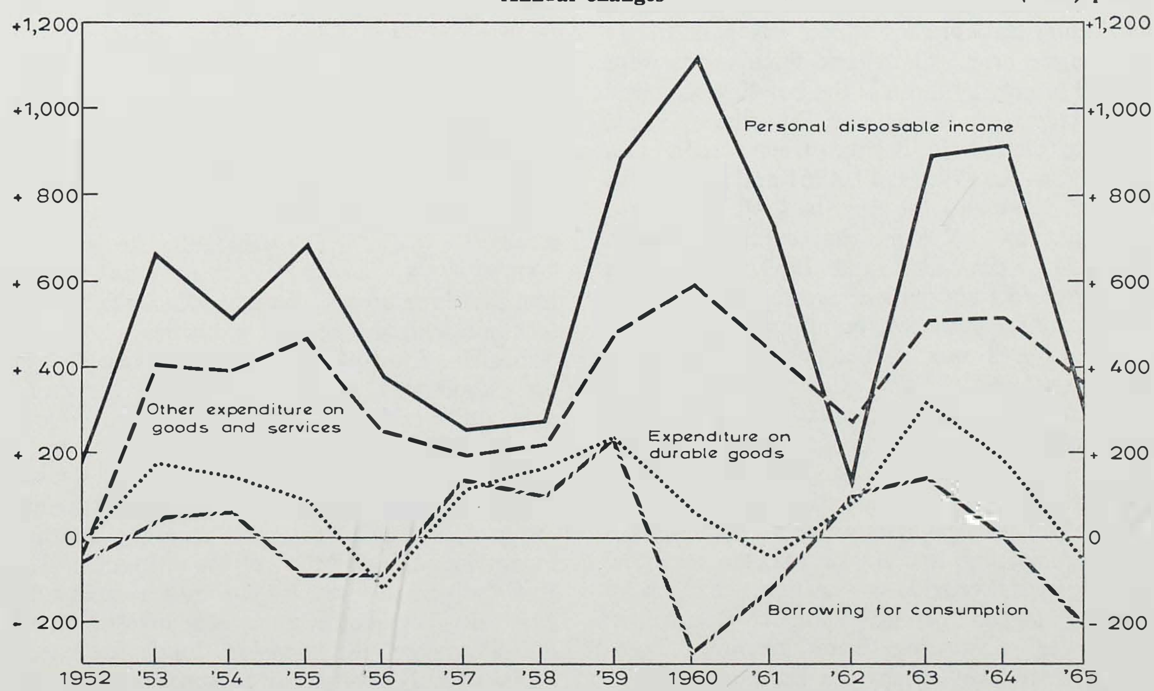
The kinds of borrowing which have been identified are principally borrowing from banks, from finance companies and shops by means of instalment debt, and from various institutions to finance house purchase. On a smaller scale, the personal sector also borrows from insurance companies (other than for house purchase) on the security of life assurance policies and from the Agricultural Mortgage Corporation. Some of the figures are approximations only, particularly in the earlier years. No estimates have been made for net trade credit received from companies.

Most of the personal sector's identified borrowing falls into two categories (Table III). The first, which mainly finances consumption, consists of bank borrowing (other than for house purchase) and instalment debt; such borrowing has been restricted during periods of credit control. The second is borrowing for house purchase, the greater part of which has generally been much more free from official control.

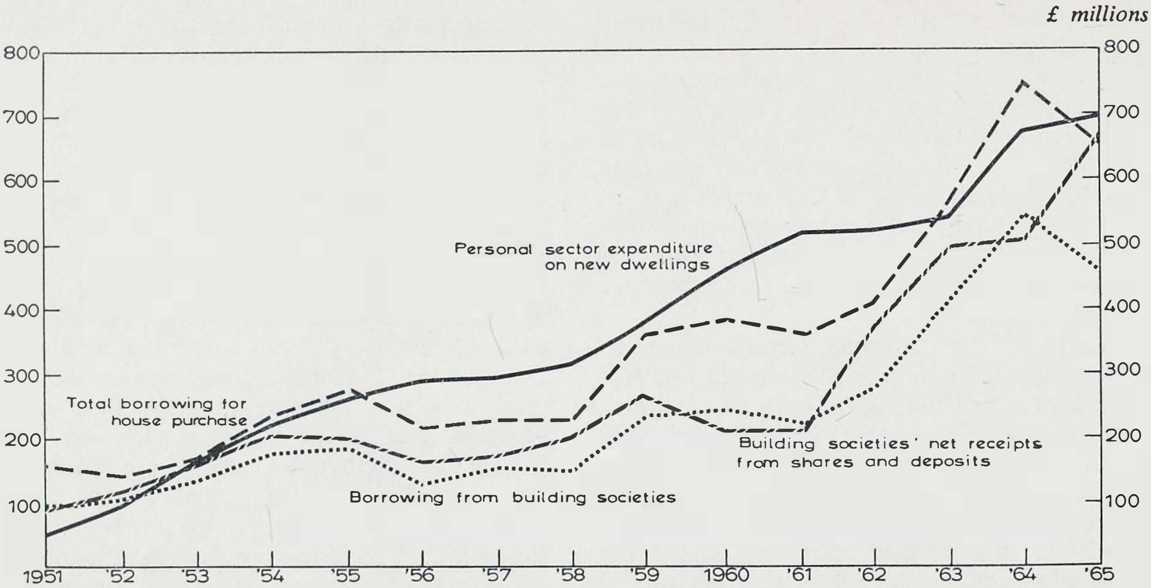
Consumer purchases of durable goods are strongly influenced by the availability of credit: as shown in the chart below, there is a close relation between annual changes in purchases of durables and annual changes in new consumer borrowing (net of repayments). The chart also shows that changes in spending on durable goods have corresponded broadly to changes in personal income. Regression analysis suggests that every £100 million increase in consumer borrowing raises expenditure on durables by about £70 million during the same period, and that, if real personal disposable income rises by £100 million more than usual, purchases of durables will rise by about £20 million.[1] Personal income seems to be the most important influence on consumers' purchases of other goods and of services—though it is noticeable that this expenditure has risen much more steadily than personal income.

Borrowing for house purchase is mainly from building societies, but significant amounts are also borrowed from insurance companies, local authorities and banks. Although borrowing is not wholly, or even mainly, for new houses, the sale of one house often provides funds for the purchase of another, so money

Annual changes *£ millions at constant (1958) prices*



(1) The regression equation is $D = -18 + 0{\cdot}20Y + 0{\cdot}67H$ ($R^2 = 0{\cdot}76$) where D is the change in spending on durable goods, Y is the change in personal disposable income, and H is the change in consumer borrowing (net of repayments)—all measured in £ millions at 1958 prices.

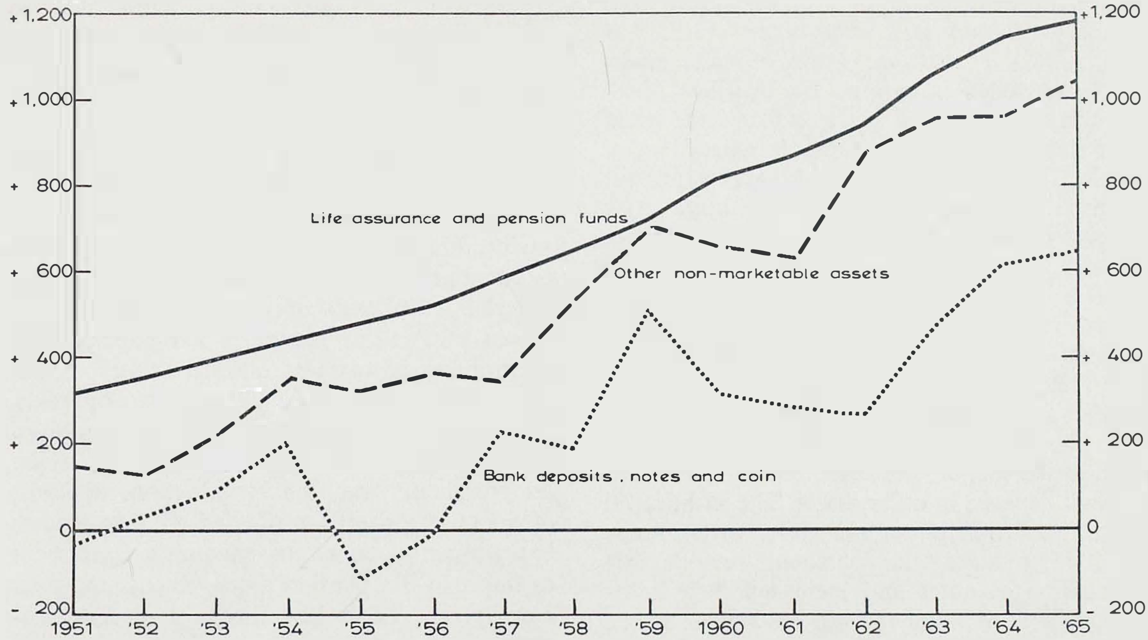


lent for the purchase of an existing house frequently finds its way into the new housing market. Total borrowing rose from a yearly average of some £200 million in 1952-55 to nearly £600 million in 1962-65; it was associated with the growth of owner-occupation and was affected too by the rise in prices (including land prices), which was particularly steep after 1958. Short-term fluctuations were caused largely by those in the building societies' net receipts on shares and deposits. These receipts tended to decline when credit was tightening—in 1956, 1960, 1961 and the second half of 1964 and the first half of 1965—and rose substantially in the easy credit conditions of 1954, 1959, 1962 and 1963. The yields obtainable on alternative investments also had a substantial effect on building societies' net receipts: this was particularly noticeable in the second half of 1965, when credit conditions were not easy but the relatively favourable rates offered by building societies attracted a large inflow of funds. The societies' lending tended to follow the pattern of these fluctuations; but because commitments to lend are made some time in advance, and the societies' liquid assets provide a cushion, changes in lending lagged behind changes in receipts. Moreover, borrowing from insurance companies and local authorities reached peaks in 1956 and 1961, and was heavy in 1965—occasions when building society mortgages were difficult to obtain.

The rise in borrowing for house purchase accounts for much of the long-term upward trend in total identified borrowing. Short-term fluctuations in the total were affected by official measures to restrict or ease credit—both directly and because of their influence on the building societies' receipts of funds and thus on their ability to lend. When people could borrow more, they spent more on durable consumer goods and on dwellings and this tended to reduce the personal sector's financial surplus; when borrowing was restricted they spent less, and the surplus tended to increase.

Identified financial assets The personal sector's financial assets may be divided into the three broad groups shown in Table IV, together with marketable securities, shown in Table II. Some of the figures for these groups are estimated, but they are probably a reasonable guide to broad movements. Apart from marketable securities, holdings of which have fallen in each year since separate figures became available in 1961, acquisitions of each group of assets have tended to grow, as both money incomes and the savings ratio increased. But the growth was by no means uniform: while the personal sector's new investment in life assurance and pension funds increased fairly steadily from year to year, the pace of growth in holdings of bank deposits and notes and coin, and in other non-marketable assets, was much less even.

Annual changes *£ millions*



People receive their incomes as notes and coin or bank deposits. Initially, new saving is the residual balance held in this form after consumer goods and services have been paid for; and savings remain held in this way until people decide to change the composition of their assets. The decision to change may be semi-automatic (as, for example, when people have contractual commitments to pay premiums to pension funds) or it may be deliberate. In any event, the decision will reflect the saver's knowledge of ways of investing funds, his needs, in varying degrees, for liquidity in his financial assets and for security of income and of capital, and the relative yields offered by alternative forms of investment.

Acquisitions of particular assets reflect not only new saving but also changes in the disposition of asset portfolios. An increase in the personal sector's holdings of bank deposits and other non-marketable assets may be caused by sales of marketable securities—and purchases of marketable securities would draw down deposits. It is noticeable that net acquisitions of non-marketable assets reached peaks in 1954 and 1959 and were high in 1963—years in which interest rates came to the end of a decline and then began moving upwards. In such years uncertainty about the future capital value of fixed interest marketable securities may have contributed to sales of stocks, and the take-over bids which were particularly prevalent in 1959 may also have left persons with liquid funds awaiting reinvestment. Again, in 1964 and 1965, uncertainty in the capital markets caused by the general elections and by tax changes may have caused people to delay investing their funds.

Bank deposits, notes and coin Notes, coin and current accounts with commercial banks do not earn interest; the rate on ordinary deposits with the Post Office Savings Bank and with the ordinary departments of the trustee savings banks is fixed at $2\frac{1}{2}\%$, though with the tax concession noted below; and only deposit accounts with commercial banks offer a rate of interest which changes with Bank rate.(1) The continued growth in holdings of these assets

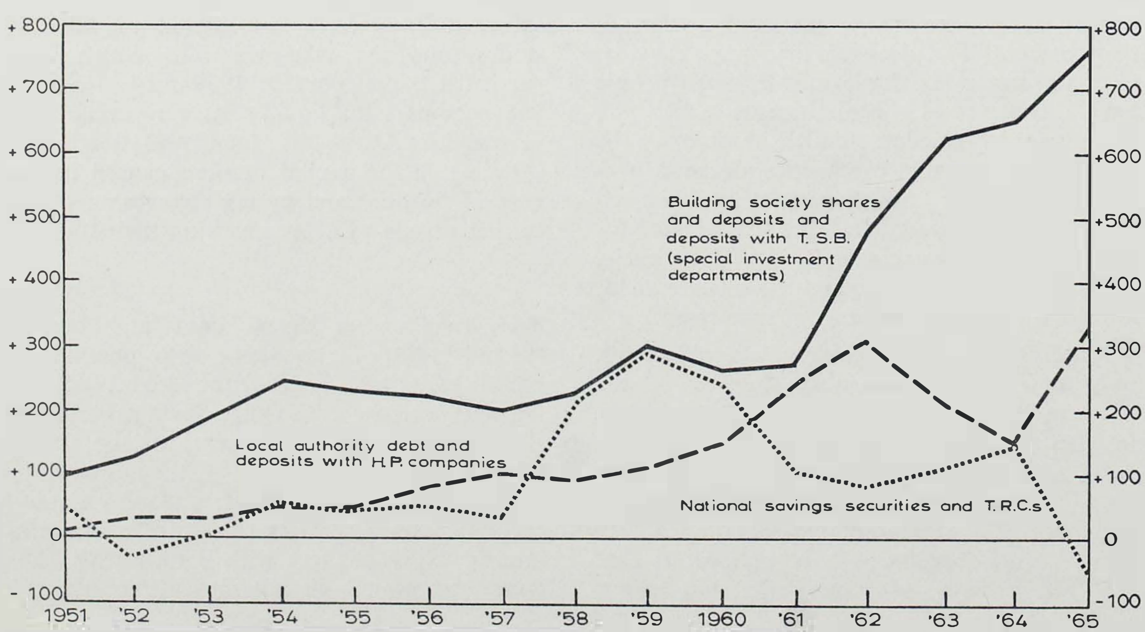
(1) Ideally, as the interest rate is variable, deposit accounts should be classified with other non-marketable assets in this analysis; but deposit accounts of the personal sector cannot be distinguished separately.

as a whole is a reflection of the growth in personal income, and the consequential need for larger liquid balances. When credit was tightening, however, the share of these assets in the personal sector's net acquisitions of all financial assets fell sharply, because the yield offered by other non-marketable assets tended to rise. The years 1956 and 1957 stand out from this general pattern, but in both cases interest rates provide an explanation. In 1956, income tax exemption was granted to the holders of deposits with the P.O.S.B. and with trustee savings banks, ordinary departments, in respect of the first £15 of interest, thus raising the effective yield: in 1957 there was a substantial switch from current to deposit accounts with the clearing banks after Bank rate had been raised to 7%; this discouraged investment of bank deposits in other assets. The withdrawal from circulation of an old series of £1 notes in 1962 reduced the personal sector's net acquisition of notes and increased their holdings of bank deposits and other financial assets. As already mentioned, the big increases in 1964 and 1965 may well have been partly explained by the uncertainty in the capital markets.

Life assurance and pension funds

As explained earlier, life assurance and pension funds are regarded, in the national income statistics, as the collective property of the personal sector. Increases in the assets of these funds, which have grown steadily throughout the period, are therefore treated as increases in personal claims on the financial institutions concerned. Most of the saving through these media is contractual, and is consequently insulated from fluctuations in the rate of growth of income. During the fifteen years there has been a big increase in the number of workers insured under occupational pension schemes. From 1956 onwards, purchases of annuities by self-employed persons have been encouraged by tax relief on premiums; and the introduction, in 1961, of the Government's graduated pension scheme has probably tended to encourage employers to improve the pension arrangements for their employees. There has also been a very substantial increase in the rent, dividend and interest incomes of life assurance and pension funds.

Annual changes *£ millions*



Other non-marketable assets The personal sector's acquisitions of other non-marketable assets, such as building society shares, local authority mortgages and national savings securities, have also grown substantially, from an average of some £250 million per year in 1952-55 to about £950 million per year in 1962-65. However, this growth did not take place evenly. As the chart on page 251 shows, it was much less steady than the acquisition of financial assets through life assurance and pension funds; but the fluctuations were less pronounced than those in bank deposits and notes and coin. Interest rates on some or all of these non-marketable assets were raised when credit became tight: so that, while the growth of acquisitions slackened, or even fell slightly, the impact of the credit squeeze on holdings of these assets was weakened considerably. As with bank deposits, the high level of acquisitions in 1964 and 1965 was probably influenced by uncertainty in the capital markets.

Relative interest rates and other features of the different assets have a strong influence on the distribution of personal funds between them. Better terms on national savings certificates and the introduction of premium savings bonds brought slightly greater investment in national savings securities in 1956; and holdings increased considerably during the easy credit conditions of 1958-59, helped by a new higher-yielding defence bond. However, in 1960-62 the yields on national savings securities did not rise in line with other rates, notably those offered by building societies and local authorities, and although limits on holdings were raised, investment in national savings securities moderated: the same pattern occurred in 1965, when there was a net withdrawal of funds. The growth in personal acquisition of local authority debt, from £40 million a year in 1952-55 to £240 million a year by 1962-65, reflected the increase in total local authority borrowing from non-government sources—stimulated by the change in 1955 in the arrangements for borrowing from the Public Works Loan Board.

Marketable securities These include gilt-edged stocks, company securities, overseas securities and unit trust units: personal holdings of local authority securities are not distinguishable from those of other local authority debt. Estimates of the personal sector's transactions in marketable securities are available only from 1961 onwards, but in each of the years for which figures are available the sector made large net sales—rising from £325 million in 1961 to an average of over £700 million a year in 1963-65.

Many personal sales of securities are associated with the distribution of deceased persons' estates and the payment of death duties. Others arise when companies make take-over bids by offering shareholders cash, rather than an exchange of shares. The large sales by the personal sector are also partly associated with the growth of life assurance and pension funds, whose annual purchases of securities regularly exceed the amount of new issues in London; this means that people are acquiring an indirect, rather than a direct, interest in securities. A particularly clear example of this occurs when securities are sold to finance the purchase of an annuity: purchases of annuities have latterly been of the order of £100 million a year. Unit trust units are a popular means of holding company securities indirectly—net purchases grew from an annual average of £18 million in 1960-62 to £65 million in 1963-65—and new issues by investment trusts also give persons the opportunity of taking an indirect interest in the securities of non-financial companies.

Persons' sales of government stocks were particularly large in 1963; interest rates reached a low point in this year and then began to rise, so that investors were inclined to take a profit or to delay reinvestment. The early 1960's were not a good period for equities; prices had risen rapidly in 1958-59, but at the end of 1965 they were generally no higher than in the spring of 1961. This may have been another factor leading to the personal sector's large sales of company securities.

Unidentified The unidentified item is the difference between the personal sector's financial surplus (or deficit) as estimated on the one hand from national income data and on the other hand from identified financial transactions. It therefore reflects errors and omissions in the national income figures as well as the extent to which financial transactions are not recorded or are inadequately estimated.

Throughout the period the financial statistics suggest an increase in the personal sector's net financial assets which, even after deducting the estimates for the sector's sales of securities in 1961-65, was consistently greater than the financial surplus indicated by the national income estimates (Table II). Thus the national income figures for personal saving may be too small (income too low, or consumers' expenditure too high) or those for capital expenditure may be too large. In the financial statistics, figures for borrowing may be too small, investment in financial assets too great or sales of financial assets underestimated.

An important omission from the financial statistics is borrowing from companies in the form of trade credit—often simply delayed settlement of accounts. This must tend to increase in the long term as money incomes rise, and may well help to explain the rise in the size of the unidentified item since the early 1950's; it might also account for some of the fluctuations in this item. The Board of Trade figures for increases in gross trade credit extended by non-manufacturing quoted companies show a rise each year from 1951 to 1965;[1] and fluctuations in the figures show some correspondence with those in the unidentified item, after allowing so far as possible for the personal sector's transactions in marketable securities for the years 1951-60—which are included indistinguishably in the unidentified item. As already mentioned, such evidence as there is points to particularly large personal sales of government stocks in 1954 and of company securities, associated with take-over bids, in 1959—two occasions on which the unidentified item was large.

Conclusion Personal saving has grown much more over the last decade than the personal sector's capital expenditure and capital transfers, and the sector now customarily has a large financial surplus. Substantial personal funds are lent to other persons—through banks, building societies and hire purchase finance companies. Other funds reach industrial and commercial companies, not only through banks and finance companies but also, and on a larger scale, through insurance companies, pension funds and investment and unit trusts; the sector's direct holdings of non-financial company securities have fallen in each of the last few years—the only ones for which figures are available. Personal lending also helps to finance the public sector, both through financial intermediaries and directly, especially through national savings and local authority debt. The personal sector borrows from industrial and commercial companies in the form of instalment debt (from shops) and probably through trade credit.

The personal sector's real disposable income, its saving, and its financial surplus all tended to follow much the same course during the past fifteen years. On three occasions after official measures had been taken to restrain domestic demand the growth of incomes was moderated; subsequently saving fell and the financial surplus was reduced or the deficit was increased. When credit restrictions were removed, the personal sector's income, saving, and borrowing increased. The growth of consumption was much steadier than the growth of income during the fifteen years.

On each occasion, the removal of credit restrictions coincided with a decline in interest rates, which continued until the rise in incomes again began to accelerate. At the troughs of the interest rate cycle persons appear to have sold marketable securities heavily, and probably received trade credit, as well as having borrowed from financial institutions. They thus accumulated other financial assets more quickly in those years, although their income growth, their saving and their financial surplus were not necessarily at a peak. They moderated their purchases of these assets when borrowing was restricted and when interest rates had risen high enough to discourage sales of marketable debt. Contractual saving, however, was virtually immune from these fluctuations. The most violent changes occurred in bank deposits, notes and coin; there were more gentle fluctuations in the group of assets whose yields moved with the general level of interest rates.

[1] See *Economic Trends* for April 1962, and later figures in *Financial Statistics*.

Table I

Derivation of financial surplus

£ millions

	A Personal disposable income	B Consumers' expenditure	C Personal saving[a] (A–B)	D Capital transfers (net payments)	E Capital expenditure[b]	F Financial surplus (C–D–E)
1951	10,374	10,215	159 (1·5)	124	451	−416
1952	11,142	10,766	376 (3·4)	100	299	− 23
1953	11,931	11,475	456 (3·8)	119	411	− 74
1954	12,600	12,160	440 (3·5)	147	527	−234
1955	13,667	13,107	560 (4·1)	120	619	−179
1956	14,644	13,821	823 (5·6)	110	586	+127
1957	15,385	14,582	803 (5·2)	129	577	+ 97
1958	16,073	15,365	708 (4·4)	134	602	− 28
1959	17,047	16,160	887 (5·2)	165	709	+ 13
1960	18,330	16,963	1,367 (7·5)	184	869	+314
1961	19,620	17,862	1,758 (9·0)	198	943	+617
1962	20,477	18,893	1,584 (7·7)	188	878	+518
1963	21,732	20,049	1,683 (7·7)	221	956	+506
1964	23,352	21,380	1,972 (8·4)	199	1,105	+668
1965	24,759	22,708	2,051 (8·3)	157	1,167	+727

(a) Figures in brackets are the ratios of personal saving to personal disposable income.

(b) Gross fixed capital formation and increase in value of stocks and work in progress.

Table II

Financial transactions

£ millions

	Identified borrowing	Identified assets	Marketable securities[a]	Unidentified[b]	Financial surplus
1951	− 273	+ 421	− 564		−416
1952	− 66	+ 503	− 460		− 23
1953	− 189	+ 707	− 592		− 74
1954	− 351	+1,000	− 883		−234
1955	− 293	+ 681	− 567		−179
1956	− 172	+ 854	− 555		+127
1957	− 271	+1,149	− 781		+ 97
1958	− 521	+1,372	− 879		− 28
1959	− 925	+1,939	−1,001		+ 13
1960	− 676	+1,786	− 796		+314
1961	− 402	+1,781	−325	−437	+617
1962	− 587	+2,087	−402	−580	+518
1963	− 736	+2,497	−747	−508	+506
1964	−1,016	+2,714	−656	−374	+668
1965	− 675	+2,860	−720	−738	+727

(a) Transactions in government stocks, company and overseas securities, and unit trust units, but excluding transactions in local authority securities which cannot be separated from changes in holdings of local authority debt as a whole. Figures before 1961 include "unidentified".

(b) The difference between identified financial transactions and the financial surplus or deficit derived from national income statistics.

Table III

Identified borrowing *£ millions*

	For consumption[(a)]	For house purchase[(b)]	Other[(c)]	Total
1951	24	160	89	273
1952	— 25	139	— 48	66
1953	9	168	12	189
1954	62	237	52	351
1955	— 15	277	31	293
1956	— 98	218	52	172
1957	40	228	3	271
1958	132	228	161	521
1959	354	360	211	925
1960	89	385	202	676
1961	— 31	361	72	402
1962	58	410	119	587
1963	178	568	— 10	736
1964	180	750	86	1,016
1965	— 9	657	27	675

(a) The " personal and professional " group in the British Bankers' Association analysis of advances (excluding estimated loans for house purchase) plus consumer hire purchase debt.

(b) From building societies, insurance companies, banks, local authorities and the central government. Borrowing from banks for financing house purchase has been estimated on the basis of published figures for the London clearing banks and interpolations for years when no published data were available.

(c) Mainly borrowing on policies from insurance companies, other than for house purchase; from the Agricultural Mortgage Corporation; and the personal sector's borrowing from banks (*e.g.* by unincorporated businesses) which is not included in the " personal and professional " category.

Table IV

Identified acquisition of financial assets *£ millions*

	Bank deposits, notes and coin[(a)]	Life assurance and pension funds	Other non-marketable assets[(b)]	Total
1951	— 43	314	150	421
1952	27	351	125	503
1953	94	393	220	707
1954	205	437	358	1,000
1955	—119	478	322	681
1956	— 13	515	352	854
1957	225	579	345	1,149
1958	188	649	535	1,372
1959	513	717	709	1,939
1960	312	816	658	1,786
1961	286	869	626	1,781
1962	268	941	878	2,087
1963	474	1,066	957	2,497
1964	618	1,140	956	2,714
1965	644	1,173	1,043	2,860

(a) Including deposits with the Post Office Savings Bank and with trustee savings banks (ordinary departments).

(b) National savings securities, tax reserve certificates, deposits with trustee savings banks (special investment departments), building society shares and deposits, local authority debt and deposits with hire purchase finance companies.