Company finance: 1952-65

This article is concerned with the finance of industrial and commercial companies[1] over the fourteen years 1952-65; it examines changes in the main sources of their funds and in the main uses to which the funds have been put. Many of the statistics are rather uncertain: in particular, the national income and expenditure accounts do not fully distinguish between the transactions of industrial and commercial companies and those of other companies; and the figures for the financial transactions of companies are not wholly comprehensive, especially in the earlier years. However, it is thought that the broad outlines of the picture which emerges would not in fact be much changed even if the statistics were complete.

Total sources and uses of funds

For the purposes of this article, current transactions are shown in more detail than in the sector financing accounts used in the analysis of financial statistics (page 16), and the figures generally are presented in a different form. There, certain items of income and expenditure are grouped together; here, total income and total expenditure, both current and capital, are divided into "sources" and "uses" of funds, as defined below.

Sources of funds are:

a gross trading profits (less stock appreciation),[1]

b other current income in the United Kingdom (rent and non-trading income),

c current income from abroad,[1]

d capital grants from the public sector,

e overseas investment in U.K. companies,[1] and

f borrowing, less net acquisitions of liquid financial assets.

Identified uses of funds comprise expenditure in the forms of:

a dividends and interest,[1] and profits due abroad,[1]

b taxes (in the United Kingdom and abroad),[1]

c subscriptions to charities,

d gross fixed investment,

e stockbuilding (the value of the physical increase in stocks and work in progress),

f investment abroad,[1]

g purchases of U.K. company securities from other sectors of the economy, and

h changes in hire purchase credit extended.[1]

The difference between identified sources of funds and identified spending – the unidentified item – has been treated as an item of expenditure. It doubtless includes some errors and omissions in the estimates of companies' receipts but a significant part of the item – and particularly of changes in it – probably relates to trade credit granted by the company sector, which is properly regarded as a use of funds.

Both sources and uses of companies' funds have fluctuated from year to year along a generally upward path (Chart A), the fluctuations broadly reflecting movements in the general level of business activity, which has chiefly determined both the need for finance by companies and the availability of it.

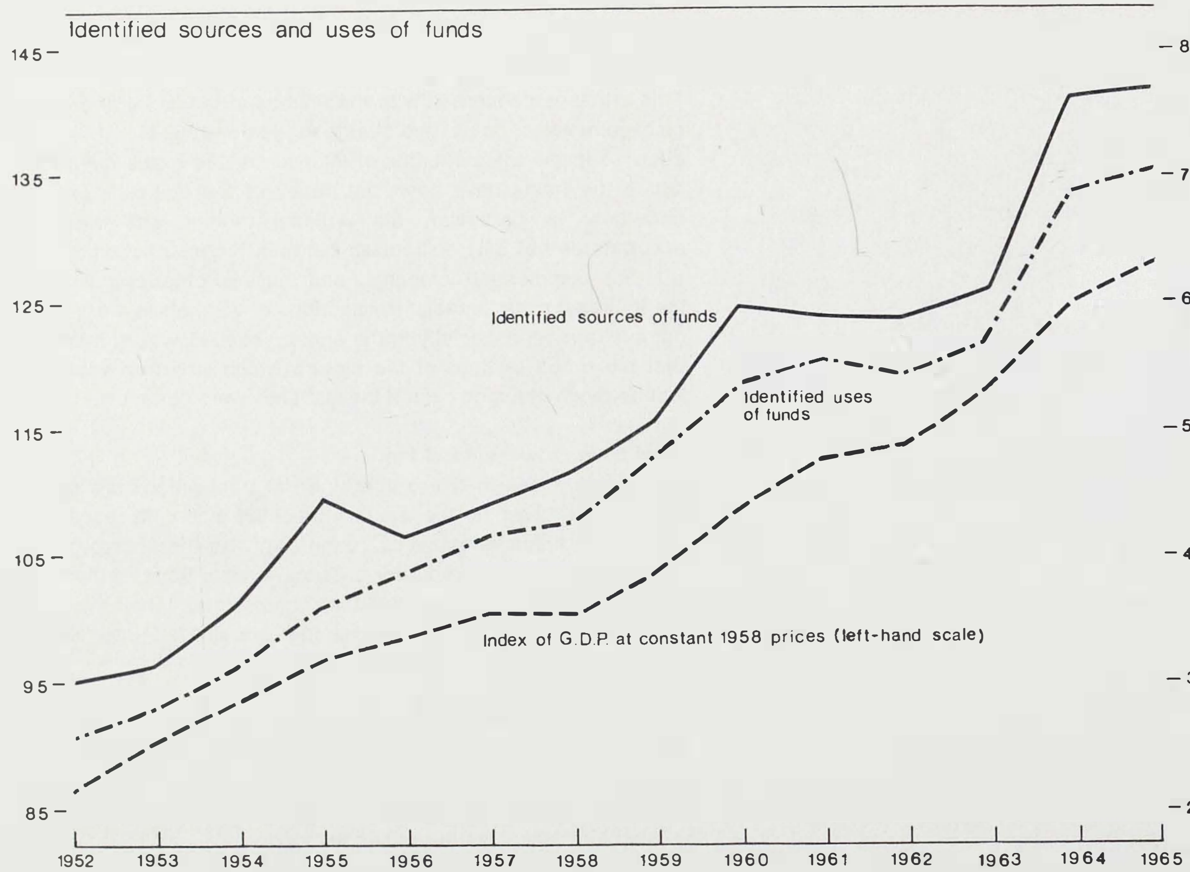
Thus gross fixed investment, which forms a large part of com-

1 Defined in the notes on page 42.

Chart A

1958=100

£ millions



panies' total spending and which is the main indicator of their expectations about business prospects, has grown unevenly year by year. Total spending, however, has fluctuated less, partly because stockbuilding and tax payments, as noted later, have usually moved differently from gross fixed investment and partly because dividend and interest payments have risen fairly consistently throughout.

Business conditions and expectations have also strongly affected the sources of companies' funds. As activity slows down, so profits and borrowing tend to decline: and conversely when business is expanding. The changes in identified sources of funds around 'boom' years have been rather more pronounced than the changes in identified spending, and there has been a marked tendency for the discrepancy between the totals – the unidentified item – to rise steeply in boom years and to fall just afterwards.

This is how one would expect the unidentified item to behave if its movements were largely attributable to trade credit granted to persons – for which no estimates have been made. For the personal sector, the unidentified item is also large but in the opposite direction.[1] But it is probable that, in each case, the item arises not only because no estimates have been made of some direct transactions between the two sectors, such as trade credit, but also because some estimates which in total are broadly correct are wrongly divided between the two sectors. This may occur, for example, in

1 The unidentified item in the personal sector indicates that expenditure is overstated (or income understated); in the company sector the indication is that expenditure is understated (or income overstated).

the figures of transactions in liquid assets, or in some of the statistics taken from the national income and expenditure accounts, such as payments of U.K. tax.

Sources of funds

Total funds available to companies can conveniently be divided between those generated by companies themselves (internal funds) and those acquired outside (external funds).

Internal funds comprise gross trading profits (less stock appreciation), other current income in the United Kingdom, and current income from abroad. External funds are capital items – capital transfers from the public sector, overseas investment in U.K. companies, and borrowing from other sectors less net acquisitions of liquid financial claims on other sectors. Figures are shown in Table A.

The treatment of transactions in liquid financial assets calls for some explanation. Over the whole period liquid assets increased, on balance, by £1,275 million. Companies need such assets as working capital to finance short-term fluctuations in their total payments and receipts, and increases on that account – in line with increases in turnover – should properly be regarded as part of expenditure. However, liquid assets have not risen as fast as turnover. The reason for this seems to be that in the earlier years a substantial part of companies' liquid assets represented a reserve for longer-term fluctuations in capital expenditure, but that by the end of the period the reserve had been reduced. The drawing down of this reserve, associated as it is with a decline in companies' reliance on internal funds for their capital expenditure, is of primary significance in the context of this article; for this reason the net increase in total liquid assets is treated as a (negative) source of funds.

As a proportion of funds from all sources, internal funds have fallen from 93% in 1952-58 to 85% in 1959-65. The corresponding increase in the importance of external funds shows up mainly in greater recourse to market finance – more borrowing on capital issues and from banks and other institutions, and the running down of some types of liquid financial assets. Overseas investment in U.K. companies has also grown faster than companies' total resources, but the figures are relatively small. Receipts of government grants, which are smaller still, declined over the period.

Among internal funds, "other current income" has grown considerably, and by almost enough to maintain its proportion of the total of companies' funds; in 1959-65 it represented 21% of the total compared with 22% in 1952-58. The lessening importance of internal sources in relation to the total is thus mainly attributable to gross trading profits, which accounted for 71% of total funds in 1952-58 but only 64% in 1959-65. This decline is reflected in a rather lower share in total domestic incomes taken by industrial and commercial companies' profits (15·8% in 1959-65, as against 16·5% in 1952-58). The counterpart of this lower share is very largely a rise in the share taken by income from employment (from 67·2% in 1952-58 to 67·8% in 1959-65). These figures illustrate, broadly, the change from the relatively easy trading conditions of the early 1950's, when increased costs were typically passed on in higher prices, to the more competitive climate at home and abroad in the 1960's.

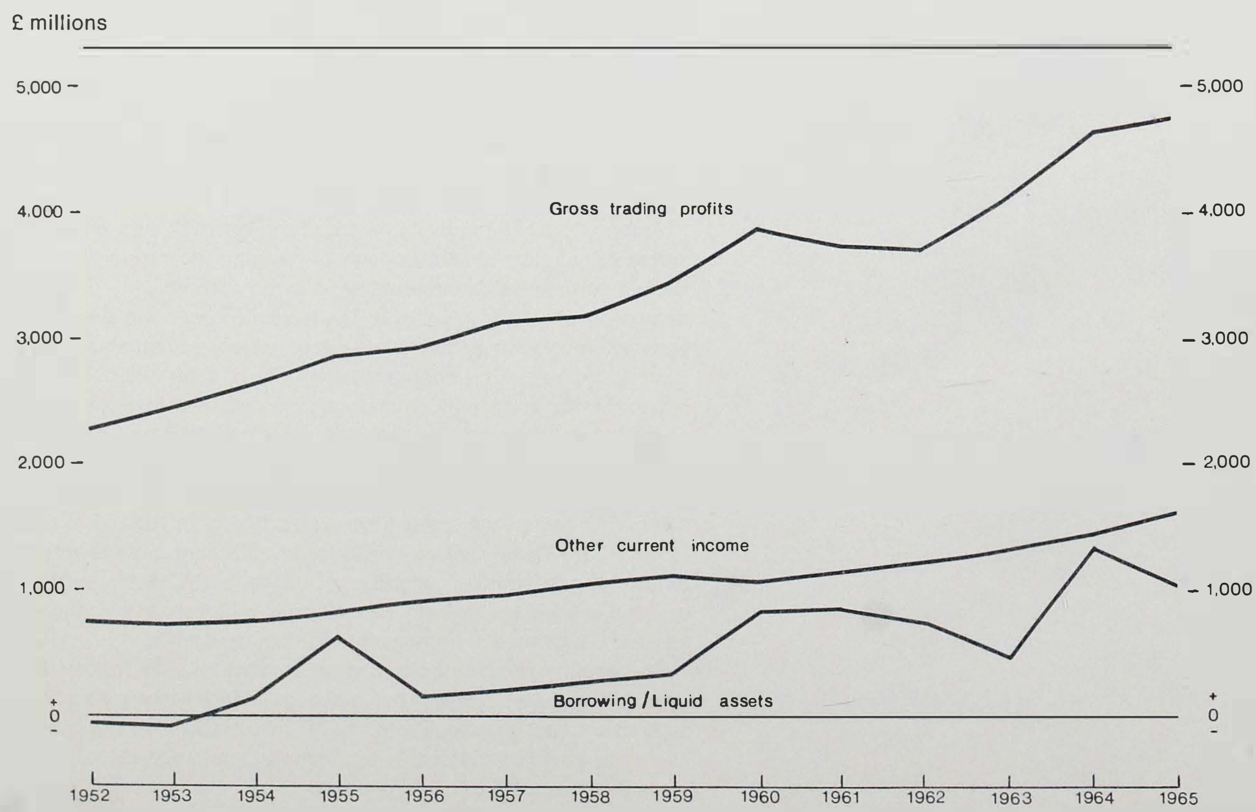
The decline in funds from internal sources relative to total funds over the period as a whole has not been steady – there has been a marked cyclical pattern. Profits have fluctuated most, but other income has changed noticeably from time to time and generally in the same direction as profits.

Table A and Chart B: Sources of funds

£ millions: percentages of total sources in italics

	Internal					External					
	Gross trading profits[a]		Other current income[b]	Total		Capital grants[c]	Overseas investment in U.K. companies	Borrowing/Liquid assets	Total		Total sources
1952	2,271	*76*	749	3,020	*101*	32	8	− 65	− 25	*− 1*	2,995
1953	2,438	*78*	720	3,158	*101*	42	13	− 85	− 30	*− 1*	3,128
1954	2,612	*73*	753	3,365	*93*	23	50	162	235	*7*	3,600
1955	2,884	*65*	807	3,691	*83*	26	97	617	740	*17*	4,431
1956	2,922	*71*	912	3,834	*93*	18	114	169	301	*7*	4,135
1957	3,115	*71*	971	4,086	*93*	11	96	196	303	*7*	4,389
1958	3,183	*68*	1,072	4,255	*91*	10	143	241	394	*9*	4,649
1959	3,443	*69*	1,112	4,555	*91*	7	117	341	465	*9*	5,020
1960	3,869	*65*	1,092	4,961	*84*	15	155	804	974	*16*	5,935
1961	3,734	*63*	1,145	4,879	*83*	9	141	849	999	*17*	5,878
1962	3,708	*63*	1,226	4,934	*84*	12	138	751	901	*16*	5,835
1963	4,072	*67*	1,338	5,410	*89*	9	200	475	684	*11*	6,094
1964	4,649	*61*	1,449	6,098	*81*	13	119	1,333	1,465	*19*	7,563
1965	4,788	*62*	1,620	6,408	*83*	20	198	1,069	1,287	*17*	7,695
Annual averages											
1952-58	2,775	*71*	855	3,630	*93*	23	75	176	274	*7*	3,904
1959-65	4,038	*64*	1,283	5,321	*85*	12	152	804	968	*15*	6,289
1952-65	3,406	*68*	1,069	4,475	*88*	18	114	490	622	*12*	5,097

a After allowing for stock appreciation but before allowing for capital depreciation.
b Rent and non-trading income in the United Kingdom and current income from abroad.
c Figures relate to all companies, because separate figures for industrial and commercial companies are not available.



The behaviour of profits has closely followed that of output in general. Before the peak of an expansionary phase has been reached, output and selling prices have tended to rise faster than costs, particularly of labour, and profits have grown rapidly. Thus between 1954 and 1955, 1959 and 1960, and 1963 and 1964, the growth of profits was unusually large – increases of approximately £270 million, £430 million, and £580 million, respectively. But when the growth of output has slowed down, margins have narrowed (probably because of rising unit costs) and profits have ceased to rise as fast, or have fallen. This can be seen in 1958 and 1961-62.

Typically, however, the years in which profits have been growing most rapidly have been those in which their contribution to the total supply of funds has contracted most. This is because expenditure in such years has risen even more rapidly (Table B), and with it the need to turn to external funds.

Similarly, in the periods when profits have grown only slowly, or have declined, their share of total resources was almost maintained. At the end of a recession in output and in the very early stages of an upturn, profits have tended to increase their share of company resources (though not by much), probably because expenditure by companies, especially on fixed investment, responds more slowly to rising output than do profits.

Uses of funds

In examining the pattern of companies' expenditure, it is convenient to distinguish between "current" uses of funds and "capital" uses. In the first category can be included payments of dividends and interest, profits due abroad, tax payments, and subscriptions to charities; and, in the second, gross fixed investment, stockbuilding, investment abroad, purchases of U.K. company securities, changes in hire purchase credit extended, and the unidentified item.[1] Details are given in Tables B and C.

Table B shows that current expenditure has accounted for a declining share of total spending over the period under review – from an average of 53% during 1952-58 to 47% during 1959-65. This reflects an absolute reduction in some current expenditure (discussed below) and also an increasing emphasis on fixed investment, which rose from 25% of the total in 1952-58 to 29% in 1959-65. To some extent this rise was associated with official measures taken to stimulate capital investment, notably by means of allowances against taxable profits – which, by reducing taxes, also helped to hold down current expenditure.

Tax allowances for wear and tear of plant and machinery are of very long standing, the statutory rates having been agreed between the Inland Revenue and industry before the war. These rates have been increased from time to time, notably in 1945 and 1963. Also in 1945 they were supplemented by initial allowances, which permit companies to set against taxable profits a larger proportion of the cost of a new asset in its first year (and less later) and thus, in effect, to delay some payments of tax. In 1954 investment allowances were introduced; these give tax relief over and above the full cost of a new asset, and effectively cancel some tax liabilities altogether. These three types of allowance have been subsequently increased and expanded, so that by 1965 total capital allowances removed the tax liability on nearly £2,000 million of companies' gross trading profits, compared with £400 million in 1952.

1 The unidentified item, as noted earlier, does not necessarily relate only to expenditure; and to the extent that it does, some of it should probably be defined as current spending.

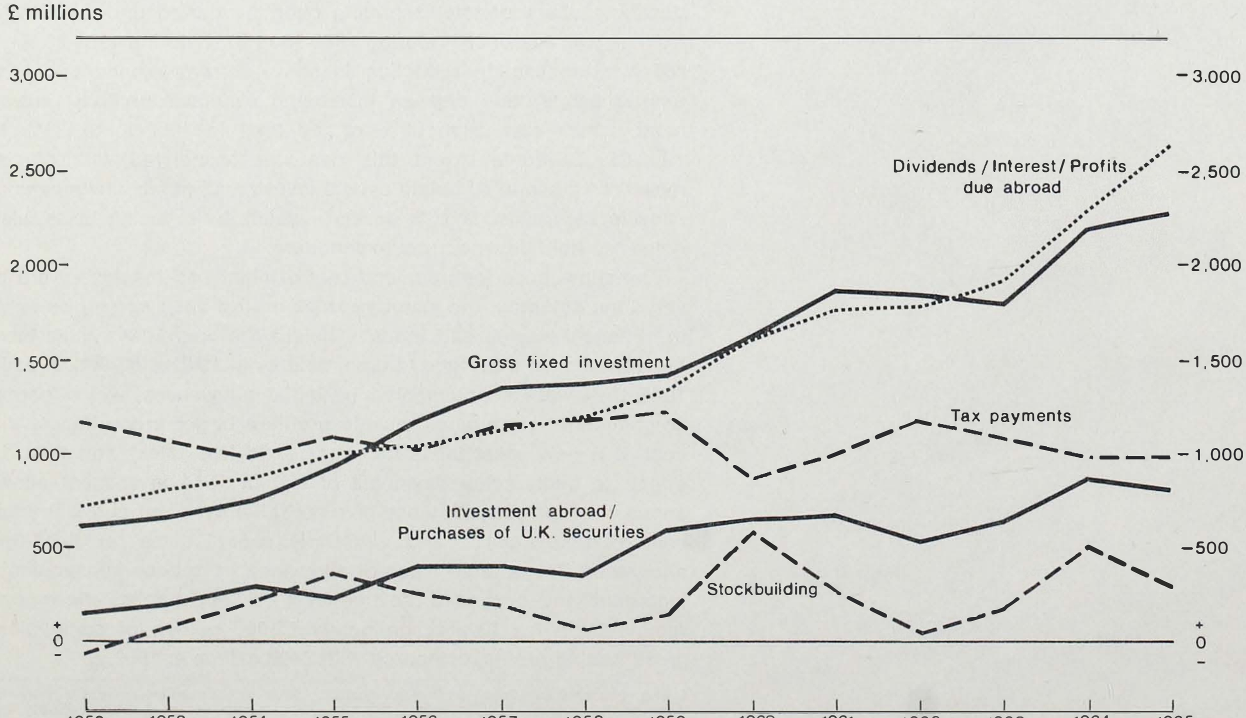
Table B and Chart C: Uses of funds

£ millions: percentages of total uses in italics

	Current						Capital				
	Dividends[a]	Interest payments/ Profits due abroad[b]	Tax payments in U.K. and abroad	Subscriptions to charities[b]	Total		Identified capital expenditure[c]		Unidentified		Total uses
1952	476	248	1,177	. .	1,901	*63*	692	*23*	402	*14*	2,995
1953	543	257	1,060	. .	1,860	*59*	930	*30*	338	*11*	3,128
1954	601	264	965	9	1,839	*51*	1,280	*36*	481	*13*	3,600
1955	662	332	1,087	9	2,090	*47*	1,482	*33*	859	*20*	4,431
1956	682	353	1,029	11	2,075	*50*	1,750	*42*	310	*8*	4,135
1957	729	388	1,143	12	2,272	*52*	1,915	*44*	202	*4*	4,389
1958	769	420	1,184	13	2,386	*51*	1,829	*39*	434	*10*	4,649
1959	878	468	1,215	15	2,576	*51*	2,215	*44*	229	*5*	5,020
1960	1,096	524	877	17	2,514	*42*	2,821	*48*	600	*10*	5,935
1961	1,232	531	978	19	2,760	*47*	2,768	*47*	350	*6*	5,878
1962	1,223	557	1,186	21	2,987	*51*	2,427	*41*	421	*8*	5,835
1963	1,300	610	1,092	24	3,026	*50*	2,644	*44*	424	*6*	6,094
1964	1,548	745	992	26	3,311	*44*	3,537	*47*	715	*9*	7,563
1965	1,733	904	988	28	3,653	*47*	3,382	*44*	660	*9*	7,695
Annual averages											
1952-58	637	323	1,092	8	2,060	*53*	1,412	*36*	432	*11*	3,904
1959-65	1,287	620	1,047	21	2,975	*47*	2,828	*45*	486	*8*	6,289
1952-65	962	471	1,070	15	2,518	*49*	2,120	*42*	459	*9*	5,097

a On ordinary and preference shares.
b Figures for profits due abroad and for subscriptions to charities relate to all companies, because separate figures for industrial and commercial companies are not available.
c Further details are given in Table C.
. . Not available.

£ millions



Current expenditure Two differing trends are apparent in companies' current expenditure. Tax payments were lower in 1959-65 than in 1952-58 and so formed a much smaller share of total outgoings (17%, compared with 28%); and dividends and interest, and profits due abroad took a larger share of the total (30%, as against 25%).

There are three main reasons for the decline in the share taken by tax. First, as noted earlier, gross profits have not grown as fast as companies' total resources. Secondly, companies distributed more of their income in the second half of the period than in the first, and so transferred to shareholders a bigger share of the total tax liability on that income. Thirdly, tax rates have fallen over the period and, as mentioned above, tax allowances against investment expenditures have increased.

Chart C shows that tax payments did not decline evenly over the period, but fluctuated considerably. The fluctuations have normally been in the opposite direction to those of profits because the tax figures represent payments, rather than accruals, of tax liabilities during each year: for example, the low tax payments in 1960 related broadly to the low profits in 1958. The lag has sometimes been helpful to companies and sometimes not; and it may well have accentuated the cyclical pattern of their capital expenditure. Thus in 1960 and 1964, when expenditure rose rapidly, financing problems were eased by the fact that the taxes due on the high profits then being earned did not have to be paid immediately. On the other hand, in 1958 and 1962, when profits were hardly rising or were falling, companies had to find the funds to discharge the high tax liabilities incurred in earlier years; and they were thereby no doubt discouraged from spending in other ways.

Interest payments (on debentures etc.) have risen slightly faster than total expenditure and therefore distinctly faster than internal sources of funds. This increase is due mainly to the rise in interest rates over the period, though to some extent it reflects heavier borrowing, particularly from banks; new issues of debentures increased faster than expenditure, but not nearly as fast as bank borrowing. Profits due to overseas parents rose in line with total trading profits.

Share dividends have grown particularly fast. The increase was not very marked before 1959; rather it was gradual with fluctuations reflecting to some extent those in profits. Companies normally wish to prevent sharp changes in payments to shareholders from year to year, and in particular are reluctant to allow dividends actually to fall; so payments tend to fluctuate considerably less than profits. Thus, in a year of sharply rising profits, dividends tend to rise less fast and, in a year of falling profits, tend to fall less, if at all. In the long term there may be some tendency for dividends to remain at a fairly constant proportion of company income – and this indeed happened in the years 1952-58.

In 1959 dividend payments rose sharply and they seem to have continued on a new path thereafter. In 1952-58 they amounted to less than 18% of funds available to companies from their internal sources; in 1959-65 this proportion had increased to 24%. Only a small part of this rise can be attributed to new equity issues; these rose broadly in line with total expenditure by companies, though rather faster than their internal funds. The change of pace probably owed something to the high incidence of take-overs towards the end of the 1950's, which made many companies less inclined to hold large reserves of financial assets. At the same time investors were paying more attention to the growth of ordinary share values, and companies which were likely to make new issues sought to maintain the status of their shares by means of increased dividends. The change was helped, too, by an alteration in the tax structure in 1958, which removed the tax discrimination against distributed profits. The introduction of corporation tax, which favours the retention of profits and the issue of loan capital rather than equities, may well encourage a return towards the previous pattern of dividend payments.

Capital expenditure Over half of total expenditure by companies is on fixed investment, which shows a strong cyclical pattern. This pattern is related to the general level of demand and the state of business expectations which, in turn, are greatly influenced by the Government's fiscal and credit policy. High activity brings large profits and the promise of maintained or rising profits in the future. Both of these will tend to encourage investment, at a time when shortages of capacity may be developing. Thus investment spending by companies has risen sharply in, or shortly after, boom years with high profits (it rose notably in 1955-56, 1960-61 and 1964-65), and has slowed down, or actually fallen, in years such as 1958 and 1962 – when there was some shortage of demand and profits were increasing less fast or had declined. Increases in initial and investment allowances (in 1954, 1958-59, and 1963) have probably stimulated expenditure on fixed investment in the up-phase of a cycle; but it is difficult to isolate their effect from the effects of variations in demand generally, or indeed, of changes in the rates of income tax and profits tax.

Stockbuilding accounts for only a small proportion of total spending, although in the latter half of the period under review, when national output was rising faster, its share increased somewhat. Of greater interest are the marked cyclical changes in stockbuilding. Stocks have generally been built up fast when output has accelerated and before expenditure on fixed investment has reached a peak; and stockbuilding has declined when the growth of output has slackened. Thus very big increases occurred in the boom years of 1955, 1960 and 1964; and only small increases in 1958 and 1962. However, annual figures mask some of the shorter-term responses of stocks to changes in output.

"Other identified" capital expenditure in Table C comprises investment abroad, cash payments to other sectors of the economy to acquire interests in other companies,[1] and changes in hire purchase credit extended. The last of these items is quite small over the whole period but there have been some sizable fluctuations around the peaks and troughs of the expenditure cycles. Such fluctuations, caused largely by official regulation of hire purchase terms, have generally been in the opposite direction to changes in total expenditure, with downward swings in 1955, 1960 and 1964-65 and upward swings in 1958 and 1962.

Expenditure on investment abroad increased from an average of £210 million a year during 1952-58 to £390 million in 1959-65. In each of these periods it represented around 6% of total expenditure, but changes from year to year have been somewhat erratic. Spending fell in 1955, 1962 and 1965 and rose sharply in 1956, 1963 and 1964. These movements have not displayed the same cyclical

1 Figures for recent years were discussed in an article "Company acquisitions" in the December 1966 *Bulletin*. Earlier figures were given in the articles "Acquisitions and amalgamations of quoted companies" in *Economic Trends* for April 1963 and November 1965.

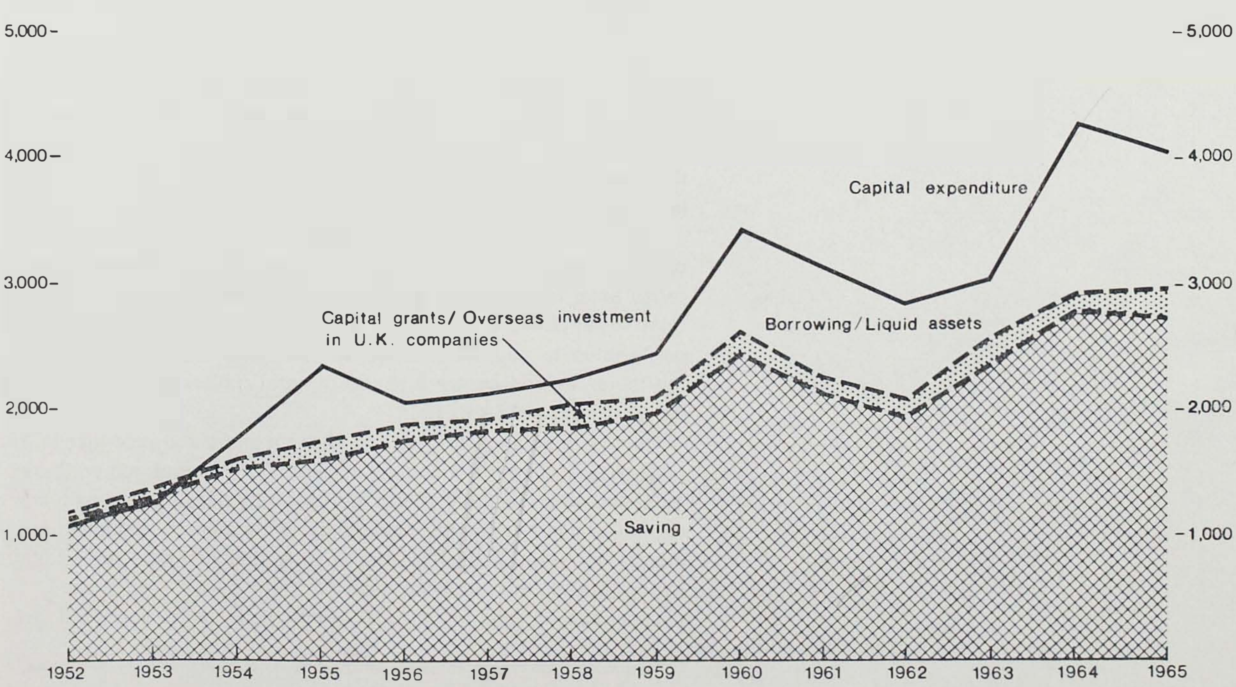
Table C and Chart D: Capital expenditure and its financing

£ millions: percentages of total capital expenditure in italics

	Capital expenditure					Financed by					
	Gross fixed investment	Stock-building[a]	Other identified[b]	Unidentified	Total	Saving[c]		Borrowing/ Liquid assets		Other[d]	
1952	605	— 63	150	402	1,094	1,119	*102*	— 65	*— 6*	40	*4*
1953	640	65	225	338	1,268	1,298	*103*	— 85	*— 7*	55	*4*
1954	750	200	330	481	1,761	1,526	*87*	162	*9*	73	*4*
1955	920	352	210	859	2,341	1,601	*69*	617	*26*	123	*5*
1956	1,160	235	355	310	2,060	1,759	*86*	169	*8*	132	*6*
1957	1,335	185	395	202	2,117	1,814	*86*	196	*9*	107	*5*
1958	1,370	64	395	434	2,263	1,869	*82*	241	*11*	153	*7*
1959	1,426	134	655	229	2,444	1,979	*81*	341	*14*	124	*5*
1960	1,622	569	630	600	3,421	2,447	*71*	804	*24*	170	*5*
1961	1,848	270	650	350	3,118	2,119	*68*	849	*27*	150	*5*
1962	1,847	45	535	421	2,848	1,947	*68*	751	*27*	150	*5*
1963	1,802	194	648	424	3,068	2,384	*78*	475	*15*	209	*7*
1964	2,180	502	855	715	4,252	2,787	*65*	1,333	*32*	132	*3*
1965	2,280	298	804	660	4,042	2,755	*68*	1,069	*27*	218	*5*
Annual averages											
1952-58	969	148	295	432	1,844	1,569	*85*	176	*10*	98	*5*
1959-65	1,858	288	682	486	3,314	2,345	*71*	804	*24*	165	*5*
1952-65	1,414	218	488	459	2,579	1,957	*76*	490	*19*	132	*5*

a Value of physical increase in stocks and work in progress.
b Investment abroad, purchases of U.K. company securities, and changes in hire purchase credit extended.
c After providing for stock appreciation but before providing for capital depreciation.
d Government grants to, and overseas investment in, U.K. companies.

£ millions



pattern as have several other forms of capital expenditure, especially stockbuilding and fixed investment in the United Kingdom. This is because there are some volatile elements in investment abroad which are not dependent on the level of domestic activity. Thus the fall in 1962 and the rise in 1964 owed much to changes in investment by the oil companies, and the fall in 1965 followed government restrictions.

Take-overs assumed increasing importance throughout the 1950's, when profits tax generally discriminated against dividend distributions and companies ploughed back a high proportion of their profits. For an individual company, the take-over of another company, like fixed investment in the United Kingdom or direct investment abroad, is a means of increasing the productive assets under its control. For the company sector as a whole, however, take-overs and mergers do not increase the volume of such assets – except to the extent that unincorporated businesses are taken over – though in some cases existing assets may be used more efficiently when organised into larger units. For the company sector as a whole, cash payments for take-overs are, in effect, a capital distribution to some shareholders, while shareholders as a body continue to own the same volume of productive assets as before.

By 1959 cash purchases of other company securities had risen to some £250 million a year. They stayed around that figure until 1964, when they rose to nearly £400 million. Over the seven years 1952-58 such purchases totalled only about £550 million, 2% of total expenditure by companies; but in 1959-65 the figure rose to some £2,000 million, nearly 5% of total expenditure.

Company saving and capital expenditure

In order to examine more closely the trend and cyclical variations in capital expenditure and its financing, it is useful to calculate net saving, that is the excess of internal funds over current expenditure. This is done in Table C, where the total of capital expenditure (as already defined) is matched by saving, capital grants from the public sector, overseas investment in U.K. companies, and borrowing less additions to liquid assets. The figures are illustrated in Chart D.

Total capital expenditure has risen quite steeply over the fourteen years – the average in 1963-65 was 85% higher than in 1954-56, compared with a rise of 70% in the value of the gross national product – and its course has been marked by very strong cyclical fluctuations. There were peaks in 1955, 1960 and 1964 and troughs in 1956-59 and 1962-63.

Stockbuilding has been the largest single influence on the cyclical pattern of the total but, as Table C shows, expenditure on gross fixed investment has also grown rapidly in the peak years for total expenditure – especially in 1964 – and the unidentified item contributed to each of the peaks. "Other identified" expenditure in the table[1] moved contrary to the general pattern in 1955 and 1960, though in line with it in 1964.

On the financing side, saving did not increase very fast in 1955 but it was an important source of funds for the peak expenditures in 1960 and 1964. In 1963 saving increased by nearly twice as much as capital expenditure, and companies were able to reduce their demands on the capital market and to conserve funds for additional expenditure in the following year.

Overseas investment in U.K. companies and government grants

1 Companies' investment abroad, their purchases of U.K. company securities, and their extension of hire purchase credit.

Table D: Borrowing and transactions in liquid assets

£ millions: percentages of capital expenditure in italics

	Borrowing: Capital issues: Ordinary and preference shares	Borrowing: Capital issues: Other	Borrowing: From banks	Borrowing: Other[a]	Borrowing: Total		Net acquisitions of liquid assets[b]		Borrowing less net acquisitions of liquid assets	
1952	96	39	−240	65	− 40	*− 4*	25	*2*	− 65	*− 6*
1953	57	58	− 50	30	95	*7*	180	*14*	− 85	*− 7*
1954	74	83	145	60	362	*20*	200	*11*	162	*9*
1955	132	105	70	120	427	*18*	−190	*− 8*	617	*26*
1956	132	57	60	10	259	*12*	90	*4*	169	*8*
1957	126	155	10	70	361	*17*	165	*8*	196	*9*
1958	73	118	175	90	456	*21*	215	*10*	241	*11*
1959	142	109	235	140	626	*26*	285	*12*	341	*14*
1960	242	77	380	140	839	*25*	35	*1*	804	*24*
1961	320	109	255	130	814	*26*	− 35	*− 1*	849	*27*
1962	155	161	280	75	671	*24*	− 80	*− 3*	751	*27*
1963	128	202	468	75	873	*28*	398	*13*	475	*15*
1964	165	241	697	157	1,260	*30*	− 73	*− 2*	1,333	*32*
1965	49	357	469	251	1,126	*28*	57	*1*	1,069	*27*
Annual averages										
1952-58	99	88	24	64	275	*15*	98	*5*	176	*10*
1959-65	172	179	398	138	887	*26*	84	*2*	804	*24*
1952-65	135	134	211	101	581	*22*	91	*3*	490	*19*

a From other financial institutions and from the public sector.
b Notes and coin, bank deposits, deposits with hire purchase finance companies and building societies, tax reserve certificates, marketable government debt and local authority debt.

(the financing column headed "other" in Table C) have together grown at the same rate as capital expenditure, and have usually fluctuated in line with it. In 1964, however, income from this source declined, and companies needed to raise more in the capital markets.

Borrowing and changes in liquid assets

Table D provides an analysis of companies' borrowing and transactions in liquid assets. Over the fourteen years 1952-65 companies have borrowed – by capital issues, from banks, and in other ways – nearly £8,200 million, 22% of their total capital requirements. At the same time, however, they have increased their liquid assets by £1,275 million, equivalent to 3% of their capital expenditure. So, on balance, they have drawn from the markets about 19% of their capital needs. Over the first seven years this proportion was 10% but over the last seven it increased to 24%; and in 1964, when expenditure was at its highest, it was as much as 32%.

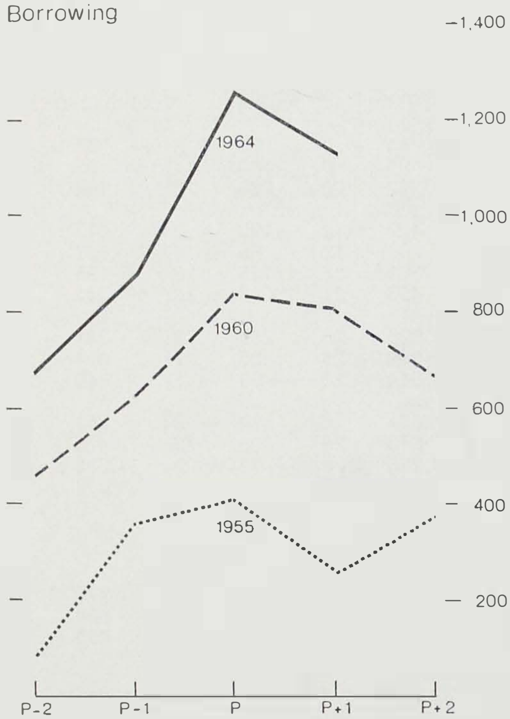
Nearly one half of total borrowing over the fourteen years was on capital issues. New issues in the second half of the period were nearly twice as heavy as in the first, but there was little change in the proportion of total capital expenditure financed in this way. Similarly, the proportion of capital expenditure financed by borrowing from institutions other than banks[1] remained broadly constant

1 "Other" borrowing in Table D.

Chart E

£ millions

Borrowing

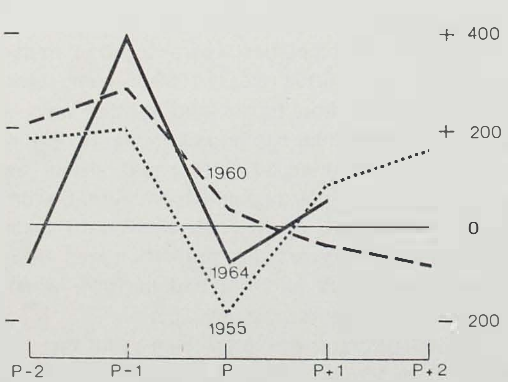


P represents peak year for expenditure.

Chart F

£ millions

Liquid assets



P represents peak year for expenditure.

(at about 4%) during each half of the period. Bank borrowing, however, was very largely concentrated in the second seven years, when it represented nearly one half of total borrowing and equalled 12% of total capital expenditure.

By contrast, companies added less to their holdings of liquid assets in the second seven years than in the first; and because they were failing to maintain the build-up of these assets, they were better placed to accelerate their capital expenditure.

Charts E and F show the pattern of borrowing and transactions in liquid assets over the cyclical peaks in expenditure in 1955, 1960 and 1964. Companies built up their liquid assets at a fast rate before expenditure reached its peaks but added little to these assets, or reduced them, in the peak years and immediately afterwards. They increased their borrowing sharply both before and during the peak years for expenditure, but thereafter borrowed less.

This pattern, and the greater reliance on borrowing from 1959 onwards, owes much to official control of credit. Capital issues were subject to control up to the beginning of 1959 – though, as noted above, there was no significant increase in the proportion of capital expenditure financed by capital issues in 1959-65. Bank advances were subject to a degree of direct restraint throughout practically the whole of the period from 1952 to 1958, restrictions being tightened in 1955. After 1958 advances were free from direct control except between mid-1961 and mid-1962, and after the end of 1964; and the only other period when they were controlled (indirectly, through calls for Special Deposits) was from mid-1960 to mid-1961. Thus, whereas in 1955 companies borrowed less from the banks than in 1954, they were able to go on expanding their bank loans in 1960 and 1964, and only in 1961 and 1965, when direct controls were in force, did the rate of increase fall away. They made good some of the reduction in bank facilities in these years by turning to capital issues, which were higher in 1961 than in 1960 and as high in 1965 as in 1964.

Summary and conclusions

There is a fairly clear and consistent pattern in the cyclical movements of companies' income and expenditure.

During a recession, as unemployment has increased, official curbs on spending have generally been removed. As demand and output begin to pick up, the labour force employed is still relatively small, and productivity rises. So do company profits, and companies, having discharged in the recession year the heavy tax liabilities incurred before profits had started to fall, become more confident about the future. They see the prospect of a continuing rise in demand and profits, and an end to the shortage of liquidity from which they have suffered at the peak of the previous expansion and during the recession. The next tax bill is likely to be smaller than the last one, and controls on borrowing have been removed.

In these circumstances, companies may well increase their dividend payments – if only to prepare the market for new capital issues. Increased borrowing, on capital issues and from banks, is needed partly to relieve the pressure on liquid assets – which have been run down in earlier years when expenditure has been exceptionally heavy, when profits have been falling, and when borrowing has been restricted. But companies also start rebuilding their stocks of materials and adding to their work in progress, and they begin to reconsider the investment plans shelved when the outlook was less encouraging.

At the next stage, at least in the 1960 and 1964 cycles, demand has increased so fast that domestic productive capacity has been strained. Wage costs have risen sharply, reducing profit margins or raising domestic prices; delivery dates have lengthened; and the balance of payments has swung into deficit. Companies have financed their increasing expenditure out of rising profits and by heavy borrowing and also by reducing their liquidity. Meanwhile the authorities have been concerned to damp down demand, and companies' income and expenditure, and economic activity in general, have begun to slow down again. Some sources of borrowing have been restricted by official action but companies have borrowed where they could and have started to augment their depleted liquid assets.

The cyclical fluctuations in income and expenditure have been much more marked in the second half of the fourteen-year period than in the first. On the same comparison, companies have earned a lower current income in relation to their total expenditure but they have distributed more to shareholders; and they have taken up fewer financial assets and increased their borrowing. This borrowing has not been subject to the same persistent official control since 1958 as before, but official restrictions have at times been severe. Thus in the more recent years, when the supply of market funds has been more volatile, companies have become more dependent on them. Nevertheless, they have managed to obtain sufficient funds to enable them to sustain a higher ratio of capital expenditure to total national expenditure than in the first half of the period.

Definitions

Industrial and commercial companies

These are as defined on page 25, and in the *National Income and Expenditure Blue Books* (issued by the Central Statistical Office). They comprise all corporate bodies in the United Kingdom other than public corporations, banks and other financial institutions. During the period under review the denationalisation of steel meant that some bodies, previously classed as public corporations, were reclassified as industrial and commercial companies. The effect on the figures used in this article, however, is quite small.

Sources of funds

Gross trading profits are those earned in the United Kingdom only. These are shown net of stock appreciation but gross of capital depreciation, because this article is concerned with flows of funds rather than with the revaluation of assets.

Current income from abroad includes profits earned abroad as defined in the *National Income and Expenditure Blue Books i.e.* they are gross of stock appreciation but net of depreciation allowances, and they include some profits not actually remitted to the United Kingdom. The related *investment abroad* – shown under uses of funds – is similarly net of depreciation, and includes the reinvestment of unremitted profits.

Overseas investment in U.K. companies comprises gross long-term investment in this country (direct, oil and miscellaneous, but excluding overseas purchases of share and loan capital – which are presumed to have been made from persons or financial institutions rather than from industrial and commercial companies). See also the note on *profits due abroad.*

Uses of funds

Payments of *dividends and interest* are calculated gross of U.K. tax; and *taxes* exclude U.K. tax deducted from dividends and interest. Figures for taxes show payments rather than accruals of tax.

Profits due abroad are net of U.K. tax and of capital depreciation allowances. They comprise profits due, but not remitted, to overseas parent companies. The reinvestment of these profits is included, net of depreciation, under *overseas investment in U.K. companies* (in sources of funds).

Investment abroad comprises gross long-term investment (direct, oil and miscellaneous, including share and loan capital) plus, from 1958 onwards, net short-term investment abroad (*e.g.* trade credit extended less such trade credit received). Figures of short-term investment abroad before 1958 are not available. See also the note on *current income from abroad.*

Hire purchase credit extended does not include credit extended by hire purchase finance companies, which are classed as financial institutions and not as industrial and commercial companies.