

Societies and Inflation

With Particular Relation to the Society and the Member

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Co-operative dividend is one area in which inflation has not adversely affected the member. Whether dividend is paid through dividend stamps or by traditional methods, the fact that the dividend return is based upon the inflating price levels of goods bought means that the level of dividend inflates pro rata, always assuming of course that other factors have not intervened to lead to a reduction in the rate of dividend.

Traditional Dividend and Stamps

Inflation does, however, raise an interesting further factor in the continuing arguments as to the relative merits of dividend stamps versus traditional dividend. This is particularly marked when inflation reaches the present levels of 20% per annum. Consider the two methods from the members' point of view. Dividend stamps give an immediate return; if spent on goods or deposited in a share account the only delay involved is that in filling a stamp book. The purchase can then be made or the share deposit will start to earn interest. Traditional dividend, however, is usually paid six monthly, approximately three months after the end of the trading period. The dividend earned therefore becomes available anywhere from three months to nine months after the purchase, an average time lag of six months. With the inflation running at 20% per annum dividend will have depreciated therefore by 10% from time of purchase to date of receipt. Thus a declared rate of 5% becomes an effective 4½%. The member loses in comparison with a dividend stamp operation but the society

naturally gains, even without considering the effects of cash flow benefits.

Inflation has marked effect upon timing considerations and the argument advanced against traditional dividend applies equally to members' stamp bonus. The total involved is not so significant as that of dividend but it is clear that the usual bonus of 10p per book exchanged for goods or deposited to share is not an attraction and is largely discounted in the members' mind. Even doubling the amount of bonus is unlikely to lead to a rush of non-members wishing to take out membership. Timing again is the stumbling block for the possibility of receiving an additional 10p (or 20p) at some time in the future is not likely to weigh in people's minds when prices are escalating as now. The remedy is surely to consider giving the bonus to members immediately rather than by subsequent credit to a share account, which in any event in terms of clerical labour, whether the accounting is computerised or not, becomes an extremely expensive 10p deposit. If in addition it is not an attraction to the member then the practice should surely be re-examined. To discard the bonus altogether, however, would lead to a loss of a membership benefit, however small, and would add to the problems of falling membership; inflation, whatever its evils, cannot be blamed as the sole reason for this particular problem facing the Movement.

Spiralling prices and the dramatic fall in the purchasing power of money have a powerful effect upon the majority of people. The uncertainty of the future, enlarged upon daily by the media, leads everyone to live for today and is undoubtedly one of the reasons for the rapid changeover within societies from traditional dividend to stamps. In rapid inflation timing becomes paramount. But what of the side effects? It is no coincidence that the rise in the popularity of dividend stamps has seen a fall in total share capital available to retail societies. When translated into real terms the fall is, of course, even more dramatic over the last five years.

Share Capital

Co-operative share capital has been built up over the years mainly from undrawn traditional dividend and the switch over to dividend stamps now has stopped this source; hence the decline. Prior to this, however, the increasingly competitive interest rates over the last twenty years had diverted much of the small savers' money away that might otherwise have found its way into Co-operative share deposits. As inflation continues therefore it is likely that share capital will continue to decline in real terms as a source of funds to retail societies.

No amount of advertising or improvement of deposit and withdrawal facilities or similar activity, important as they are, will improve the inflow of new money to share capital whilst there is so much disparity with the interest rates being offered by the competitive investments. The attractions of Government sponsored savings often with tax concessions, building societies and the like are well known and the investor conscious of the return he is receiving has almost certainly already moved capital away from Co-operative societies and the capital which remains is there for convenience rather than to obtain a return. This factor, one feels, is the answer to those that seek a rise in share interest rates. In 1973 the average national share interest rate was 3.4% of share capital. At today's inflated interest rates it would be necessary to increase this rate four-fold to be competitive, at an additional cost in interest of more than £14 millions - over half the amount provided in dividend in 1973. At this level I would suggest Co-operative principles are called into question and the charge of remunerating capital, rather than rewarding member trading loyalty, would be hard to refute. In times of inflation, unless incomes rise faster than prices and consumer spending is held down, savings are unlikely to rise. The possibility of the introduction of index-linked loans to increase the attractiveness of saving to the investor cannot, of course, be ignored. Having regard to the economic climate therefore there is little optimism one can find in favour of share capital which is likely to continue to decline in real terms.

Before leaving the question of subscribed capital a word must be said about ordinary loan capital and small savings. The general economic factors affecting share capital apply equally in this sector also, though undrawn dividend has not provided a source for loan capital as it has for shares. In the national statistics the loan capital total is dominated by the employees' superannuation funds invested with the societies which amounted in 1973 to £86 million out of a total of £146. In the last five years, however, ordinary loans and small savings have been static at approximately £28 millions which means an actual decline in real terms.

Reserve Funds

If the introduction of dividend stamps has had a detrimental effect upon share capital accumulation then the real decline in that source of funds has galvanised societies into the realisation of the importance of building up reserve funds. The importance, in times of inflation, of collectively owned funds has been clearly seen by retail officials, and it must be said, the use of dividend stamps has given them room to manoeuvre in dramatically improving surplus retentions. Between 1964 and 1968 retail societies reserves improved by £4.2 millions to £49.0 millions; in the subsequent five years to 1973 there was an improvement of £67.3 to £116.3 millions. In considering these figures, however, it should be remembered that allocations to reserve in this period have included two main elements. First there has been the straightforward allocation from current surplus but, secondly, to this has to be added the capital surplus arising from the sale of assets. Particularly in the latter years of the past decade, societies have been active in closing smaller and loss making trading units and disposing of these and other surplus freeholds to take advantage of the inflated property values. The report of the Capital Resources study group quoted a figure of £7 millions surplus from property sales in 1971 but these are, of course, "once for all" gains, for the availability

of surplus property is obviously limited and the fall in property values will in the short period at any rate, restrict the surplus to be made from property sales.

The General Prospect

Inflation, and the increasing rate of inflation, has resulted in a dramatic change of emphasis in the way retail societies are financed. The economic factors affecting the level of savings combined with the high level of interest rates prevailing, will mean that there will be no immediate future increase in share and ordinary loan capital available to retail societies. Emphasis on increasing retentions to build up reserves must continue to the point at which societies become independent of subscribed capital. The lesson of the last ten years, however, would seem to indicate that this alone will not be sufficient. The total funds available in 1973 of £402 millions compares with £434 in 1964. Even allowing for the healthy increase in reserves in the latter part of the decade there has been a marked real decline in funds available. The costs of new developments both in terms of fixed and working capital continue to inflate, however, to say nothing of the inflationary effect upon existing working capital. Once societies have run down their own investments further capital can only be obtained by going to the market for money either in the form of overdraft or on short term borrowing at the market rate. Such short term borrowing is likely to be most likely to succeed if directed to the institutional investor rather than the member however. What does emerge, very clearly indeed, is that if inflation continues at 1974 levels then further retail development is likely to be curtailed due to the high costs and limited supply of capital.