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Recent Instalment Credit Developments in Britain

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Recent Instalment Credit Developments in Britain

Alfred P. Johnson*

Direct controls over instalment credit were reimposed in the United Kingdom on February 24, 1955, after earlier controls, instituted in February 1952 had been repealed in July 1954. This action was taken as part of a general move by the monetary authorities to restrain credit and moderate excessive demand with a view toward improving the U. K. trade balance.

The recent weakness in the trade balance was in part due to a substantial rise in consumption during 1954. Expenditures for cars and motoring and for household goods, for example, increased during the year by 19 and 10 per cent, respectively. ^{1/} During 1954, instalment credit also grew rapidly both in the regulated period prior to July and in the following unregulated period. The growth in instalment credit is a reflection of the increased demand for consumer goods by the British public, the increased supply of these goods available in the domestic market, and the changed attitude of the consumer toward the use of instalment credit. Since it is expected that all of these factors will, to a degree, continue to operate in the immediate future the return to direct regulation probably will restrain the rate of expansion rather than actually reduce the level of instalment credit.

Instalment credit regulation in 1952-54

Prior to the summer of 1954, instalment credit was regulated by (1) control over credit terms, and (2) restrictions on funds to finance instalment credit. On July 24, 1954, the restrictions on credit terms were removed and on August 21 those limiting financing for instalment credit firms were virtually abandoned.

The restrictions on hire purchase terms represented the continuance of an order introduced in February 1952. Under this order, some 30 kinds of categories of articles were subject to regulation, including motor vehicles, motor and pedal cycles, radio and television sets, phonographs, refrigerators, and vacuum cleaners. The order did not regulate hire purchase sales of furniture or instalment cash loans but certain nonconsumer goods, such as trucks and office equipment, were regulated. All items listed in the order were subject to a minimum down payment of 33-1/3 per cent and a maximum period of repayment of 18 months, except for bicycles where the down payment was 25 per cent and 12 months to repay. The required minimum down payment for any article could be in cash or trade-in.

The British authorities also acted to limit funds to finance hire purchase credit. The Capital Issues Committee was instructed to refuse permission for any new issue to be used for hire purchase finance purposes. However, the Committee's authority extended only to issues over 50,000 pounds and, while this order slowed up the development of the big finance houses, it stimulated the start of small firms. ^{2/}

^{1/} Economic Survey 1955, p. 21.

^{2/} "Hire Purchase Finance," The Financial Times, August 21, 1954, p. 1.

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Growth of consumer credit

Despite these regulations, hire purchase credit increased markedly during early 1954 and accompanied a general expansion in consumption expenditures which resulted from the higher levels of disposable income. The credit expansion in 1954 reflected increases in both the purchases of consumer durable goods and in the proportion of such purchases financed by credit. The larger supply of durables resulted not only from the expansion in production of these goods but also from an increase in the percentage allocated to the domestic market. Production of passenger automobiles, for example, was about 75 per cent higher in 1954 than in 1952 and exports accounted for only 52 per cent of total production of passenger cars in 1954 as compared with 62 per cent in 1952, as may be seen in Table I. Earlier in the postwar period, the supply of consumer durables was severely restricted in the interest of expanding exports.

Table I 1/

Production and Export of Passenger Automobiles

	Passenger car and chasis		Ratio: Exports to total production
	Total production	Export	
Monthly average			
1951	39,660	30,552	77
1952	37,334	22,945	62
1953	49,567	26,121	63
1954	64,097	33,158	52
1954 - January	53,504	24,690	46
February	56,130	27,816	50
March	73,534	41,731	57
April	58,224	32,759	65
May	64,522	37,602	58
June	73,566	40,744	55
July	62,641	32,914	53
August	49,060	27,677	56
September	58,155	30,488	52
October	64,990	28,882	44
November	78,860	34,808	44
December	75,979	37,785	50
1955 - January	69,146	33,541	49
February	71,682	34,435	48
March	93,142	45,458	49

1/ Table based on estimates prepared by the British Central Statistical Office and published in the Monthly Digest of Statistics.

Production of all major appliances also increased in 1954. Smaller appliances such as electric irons and cookers, in most cases, showed even greater gains than did larger appliances. The rate of production accelerated in the latter part of the year in response to an increase in demand which followed abolition of hire purchase restrictions. Increases in production for the last five months of 1954 over the comparable period in 1953 ranged from 9 per cent for television receivers to 77 per cent for radios.

Sales of electrical and household goods for the last five months of 1954 were 21 per cent higher than for the comparable period a year earlier. Sales of television sets reached a record level for the year, and reports indicate that during the latter months two-thirds of the sets sold were bought on hire purchase terms. 1/ The third quarter of the year, usually a slack period for appliance manufacturers was, in 1954, the most profitable in the history of many companies. 2/

Monthly figures on number of hire purchase contracts written shown in Table II indicate the extent of the expansion of automobile and motorcycle credit. In 1954, hire purchase sales of new cars were almost twice, and those of used cars more than 1-1/2 times, as high as in 1953. Consequently, in 1954, hire purchase sales accounted for 14 per cent of all new car registrations as compared with 9.1 per cent in 1953. During the first quarter of this year, hire purchase sales continued at exceptionally high levels.

Data on the amount of consumer credit extended or outstanding in Great Britain is fragmentary, however, it is believed that total instalment credit increased about 100 million pounds during 1954. Outstanding instalment credit was estimated at between 350 and 450 million pounds, about 3 per cent of disposable income. 3/

The recent rapid growth of instalment credit represented a shift in the attitude of the British consumer toward the use of instalment credit as well as a change in his consumption pattern to include more durable goods. This gradual change in attitude is described in the London Times in these words:

"Before the war, generally speaking, the middle-class could manage to save up to buy the half luxuries and conveniences that they wanted...Hire purchase, then, was a working-class device (house buying apart) for obtaining, not luxuries or even semi-luxuries, but such necessities as furniture. Not to put too fine a point on it, at that time hire purchase was of the class stigmata."

1/ "Growth of Hire Purchase Trade," The Financial Times, November 18, 1954, p. 1.

2/ The Financial Times, November 18, 1954, p. 1.

3/ The Economist, February 5, 1955, p. 472.

Table II

Number of Hire Purchase Agreements Signed During Month 1/

	Private Cars		Motorcycles	
	New	Used	New	Used
Monthly average				
1951	756	6,216	3,922	3,725
1952	1,171	7,549	3,849	4,618
1953	2,207	13,971	2,684	8,559
1954	4,399	21,122	3,746	10,501
1954 - January	2,997	14,219	2,002	5,696
February	2,873	14,307	2,018	6,094
March	4,746	20,881	4,053	10,095
April	4,677	22,254	4,890	12,411
May	4,099	23,169	4,917	12,813
June	3,973	22,911	4,509	12,021
July	4,536	25,728	4,977	13,372
August	3,045	26,208	4,449	13,287
September	4,396	23,410	3,757	12,735
October	4,784	21,254	3,553	11,294
November	6,848	19,810	3,228	8,914
December	5,820	19,312	2,592	7,275
1955 - January	6,069	18,026	2,887	6,737
February	6,754	22,507	4,123	11,032

1/ Figures supplied by H. P. Information, Ltd.

"Today it is a different story. The post-war middle class...are not buttressed by capital, and have little opportunity to save for expensive gadgets that make life easier or more agreeable. At the same time, the artisan and clerical class have a few shillings to spare each week after their necessities have been bought. So it is that two broad bands of the population have a small surplus of weekly or monthly income that enables them to enter confidently into a hire purchase agreement for the ever-increasing variety of consumer goods that are being made available...The class tincture of being a hire purchaser has vanished altogether. To all social grades it seems a common sense way of "saving"--and of coming into an inheritance of contemporary boons the moment the deposit is made." 1/

In Great Britain, durable goods are fast becoming "conventional necessities" rather than "luxuries." The desire to acquire these goods has apparently provided an incentive to workers and consumer credit the means to make their demand effective. As The Economist states:

1/ The Financial Times, June 10, 1954, p. 1.

"Consumer credit...shows signs of being precisely the sort of dynamic influence that the country so badly needs. By almost universal testimony, one of the reasons for the strange and striking sluggishness and leisure-mindedness of the British economy in these post-war years has been the lack of incentive to the individual worker." 1/

At the same time, this may also account in part for the recent rise in over-all British output and productivity. Mr. Fry, for example, has reported that:

"In the cities and towns where the ambition to own "durable consumer goods" has been thoroughly aroused, almost every working-class household seems to have some commitment to pay instalments. It may be for a television set, for furniture, carpets, refrigerators, electric wash boilers, a bicycle, or even a car."

"A workman who agreed that this was true said calmly: 'When a chap wants a TV he finds a job for his wife.' It is because of the hire-purchase instalments that women in one area demanded to be allowed to work $5\frac{1}{4}$ hours a week. Many men are said to have more than one job. If the regular job stops at four or five o'clock, they do another two or three hours in the evening and "help out" somewhere at the week-end." 2/

Financing the increased volume of hire purchase

Between 1952 and August 1954, the funds necessary to finance hire purchase were obtained partly from the small finance houses not subject to the sanctions of the Capital Issues Committee and from the increased use of unrestricted short-term funds by hire purchase houses. 3/ The latter seems to have been the predominant source of funds prior to the restrictions of hire purchase finance, enacted in 1952.

On August 21, 1954, Mr. Butler, Chancellor of the Exchequer directed the Capital Issues Committee not to impose a rigid ban on the raising of finance for hire purchase. He asked the Committee, "to deal with hire purchase applications on their merits, having regard to the purposes for which the money is raised, and bearing in mind the general consideration that an increase in the volume of hire-purchase finance leading to an excessive expansion of consumer credit would not be in the national interest." 4/ The Treasury asked the banks to apply similar principles when considering applications for advances to finance hire-purchase business.

1/ The Economist, February 26, 1955, p. 688.

2/ "Men at Work," Manchester Guardian Survey of Industry, Trade and Finance, 1955, p. 24.

3/ "Credit for Everyman," The London Times, September 23, 1954, p. 7.

4/ "Hire Purchase Finance," The Financial Times, August 21, 1954, p. 1.

In addition to the funds provided by the larger hire-purchase houses and the steadily increasing number of smaller firms, credit was supplied by retailers in undetermined amounts. Little is known about the financial structure of these stores. The Statist comments as follows:

"At present nobody outside the companies has any conception of the amount lent by them for hire-purchase trading. In banking statistics they appear as shops and stores...Further, it is virtually impossible to begin to calculate the extent to which their hire purchase is financed by their own suppliers on bills of exchange or open account, on terms imposed by them in their own particular buyers' market...It would also be interesting, though impossible, to learn how much money the manufacturers and suppliers borrow from their own bankers whilst they are awaiting payment of six months' bills or running accounts." 1/

The retailer engaged in instalment business may secure funds by: (a) selling the paper outright to the finance house (currently the most common method), (b) getting the finance house to agree to block discount a proportion of Hire Purchase contracts (becoming more popular), and (c) obtaining an advance from the bank. Assuming a retailer can secure a bank loan, it is much cheaper to obtain funds from a bank than a finance house. Bank over-draft charges of 4 to 5-1/2 per cent per annum 2/ compared favorably with finance house charges of 5-9 per cent flat rate. The rate charges for credit by the retailer (which includes not only interest but also the cost of credit investigation, accounting, and collection) varies from shop to shop. A general statement, however, might be that the charge for credit varies inversely with the cost of the good. Thus, the average charge on most household goods is 5-9 per cent, on radio and TV sets 10-12-1/2 per cent, and on bicycles 15-20 per cent. 3/

Banks in Great Britain do not participate in consumer instalment credit business directly but provide overdraft facilities to the specialized institutions operating in the field. Thus, when the Commercial Bank of Scotland recently acquired the whole of the share capital of the Scottish Midland Guarantee Trust, Ltd., a company engaged in hire purchase business, it caused something of a stir in banking circles in Britain and revived the controversy over the role of the commercial banks in the country's economic life. The governor of the Scottish bank argued that the acquisition of this institution will make it possible to convert indirect lending back to direct lending without in any way overstepping the traditional borderlines of safety and liquidity. 4/

It is believed in some quarters that the easing of controls on hire-purchase finance was a more important factor in the increased expansion of hire purchase credit than the lifting of regulation over down payments and maturities.

1/ "Hire Purchase and The Shopkeeper," The Statist, March 12, 1955, p. 353.

2/ These rates were in effect prior to the rises in the Bank of England's discount rate in early 1955.

3/ "The Cost of Hire-Purchase," The Financial Times, January 24, 1955, p. 4.

4/ "The Banks in Hire Purchase," The Financial Times, December 17, 1954, p. 6.

Return to regulation

On February 24, 1955, controls on hire purchase were reimposed. In his announcement in the House of Commons, Mr. Butler stated, "The Orders are designed to deal with the immediate situation, but it is the Government's intention, as soon as opportunity offers, to seek permanent powers for this purpose." The regulation specified down payments of 15 per cent and maximum maturities of 24 months for most types of controlled goods. For the most part, the categories of goods previously controlled and mentioned above were again regulated. The main additions were furniture, jewellery, and cameras.

Mr. Strauss, the Parliamentary Secretary to the Board of Trade stressed the differences between the present Order and the one in effect last July:

"...The range of the goods now covered is wider, but the terms are less onerous. The deposit is 15 per cent instead of what was usually in the former Orders, namely one-third. The period for payment is normally two years instead of 18 months. It is four years in certain cases--cookers, water heaters, and wash boilers.

"The need for this Order does not now rest, as did the former, on the need for restricting the use of metal-using goods that were required for defense and export. The aim of the present Order is to reduce internal demand roughly over the whole field of durable consumer goods." 1/

In early March, the banks agreed as to how they should interpret the Government's request for restraint in granting credit to finance hire-purchase transactions. The president of the British Bankers Association advised member banks: (1) to grant no additions to the credit lines already outstanding in favor of hire purchase finance houses, and (2) not at present to consider hire purchase finance from new customers. It is believed that bank advances for hire purchase increased 50 per cent in the last quarter of 1954 and the total trebled during the year. 2/ These estimates, moreover, would not reflect advances granted to customers of the banks for providing extra working capital but utilized by the recipients to finance hire purchase.

Effect of the regulation

The British Government has indicated that it regards hire purchase regulation primarily as a supplementary anti-inflationary measure. By reducing domestic demand for the regulated consumer goods, it is hoped that additional resources will be channeled into export trade. Although exports

1/ Hansard, 22 March, 1955, column 2032.
2/ Hansard, 22 March, 1955, column 2034.

of automobiles, radios, television receivers, and washing machines increased during 1954, the ratio of goods exported to total production declined in all cases. The February 26, 1955 issue of the Economist states as follows with respect to the effects of hire purchase regulation on exports:

"It so happens that many of the goods that are bought on hire purchase---motor cars, household appliances and so on---are either goods that could be exported or else goods that are made by workers who could find employment in similar export trades. Many of the goods and services to which demand might be diverted now that hire purchase is to be slowed down, on the other hand, are natural absorbents of inflation, which can suck in a flood of purchasing power with little transfer of real resources from other employment...If a man switches his furniture money to beer and cigarettes, he adds to Exchequer revenue by far more than he diverts brewers from exporting or draws dollar tobacco from stock...If he goes more frequently to the cinema or the greyhound stadium, he makes more intensive use of these underfilled pieces of capital equipment;..." 1/

The initial reaction of producers and retailers to the new order was that the present level of hire purchase would probably not be depressed to any great extent although they agreed that any further expansion would be checked; the main effect would be on traders, such as furniture dealers,2/ who have been offering "no deposit" terms with repayment periods up to three years.

Such information as is available for the period of regulation seems only in part to substantiate the first reaction. Reports from the furniture trade indicate sales declines of between 20 and 30 per cent. Sales of radios and televisions have also declined somewhat. 3/ On the other hand, credit to finance sales of new and used passenger cars has continued to increase, but the rate of expansion appears to be declining somewhat. The number of hire purchase agreements signed in March was considerably above the number signed in February; however, while the number reported in February was 70 per cent above a year ago, the number in March was 49 per cent above the corresponding month of 1954.

Conclusions

Consumer credit has been developing rapidly not only in Great Britain but also in several other countries of Western Europe and has been a factor in the expansion of purchases of durable goods in that area. In European countries the relationship of consumer credit to disposable income is still low relative to the United States; however, the trend toward increased use of consumer credit is expected to continue. As a result of

1/ The Economist, February 26, 1955, p. 687.

2/ Business Credit, April 1955, p. 1.

3/ Business Credit, May 1955, p. 13.

this trend, interest in consumer credit has been stimulated, especially with respect to its impact on the trade balance. To relieve trade balance pressures, Denmark, in addition to Great Britain, has imposed controls over consumer credit, while Belgium is presently reviewing the feasibility of such measures.

The effect of consumer credit on the balance-of-payments-position and the need for control vary by country depending upon the stimulus this type of credit provides durable goods purchases, the extent to which it diverts goods from export into the domestic market, and the domestic availability of raw materials and production facilities.