

Financial Accounts

United Kingdom 1993

Financial institutions in the United Kingdom considerably developed their financial activity during the past decade. This development took place at a steady pace in a context of financial deregulation. As far as financial flows are concerned, 1993 was especially remarkable, however, given the level of transactions in securities, term saving and foreign currency deposits undertaken by the *credit institutions*. As in the previous years, insurance companies increased their technical reserves and were heavily involved in the securities market.

On the borrowers' side, the financial deficit of *general government* has increased during the period 1989-1993 and has reached the equivalent of 7.5% of GDP in 1993 mainly because of growing health expenditure¹.

In contrast, *non-financial corporate and quasi-corporate enterprises* have continued the process of improving their finances since 1990 by year, reducing their deficit to a mere 1.2% of GDP in 1993.

On the lenders' side, the recovery in consumer confidence took the form of a fall in the savings rate and in investments. Therefore, the net lending of *households and private non-profit institutions serving households* declined in 1993. Nevertheless, it still accounts for 5.8% of GDP in 1993.

After some methodological notes aimed at facilitating the interpretation of this publication's data, a brief analysis of the financing of the British economy as a whole in 1993 is followed by comments on each institutional sector.

Methodology

Eurostat ensures that the financial accounts of the European Union Member States are in compliance with the European System of Integrated Economic Accounts (ESA)^{2,3}. These accounts permit the analysis of the structure and changes in the financing of the national economies, on the basis of internationally standardised classifications.

The financial accounts are the financial part of National accounts. They reflect all the transactions carried out by the institutional sectors during a reference period. Each financial transaction appears as the counterpart of an other transaction. This latter may be a transfer of goods and services, a distributive transaction or an other financial transaction. Financial transactions are expressed in terms of transaction prices.

Changes in assets and changes in liabilities are separately registered. Consequently, an increase in resources will be recorded differently if it arises from a new debt contracted (increase in liabilities) or from a redemption of assets (reduction in assets).

Financial accounts data record the transactions leading to changes in assets and liabilities (flows in assets and liabilities). Therefore, they differ from balance sheet changes in assets and liabilities (difference between opening and closing balance). The latter may encounter certain modifications not based on transactions (losses, revaluations of physical capital, etc.). Nevertheless in practice, compilers of national accounts often use changes in balance sheet statistics to derive some financial

accounts items.

Moreover, despite the consistency that exists between the financial and non-financial area of national accounts, recording procedures used frequently result in statistical discrepancies. For each sector, an additional adjustment item is needed to link the net change in financial assets and liabilities in the financial account to the balance of the capital account (net lending/borrowing).

Financial accounts have a specific arithmetic:

- the ESA recommends the consolidation of all financial transactions in each sector, except for transactions in securities (F40, F50 and F60) which are never consolidated. Nevertheless, data communicated to Eurostat are often non-consolidated. In this case, the total of financial transactions carried out by an institutional sector is equal to the sum of financial transactions undertaken by the sub-sectors of which it is composed;
- for each financial transaction there must be symmetry between changes in assets and in liabilities;
- by taking the *rest of the world* into account, the net changes of assets and liabilities of all economic sectors must be equal to zero. As certain operators are overall lenders and others borrowers, the general balance is established when the sum of the former's net lending is equal to the sum of the latter's net borrowing.

Specific national characteristics

The methodological framework in which UK's financial accounts are elaborated is not exactly that recommended by the ESA-1979⁴.

Classification of institutional sectors

The conversion of British statistics to ESA definitions involves regrouping institutional sectors (see table 1).

The ESA sector of *non-financial corporate and quasi-corporate enterprises* (S10) is defined as the sum of the industrial and commercial companies sector and the public enterprises sector.

There is no separate sector for central banking authorities. The Bank of England is divided into two departments: the Banking Department, which comes under the *other monetary institutions* sector (S42), and the Issue Department, which comes under *central government* (S61). Therefore, bank notes issued by the Bank of England are recorded as a liabilities flow of the central administration.

Besides the Issue Department of the Bank of England, the central administration sector includes bodies which are recorded differently under the ESA classification:

- (a) the Exchange Equalisation Account, which holds the British official reserves,
- (b) the Social Security Fund,
- (c) the ordinary and investment accounts of the National Savings Bank.


Private non-profit institutions serving households are presented together with *households* (S70/S80).

Classification of financial instruments

Statistics communicated to Eurostat by the United Kingdom do not allow the separate showing of:


- (a) *special drawing rights* (SDRs) (F10),
- (b) *net position in the IMF* (F23),
- (c) position in ecus vis-à-vis the EMCF/EMI (F24)⁵.

Table 1: Classification of institutional sectors

 eurostat	ESA	United Kingdom
S10	Non-financial corporate and quasi-corporate enterprises	Industrial and commercial companies and public corporations
S41	Central banking authorities	Not coded
S42	Other monetary institutions	Banks and Building Societies
S43	Other credit institutions	Other financial institutions
S50	Insurance enterprises	Life insurance and pension funds
S61	Central government	Central Government
S62	Local government	Local Government
S63	Social security funds	included in S61
S70	Private non-profit institutions serving households	included in S80
S80	Households	Personal sector
S90	Rest of the world	Overseas sector

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(Millions of pounds)

 Sectors and sub-sectors		Credit institutions and insurance enterprises				General government				Non-financial	Private non-	National	
		Other	Other	Insurance	Total	Central	Local	Social security	Total	corporate and	profit institutions		
		monetary	credit	enterprises		government	government	funds		quasi-corporate	serving household		
Financial transactions		S42	S43	S50	S5	S61	S62	S63	S60	S10	S70/S80		
Changes in assets		Total	88058	128912	30229	247199	-321	1729	NA	1408	25634	54157	149451
Currency and transferable sight deposits	F20	135	3428	2014	5577	-127	547	NA	420	9407	15969	6072	
Other deposits	F30	17682	6537	-259	23960	599	1206	NA	1805	4542	-687	1141	
in national currency	F31	1389	2212	-402	3199	-79	1207	NA	1128	3865	-113	439	
in foreign currency	F32	16293	4325	143	20761	678	-1	NA	677	677	-574	702	
Insurance technical reserves	F90	NA	69	NA	69	NA	47	NA	47	947	31675	NA	
Bills and short-term bonds	F40	338	1012	-637	713	1539	844	NA	2383	491	-139	1748	
Long-term bonds	F50	11094	56733	10099	77926	NA	27	NA	27	1262	6236	46711	
Shares and other equities	F60	41845	54735	18519	115099	-5376	-1	NA	-5377	4851	475	88214	
Financial gold	F00	NA	NA	NA	0	NA	NA	NA	NA	-1000	NA	-1000	
Special drawing rights (SDRs)	F10	NA	NA	NA	0	NA	NA	NA	NA	NA	NA	NA	
Short-term loans	F70	-6622	6108	458	-56	4658	-560	NA	4098	877	86	-1633	
medium and long-term loans	F80	23586	290	35	23911	-1614	-381	NA	-1995	4257	542	7598	
Changes in liabilities		Total	84263	125655	31131	241049	48904	-98	NA	48806	33019	17896	161823
Currency and transferable sight deposits	F20	24600	0	NA	24600	1689	NA	NA	1689	0	0	988	
Other deposits	F30	47304	-402	NA	46902	3268	NA	NA	3268	896	NA	22587	
in national currency	F31	3945	-402	NA	3543	3931	NA	NA	3931	0	NA	-166	
in foreign currency	F32	43359	NA	NA	43359	-663	NA	NA	-663	896	NA	22753	
Insurance technical reserves	F90	NA	2309	31184	33493	-501	NA	NA	-501	NA	NA	254	
Bills and short-term bonds	F40	159	1000	NA	1159	-812	7	NA	-805	1714	376	744	
Long-term bonds	F50	NA	NA	-466	-466	53420	NA	NA	53420	162	NA	14376	
Shares and other equities	F60	12574	19678	NA	32252	NA	NA	NA	NA	23502	NA	28920	
Financial gold	F00	NA	0	NA	0	0	NA	NA	0	NA	NA	0	
Special drawing rights (SDRs)	F10	NA	NA	NA	0	0	NA	NA	0	NA	NA	0	
Short-term loans	F70	-359	94845	63	94549	-8109	-425	NA	-8534	5830	-48	85759	
medium and long-term loans	F80	-15	8225	350	8560	-51	320	NA	269	915	17568	8195	
Net change in financial assets and liabilities		N6	3795	3257	-902	6150	-49225	1827	NA	-47398	-7385	36261	-12372

NA = Non available

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(Millions of ecus⁽¹⁾)

 Sectors and sub-sectors		Credit institutions and insurance enterprises				General government				Non-financial corporate and quasi-corporate enterprises	Private non- profit institutions serving household and households	National economy	
		Other monetary institutions	Other credit institutions	Insurance enterprises	Total	Central government	Local government	Social security funds	Total				
		S42	S43	S50	SS	S61	S62	S63	S60				S10
Financial transactions													
Changes in assets		Total	112897	165275	38756	316928	-412	2217	NA	1805	32865	69433	191607
Currency and transferable sight deposits		F20	173	4395	2582	7150	-163	701	NA	538	12060	20473	7785
Other deposits		F30	22670	8381	-332	30719	768	1546	NA	2314	5823	-881	1463
in national currency		F31	1781	2836	-515	4102	-101	1547	NA	1446	4955	-145	563
in foreign currency		F32	20889	5545	183	26617	869	-1	NA	868	868	-736	900
Insurance technical reserves		F90	NA	88	NA	88	NA	60	NA	60	1214	40610	NA
Bills and short-term bonds		F40	433	1297	-817	913	1973	1082	NA	3055	629	-178	2241
Long-term bonds		F50	14223	72736	12948	99907	NA	35	NA	35	1618	7995	59887
Shares and other equities		F60	53648	70174	23743	147565	-6892	-1	NA	-6894	6219	609	113097
Financial gold		F00	NA	NA	NA	0	NA	NA	NA	NA	-1282	NA	-1282
Special drawing rights (SDRs)		F10	NA	NA	NA	0	NA	NA	NA	NA	NA	NA	NA
Short-term loans		F70	-8490	7831	587	-72	5972	-718	NA	5254	1124	110	-2094
medium and long-term loans		F80	30239	372	45	30656	-2069	-488	NA	-2558	5458	695	9741
Changes in liabilities		Total	108031	161099	39912	309042	62698	-126	NA	62573	42333	22944	207469
Currency and transferable sight deposits		F20	31539	0	NA	31539	2165	NA	NA	2165	0	0	1267
Other deposits		F30	60647	-515	NA	60132	4190	NA	NA	4190	1149	NA	28958
in national currency		F31	5058	-515	NA	4543	5040	NA	NA	5040	0	NA	-213
in foreign currency		F32	55589	NA	NA	55589	-850	NA	NA	-850	1149	NA	29171
Insurance technical reserves		F90	NA	2960	39980	42940	-642	NA	NA	-642	NA	NA	326
Bills and short-term bonds		F40	204	1282	NA	1486	-1041	9	NA	-1032	2197	482	954
Long-term bonds		F50	NA	NA	-597	-597	68488	NA	NA	68488	208	NA	18431
Shares and other equities		F60	16121	25229	NA	41350	NA	NA	NA	NA	30131	NA	37078
Financial gold		F00	NA	0	NA	0	0	NA	NA	0	NA	NA	0
Special drawing rights (SDRs)		F10	NA	NA	NA	0	0	NA	NA	0	NA	NA	0
Short-term loans		F70	-460	121598	81	121219	-10396	-545	NA	-10941	7474	-62	109949
medium and long-term loans		F80	-19	10545	449	10975	-65	410	NA	345	1173	22523	10507
Net change in financial assets and liabilities		N6	4865	4176	-1156	7885	-63110	2342	NA	-60768	-9468	46489	-15862

The British data in 1993, communicated in millionsof pounds, have been converted into Ecus at average annual exchange rate (0,779988 £ = 1 ECU).

NA = Non available.

Financing the national economy

Following the slow-down recorded during the period 1989-1991, financial transactions between the British economy and the *rest of the world* were particularly dynamic in 1992-1993. The financial balance for 1993 (-12 372 million pounds sterling) is the result of substantial flows: +149 451 million pounds in asset changes and +161 823 million pounds in liability changes, that is to say, nearly double that of the previous year. In 1993, foreign investments in the United Kingdom principally took the form of securities (F50/F60), *short-term loans* (F70), and *other deposits* (F30).

For a better understanding of the financial accounts, it is necessary to recall

some indicators of the United Kingdom's economy in 1993. The GDP growth rate recovered in 1993 with an increase of 1.25% in real terms, and the consumer price index increased by 1.9%. The current account deficit increased sharply in 1993, not due to deficit items (trade balance, government transactions and unilateral transfers), which have actually improved, but rather by the drop in income from investments which could not be offset by the rise in surpluses from services. Monetary aggregates increased in real terms, and sterling depreciated, particularly in relation to the US dollar and ecu. Lastly, British interest rates fell, thereby reducing the interest differentials with trade partner countries.

Table 2: Financial accounts between 1984 and 1993

Unit : million pounds sterling		1984	1985	1986	1987	1988	1989	1990	1991	1992	1993
National economy	Total change of financial assets	27243	45658	87714	75649	49503	81707	72507	15094	77099	149451
	Total changes of liabilities	21307	43134	87407	85866	66019	106565	96903	28866	85199	161823
	Net change in financial assets and liabilities	5936	2524	307	-10217	-16516	-24858	-24396	-13772	-8100	-12372
Net change in financial assets and liabilities (N6)	Credit institutions (S40)	2727	3834	3359	1569	8125	-1869	-924	-6546	9834	7052
	Insurance enterprises (S50)	-482	-350	97	550	-1601	-987	-436	659	-107	-902
	General government (S60)	-12264	-10304	-9778	-6468	3612	5111	-6577	-15427	-37412	-47398
	Non-financial corporate and quasi-corporate enterprises (S10)	2953	-3080	-2276	-9095	-20126	-25014	-28301	-19469	-20064	-7385
	Households and private non-profit institutions serving households (S80/S70)	13002	12424	8905	3227	-6526	-2099	11842	27011	39649	36261

Payment instruments

The payment instruments traditionally comprise:

- F00 - *financial gold*,
- F10 - *special drawing rights*,
- F21/F22 - *currency and transferable sight deposits*,
- F23 - *position in the IMF (F23)*,
- F24 - *ecus swapped with the EMCF/EMI*⁵.

After the monetary crisis which led to the

devaluation of several currencies including that of the pound sterling, in September 1992, 1993 seemed to show a new departure with an increase of monetary flows⁶.

Investment instruments

The share of investment instruments in the overall asset changes increased after 1991. They represented 92% of the asset flows in 1993.

Deposits other than transferable sight deposits (F30) (mainly time and saving

deposits) became less attractive after 1990. In 1993, the resumption of such flows was attributable to the activity of *non-financial corporate and quasi-corporate enterprises* (S10) and *general government* (S60), while demand by *households*, and *private non-profit institutions serving households* (S70/S80) fell in line with the continued decline in savings, which began in 1989.

Bills and short term bonds (F40) comprise certain Treasury bills, local authority bonds, trade bills, certificates of deposit issued by banks and building societies (in pounds sterling only for the latter) and eligible bills. Although less pronounced than in the period from 1988 to 1991, there was still an increase in the issue of *bills and short term bonds* in 1993, with a flow of 1 714 million pounds for *non-financial corporate and quasi-corporate enterprises*. Only *general government* (S60) reduced the volume of its issue of *bills and short term bonds* (-805 million pounds sterling).

The securities market expanded

considerably in 1993. Issues of **long term bonds** (F50) by *central government* (S61) increased by 53 420 million pounds with important flows for the *credit institutions* (S43), the *rest of the world* (S90), and *households and private non-profit institutions serving households* (S70/S80). Issues and purchases of **shares and other equities** (F60) also rallied strongly in 1993 even if households (S70/S80) were not significant buyers of this type of financial instrument.

Insurance technical reserves (F90), which are liabilities of *insurance enterprises* (S50), grew steadily from the start of the 1980s (+32 992 million pounds in 1993).

Financing instruments

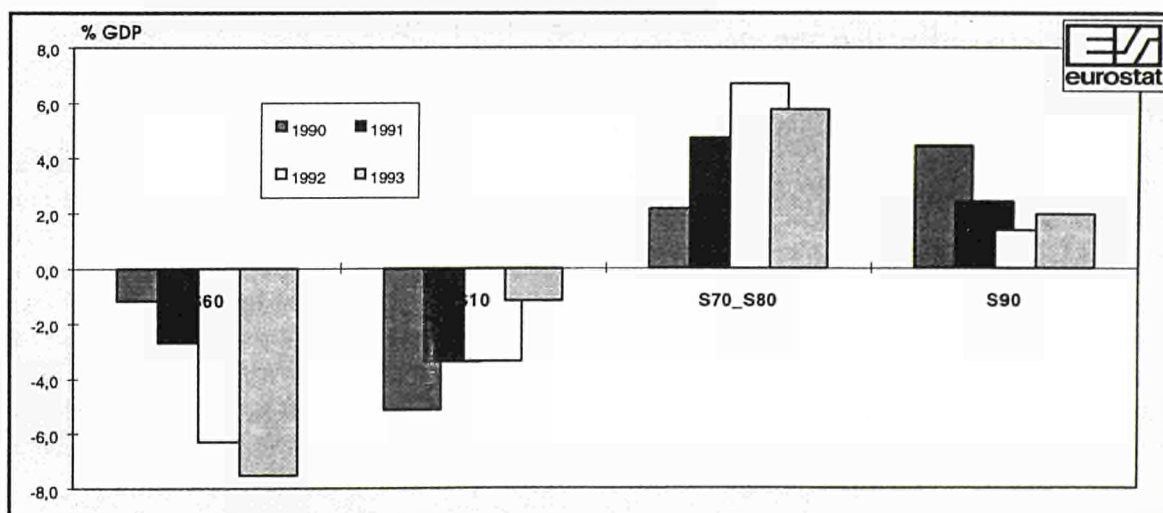
In 1993, non-commercial lending flows between the British economy and the *rest of the world* were important despite the decrease in *other short term loans* (F79) granted by the *other monetary institutions* (S42).

Institutional sectors

Figure 1 shows the trend in net changes in financial assets and liabilities of economic operators from 1990 to 1993 (or

after adjustment, their net lending/borrowing), in relation to GDP.

Figure 1: Trends in the net change in financial assets and liabilities by institutional sector from 1990 to 1993 in percentage of GDP¹



On the **borrowers'** side, the *general government* (S60) financial deficit rose over the period 1990-1993, accounting for 7.5% of GDP in 1993¹, the peak of the decade. *Non-financial corporate and quasi-corporate enterprises* (S10) embarked on the reverse process, reducing their financial deficit over the years to reach only 1.2% of GDP in 1993. On the **lenders'** side, the net lending of households (S80/S70), declined in 1993, but their positive financial balance (5.8% of GDP) remains high in the context of the past decade.

Financial sectors

Credit institutions (S40)

In the United Kingdom classifications, *credit institutions* (S40) are divided into two major groups⁷ :

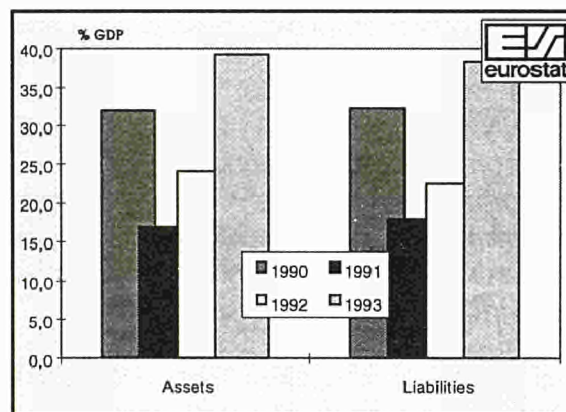
- monetary institutions, which include the banks (and the Banking Department of the Bank of England) and building societies;
- other financial institutions, which comprise investment funds, unit trusts, leasing companies, finance houses and a few banks not subject to monetary control regulations of the United Kingdom (Channel Islands and Isle of Man banks).

In the general context of increasing competition between banks and with a slowdown of tensions following the pound's depreciation and the decrease of interest rates in 1992, the development of activity in the *credit institutions* sector (S40) reached new heights in 1993, with a flow of 209 918 million pounds in liabilities (cf. Figure 2 in terms of GDP).

The financial activities of *other monetary institutions* (S42) had seen a sharp slowdown in 1991. This seems to have ceased in 1992 and 1993. In 1993, the liability flow of the sector reached 24 600 million pounds in transferable sight

deposits (F20), and 47 804 million pounds in *other deposits* (F30). Issues of *shares and other equities* (F60) have more than doubled in comparison with 1992. Regarding the type of assets used in conjunction with these flows of liabilities, there was a decline in the use of financing instruments, especially at short-term, whereas the volume of securities (F50/F60) and *other deposits* (F30) rose sharply.

Figure 2: Changes in financial assets and liabilities of financial institutions (S40/S50) from 1990 to 1993 in percentage of GDP



In 1993, *other credit institutions* (S43) sharply increased their activity particularly on the securities market (F50/F60), with an asset flow of 128 912 million pounds and a liability flow of 125 655 million pounds. Recourse to *short term loans* (F70) increased sharply, along with issues of shares and other securities (F60).

Insurance enterprises (S50)

Since the start of the 1980s, *insurance enterprises* (S50) have been steadily increasing the amount their technical reserves (F90, +31 184 million pounds in 1993). As counterpart to these liabilities, the *insurance enterprises* gave preference to *long term bonds* (F50, +10 099 million pounds in 1993) and to *shares and other equities* (F60, +18 519 million pounds in 1993).

Non-financial sectors

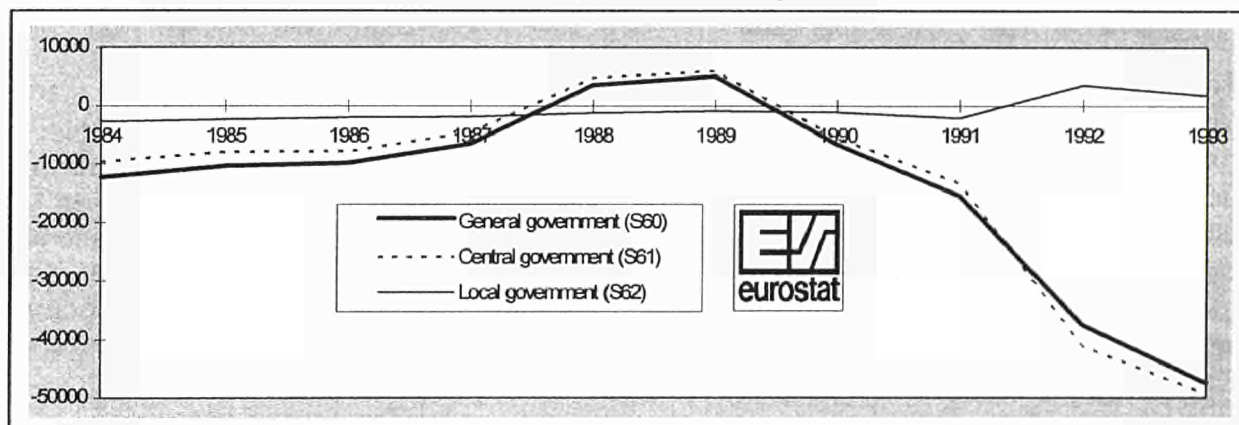
General government (S60)

There was a deterioration in the financial assets and liabilities balance of *general government* (S60) each year during the period 1989-1993 (see figures 1 and 3) due to the *central government* (S61) deficit¹. From 1.0% of GDP in 1990, the later reached 7.5% in 1993, or 49 225 million pounds. Growth in expenditure on health has continued unabated in recent

years. To finance the deficit, it has been necessary to resort increasingly to issues of *long term bonds* (F50).

Local government (S62) activities continued to have little impact. It is apparent however, that the net lending generated in 1993 was a result of an increase in flows of assets, in particular in currency and deposits (F20/F30) and *bills and short term bonds* (F40), and of a further decline in liabilities following the reduction in direct borrowing from the *central government* (S61).

Figure 3: Net change in financial assets and liabilities of general government and its sub-sectors from 1984 to 1993, in millions of pounds



Non-financial corporate and quasi-corporate enterprises (S10)

In the United Kingdom, non-financial corporate and quasi-corporate enterprises comprise nationalised industries and public corporations (British Rail, the Post Office, certain local airports, the BBC, etc.) and industrial and commercial companies.

In the context of economic recovery, the net change in the financial assets and liabilities of *non-financial corporate and quasi-corporate enterprises* was slightly negative in 1993. After the pound's depreciation, exports grew more than imports and the trade deficit was smaller than in 1992. The deficit for industrial and commercial companies, which had been declining for several years, was

transformed into a surplus, despite a revival of gross fixed capital formation.

The level of financial flows (respectively 25 634 million pounds in assets and 33 019 million pounds in liabilities), marked a new revival in the financial activities of corporate and quasi-corporate enterprises. There was increased recourse to internal funds, accompanied by issues of *bills and short term bonds* (F40) and particularly of *shares and other equities* (F60). Although still low, foreign investment also increased.

Households and private non-profit institutions serving households (S70/S80)

The sector *households and private non-profit institutions serving households*

(S70/S80) includes private individuals and trusts, unincorporated enterprises and non-profit bodies serving private individuals.

The lending capacity of the sector remained significant in 1993, though down on 1992. The financial net change of 36 261 million pounds was the outcome of substantial financial flows on the assets side, while financial flows on

the liabilities side were sluggish.

Despite the fall in long-term interest rates and the greater risk taken by *credit institutions* in the form of loans to private individuals, the increase in housing loans in the third quarter of 1993 and in loans for private consumption correspond to flows of liabilities well below those recorded during the period 1986-1991 (+17 568 million pounds in *medium and long term loans* in 1993; F80).

Additional information

This publication has been prepared by Mrs. F. Perret, Tel (..352) 4301-33275, for the Eurostat unit on "Financial accounts, monetary and financial statistics", based on statistics supplied by the Central Statistical Office (CSO) of the United Kingdom for the financial accounts database managed by Eurostat (management: Mr H. Vreeswijk,

Tel (..352) 4301-34323).

Further information on harmonised financial accounts of the European Union Member States can be found in the following Eurostat publications: "Money and Finance", "National Accounts ESA - Detailed tables by sector" and "General government accounts and statistics".

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- 1 The financial surplus (deficit) concept referred to in this study corresponds to the change in assets and liabilities of the financial accounts (code N6) as defined in the present version of the ESA (ESA-1979 or ESA, 2^o edition). Theoretically, this balance has to be strictly equal to the net lending (borrowing) of the capital account (code N5). For technical reasons (various statistical sources), differences may appear and, in practise, a balancing item is necessary between the financial account and the capital account. It should be mentioned that the balance of the capital account is used to measure the public deficit of the *general government* sector in the excessive deficit procedure. As an example, the *Central government* deficit (net borrowing) registered in 1993 by the British authorities for the excessive deficit procedure represents 7.8% of GDP whereas the changes in assets and liabilities reaches 7.5% of GDP.
 - 2 At present, 8 Member States transmit to Eurostat their Financial Accounts based on the ESA definitions: Belgium (B), Germany (D), Spain (E), France (F), Italy (I), The Netherlands (NL), Portugal (P), and the United Kingdom (UK). All financial accounts statistics of the Member States (based on the ESA-1979) are published annually by Eurostat, without commentary. Data relative to each Member State are checked from time to time and Eurostat usually uses this opportunity to publish the data of the country concerned, as is now the case with the United Kingdom. It should be noted that the British figures are available from 1984 onwards.
 - 3 The ESA version used at present (ESA 1979 or ESA, 2^o edition) is being revised.
 - 4 With the exception of calculation methods of certain data (GDP, net lending/borrowing of the *central government*), the ESA-1979 is not obligatory in its entirety. On the contrary, compliance with the ESA-1995, which will soon come into force, will be obligatory. From 1998 onwards, all the Member States of the European Union will have to communicate to Eurostat their financial accounts relative to 1995 onwards, based on the ESA-1995 methodology.
 - 5 Most of the mentioned statistics are available in the publication of the International Monetary Fund. Nevertheless, data communicated to Eurostat by the United Kingdom and presented here without any modifications do not allow for separate itemisation.
 - 6 We should be careful in the interpretation of flows concerning payment instruments. Evaluation methods of British financial accounts probably lead the inclusion of a part of the revaluation gains realised by the *non-financial corporate and quasi-corporate enterprises* holding deposits in foreign currency, following the depreciation of sterling in 1993.
 - 7 The definition of other financial institutions has underwent profound changes in 1982, with the "monetary sector" replacing the former "banking sector".

