

IV. Markedly changing structure of Czech households' savings

In mid-2004, the population of the Czech Republic disposed of assets in form of various kinds of savings totalling CZK 1354 billion. While the most dynamic increase in recent years was reported for saving in building societies and for value of property in shares funds, 44.3% of Czech households' savings is still kept as time and sight deposits at banks. From the macroeconomic point of view, people save less year by year, which decreases the ratio of gross household's saving to household disposable income. Yet the average amount of household's assets in the wide range of savings grew from CZK 285 thousand per household at the end of 2001 to CZK 341 thousand in mid-2004. The population of the Czech Republic thus enlarged their wealth by CZK 215 billion.

In terms of dealing with money, behaviour of Czech households¹ in recent years is characterised by changing trends – alternative forms of saving and investment are gaining ground in contrast to the traditional way of time deposits that had been prevailing for a long time on the one hand, and a shift in the mentality of people who are willing to contract debts on the other hand.

Compared to the end of 2001, in mid-2004 the **money increase** across the whole range of deposit and investment products, life insurance and supplementary pension insurance, incl. estimated cash kept at home amounted roughly to **CZK 215 billion, i.e. a growth of 18.8%**. Most money of Czech households (CZK 303.4 billion) was on sight deposits whose volume at the end of June 2004 exceeded for the first time the traditionally high amount on time deposits at commercial banks (CZK 296.7 billion). In spite of the fast growth of saving in building societies and investment in shares funds, **there is still nearly a half of Czech households' total savings kept in form of the above-mentioned kinds of bank deposits**.

Alternatives to deposits are on the increase, yet bank accounts are still high

Deposit books and bank accounts are no longer a synonym of Czech households' savings. A **dramatic fall in time deposits** at commercial banks was recorded especially from mid-2001 to September 2004. Within this short period of time, the volume of money on time and savings accounts dropped by CZK 175 billion, i.e. 37.1%. At the same time, **deposits in form of saving in building societies and investment in domestic and foreign shares funds more than doubled**. **The total amount on accounts of supplementary pension insurance grew by more than a half and shares in technical reserves of life insurance by roughly a third**.

On the other hand, the **population's foreign currency savings and the volume of securities held by households** (at estimated market value) slightly **decreased**. A marked movement of money which households want to have quickly available was recorded as a response to lower nominal yields of traditional savings – the **volume of money on current and giro accounts** of the population **rose** by nearly 60% and reached CZK 303.4 billion in mid-2004 against the end of 2001. Also so-called stored up **money kept by people at home** without depositing or investing it grew. According to a very rough estimate, its volume can be about CZK 40 billion.

All the above-mentioned changes document a massive start of alternative forms of saving, which bring **Czech households closer to the behaviour of households in Germany or Austria** (the popularity of saving in building societies) and partly to the behaviour of **Anglo-Saxon households** (collective investment). Better knowledge, seeking more profitable, adequately-risk or most liquid saving opportunities according to preferences of the family budgets – also this is an explanation of the above-mentioned shifts in volumes between various kinds of Czech households' savings.

Nominal versus real interest rates

Of course, it would be misleading to say that time deposits and savings accounts of households-population are decreasing in consequence of weak yields in the period of low interest rates. This holds for the nominal level because interest rates declared by banks are the main criterion for an overwhelming majority of savers. Paradoxically enough, **increases of money deposited by households-population were at the lowest level in the years when deposits were profitable in real terms**.

In spite of the fact that nominal interest rates on deposits of the population in the banking sector were low in 2003 (the average of 1.467% p.a.² also includes interest rates on saving deposits at building societies which yield higher interest than usual bank deposits), bank deposits in total were profitable thanks to stagnating prices in the economy. Consumer prices grew substantially less than these yields and, as a result, the real interest rates were above zero. The situation in the years 1993-1998 was rather different, because, in spite of relatively high nominal interest rates on deposits, the average inflation was nibbling away at yields so much that the real interest rates on deposits of the population were considerably below zero. Between 1993 and 2004, **savings were profitable only in 1999** (in response to a sharp fall in the average inflation rate from 10.7% to 2.1%, real interest rates increased to 2.6%) and in **2002 and 2003**, when thanks to very low inflation (1.8% and 0.1%, respectively), real interest rates on deposits of the population were 0.3% and 1.4% p.a., respectively. **Bank deposits in the other years were unprofitable**.

¹ Households for the purposes of this analysis are the sector of households-population excl. households-businesses.

² From monthly data of CNB on interest rates in the sector of households-population – non-weighted.

The shift from banks to building societies

At the end of September 2004, the population had roughly the same amount of money on time deposits in the banking sector (commercial banks and building societies) as at the beginning of 2001. However, in focus of the Czech savers was predominantly saving in building societies because deposits on accounts at commercial banks, i.e. **time deposits at banks, decreased sharply during mere three years – by CZK 180 billion** between September 2001 and September 2004, which was a fall by more than a third.

The y-o-y decreases in bank deposits started to occur at the beginning of 2002, the fall accelerated and its rate reached a double-digit level – in the May to July 2003 period the deposited money decreased each month by as much as a fifth y-o-y. Whereas time deposits and money on savings accounts at commercial banks amounted to CZK 469.3 billion at the end of 2001, it was only 296.7 billion in mid-2004. A fall like this during such a short period represents a marked structural change in Czech households' savings – the amount of CZK 117 thousand per household in form of time deposits at commercial banks at the end of 2001 dropped to CZK 75 thousand in mid-2004.

Saving in a building society is a deposit as well

Clients' deposits at building societies grew from CZK 120.5 billion at the end of 2001 to CZK 261.1 billion in mid-2004, i.e. by CZK 140.6 billion. This sort of saving dominated particularly in 2003, before the terms of the product became stricter, especially through granting a lower state contribution and prolonged saving period, which motivated clients, under massive promotion by the building societies concerned, to sign new contracts or raise the target amount of existing contracts. As the graph shows, a large part of the money was transferred from bank deposits. In 2003 clients deposited CZK 56.5 billion in building societies. The strong impetus of the exceptional year 2003 is **also** corroborated by the development **in the first half of the "normal" year 2004** when people **kept depositing** – while deposits with building societies rose by 31.5% in 2003, the y-o-y increase at the end of June 2004 was also very strong: by 27.3%, i.e. CZK 56 billion (however, lower demand showed itself in the number of new contracts).

Each household has its own shopping basket

Besides the flow of money from banks to building societies, people also transferred their fixed deposits and time deposits to sight deposits. Both these trends came on at the time of household consumption recovery, after a marked reduction particularly in 1998.

As mentioned above, Czech savers draw most money on their time deposits at the time when these deposits actually brought in the highest profits – inflation was so weak that, in spite of very low nominal interest rates, the yield was substantially higher than in the periods of seemingly better (at some banks even double-digit) client interest rates on deposits. The explanation of this "irrational" behaviour of the overwhelming majority of Czech households does not necessarily rest only on people having been insufficiently informed. The statistically reported movement of prices in the economy does not have to correspond to the subjective feeling of price increases because the shopping basket of each family is "defined" differently. However, the development of prices of food whose weight is higher in expenditures of families on low income was strongly disinflationary over last two years. The rate of households' savings broken down by income is not exactly known.

Sight deposits gained attractiveness

In relation to products of the sector of commercial banks, the decrease in time deposits among households showed itself in an **increase in the volume of money left on current and giro accounts**. Between December 2001 and June 2004, their balance grew from CZK 191.1 billion to CZK 303.4 billion (i.e. CZK +112 billion and nearly 59%) and monthly increases in the period were 18.8% y-o-y on average. **Only from 2004 the rate of accumulating money on sight deposits started to decrease to the level of 13%, which is still a very high y-o-y growth.**

On top of money being quickly available, current accounts have one more advantage for clients, which are overdraft facilities in form of debit balances on current accounts. These actual loans are growing fast too – this way people had available CZK 2.6 billion at the end of 2001, CZK 8.1 billion in mid-2004 and, according to preliminary data, even CZK 10.2 billion at the end of 2004.

Volume of deposits in dollars and euros dropped

On the other hand, foreign currency deposits show a stable decrease in recent years. Foreign currency deposits of households stood at CZK 88.2 billion at the end of 2001 and CZK 68.4 billion in mid-2004. The **constant appreciation of the koruna against the dollar during the period** (total appreciation against the euro was substantially weaker) **reduces the value of dollar deposits**, which makes savers respond. The fall in foreign currency deposits is therefore provoked by the above-mentioned exchange rate effect on the one hand, and by outflow of deposits and their conversion into other financial products. Higher interest rates on euro deposits than on dollar deposits stem from the higher level of basic rates in the Euro-zone than rates in the American economy. Nevertheless, the interest differential between these

currencies that was sizeable in 2002 and 2003 is not that marked after several rate increases in the U.S. Yet deposits in *dollars* and *euros* yield largely higher interest than deposits in Czech *korunas* even now (the highest interest rates on yearly clients' deposits in *dollars* may produce up to 2.8% of gross yield if the deposit reaches USD 10 thousand; when this equivalent is deposited in *euros*, gross yield can be 3.2%).

Money kept at home

Out of the total of the monetary aggregate M2 measuring the volume of money in the economy, in particular the component M1 is growing, i.e., besides sight deposits of households and companies also money in circulation (not only the volume of money in circulation, but also credit transfers are on the increase). Estimates of so-called stored up money that is not put in any financial product by the population but kept at home, are not included in the bank statistics and are hard to make.³ However, we can assume that the above-mentioned **unattractive nominal interest rates on deposits in recent years caused that many households keep their money at home** or on sight deposits rather than as deposits on time accounts; moreover, liquidity of time deposits is lower. According to a very rough estimate, volume of money "under the pillow" may have been CZK 40 billion in mid-2004⁴.

Life insurance and supplementary pension insurance are gaining ground

As far as saving on accounts of life insurance policies and supplementary pension insurance is concerned, **money** saved by **clients of pension funds** incl. state contributions increased by 58.5% from December 2001 to June 2004 and reached CZK 98.1 billion. However, there is less money in the sector of pension funds because it not only flows in from clients but also flows out in form of pensions and lump sum payments. In 2003 pension funds paid CZK 7.4 billion as benefits. The average monthly contribution of participants is still relatively low (CZK 384 in 2003 and CZK 340 in 2001). In 2003 clients of pension funds gained CZK 1.7 billion as tax deductions, in 2002 it was CZK 1.4 billion and in 2001 CZK 1.1 billion⁵.

Roughly a tenth of the entire Czech households' savings is deposited as **life insurance**. The volume of money in form of so-called insurance companies' technical reserves, i.e. the hitherto savings of clients reduced by the risk component, rose by 35% from the end of 2001 to mid-2004 and reached **CZK 132 billion**. In spite of this growth, the share of life insurance in the CR computed as the received annual premiums to GDP (current prices) ratio is only 1.6%, which is considerably less than in the EU member states. However, this ratio is relatively favourable in comparison to the annual volume of money deposited by households as supplementary pension insurance where the ratio is a mere 0.58% of GDP. Also the product of life insurance benefited from the advantage of tax deductions available to depositors if they meet certain conditions (annual amount saved and term of the contract). **The volume of technical reserves of life insurance of the population has now been growing at a rate higher than ten per cent.**

Shares funds build up a strong position

Czechs accepted collective investment. After bad experience of funds from the mid-1990s and losses suffered by small investors, the image of the sector of funds was not good for a long time. However, the property accumulated in shares funds started to grow markedly from 1998, under a simultaneous decrease of property in the sector of investment funds founded during the first and second waves of voucher privatisation. Opening of the funds led to repurchases by investors on the one hand, which reduced property of the funds. On the other hand, new unit holders entered these entities and purchases of shares funds certificates together with the increasing value of property invested in the funds raised the volume of their book value. According to data of the Union of Investment Companies of the Czech Republic (UIC CR) (encompassing unit holders as both legal and natural persons), the value of property of only domestic open shares funds rose from CZK 66.5 billion at the end of 2001 to CZK 112.1 billion in mid-2004. Also investment of Czech residents in foreign funds grew considerably (the volume more than doubled in the June 2002-June 2004 period and reached CZK 53.3 billion). The property in domestic and foreign shares funds together with the rest of property in investment funds totals CZK 163.3 billion.

The above-mentioned figures apply to the whole sector of funds. **The value of property of natural persons is somewhat less**, because, according to information of the biggest Czech investment companies, property of their clients-natural persons accounts for 80-90% of the value of total property in funds. This suggests that **property of Czech households in the funds was about CZK 139 billion⁶ in mid-2004.**

³ For the purpose of this analysis, an estimate was made based on the average growth rate of sight deposits in the above-mentioned period and the average growth rate of money in circulation – dynamics of volume of money kept at home is estimated as the mean value of growth rates of both variables raised by coefficient 1.5 because the base of volumes of stored up money is considerably lower than volumes of money in circulation and sight deposits.

⁴ This very rough estimate is based on volume of money in circulation, cash at bank counters, cash with traders and companies, structure of banknotes by nominal value, consultations on money distribution and circulation.

⁵ Source: Statistics of the Association of Pension Funds, financial data according to annual reports, Office of the State Supervision in Insurance and Pension Fund, Ministry of Finance.

⁶ For the purpose of this analysis, all data on the sector of shares funds are calculated by means of a coefficient 0.85 taking into account the share of natural and legal persons among the funds' clients; the resulting figures are thus estimates and risk needs to be borne that the share of investors-natural persons and investors-legal persons differs by kind of funds.

Investment grows fast, low-risk funds are preferred

The year 2001 was not very favourable for shares funds because repurchases were prevailing and the property, as to natural persons, fell by nearly CZK 12 billion y-o-y. However, a more realistic comparison of the two-year period June 2002 to June 2004⁷ shows that the property of Czech investors-natural persons in domestic and foreign shares funds rose by CZK 47 billion during the short period (by CZK 41 billion if investment funds and development of their property are included). In June 2004 thus the value of property of natural persons in foreign funds was CZK 45 billion, whereas in June 2002 only less than CZK 20 billion.

Increasingly more money flows into foreign funds. Whereas at the end of 2002 the value of natural persons' property in foreign funds amounted only to 27% of the value of property in domestic funds, a year later it was already 42% (CZK 39 billion as against CZK 93 billion). Just within the fourth quarter of 2003 the property of investors-natural persons in foreign funds increased by 11.1%, whereas domestic funds recorded a drop of 0.7%. In the whole year **2003 the value of property of investors-natural persons in foreign funds grew by 49.5%, whereas that in domestic (incl. investment) funds decreased by 3.5%.**

The conservativeness of Czech investors shows itself also in the choice of **low-risk funds**. Most money has been invested in money market funds whose yields do not strongly overshoot the PRIBOR interest rates. At the end of the third quarter of 2004 the value of natural persons' property in domestic money market funds was CZK 49 billion, which was more than half of all their property in domestic open shares funds.

Property deposited in securities is hard to estimate

A similar development is characteristic for direct investment of the population of the Czech Republic in securities. Although the total volume of natural persons' property in nominal value was CZK 92.9 billion (but only CZK 29.7 billion registered) according to data from the Prague Securities Centre (PSC), this figure gives actually no relevant information about Czech households' property deposited in securities. According to a very rough estimate of the PSC, the market value of the securities may be somewhere between 15-20% of the total nominal volume, which would have been very roughly CZK 17 billion at the end of 2003. This figure seems to be relatively low not only with regard to the fast growth of the stock exchange index PX50 containing the most liquid titles of the Prague Stock Exchange and growing by more than 40% in 2002 and 2003 (over 50% in 2004), but also with regard to the increasing number of people trading in shares via stock brokers (less at bank counters, more at brokerage firms which regain credibility after several collapses – in particular trading online or by phone is on the increase). The growing market capitalisation of traded titles includes not only property changes with investors-natural persons, but also with institutional investors, domestic and foreign alike. Only an analysis of the structure of traded companies' equity could provide a more accurate insight.

The development since the first half of the 1990s when the first and second wave of voucher privatisation was in progress is characterised by a logical and strong decrease in the number of Czech "shareholders" from 5.5 million in 1995 to 2.1 million in mid-2004. A decrease in the number of emissions of securities occurred simultaneously, especially those registered by the PSC, from 2233 in 1995 to 221 at the end of the third quarter of 2004. Deaths of companies or conversion of registered shares into stock certificates held by households actually make an estimate of this property impossible.

Conclusion

In mid-2004 Czech households disposed of savings amounting to CZK 1.354 billion. This volume was the sum of households' sight and term deposits and savings accounts at banks in *korunas* and foreign currency, saving in building societies, technical reserves of life insurance and deposits on supplementary pension insurance. Included are also households' investments and their appreciation in domestic and foreign shares funds incl. investment funds, and estimates of direct investment in securities and money kept at home.

As a result, savings of roughly CZK 341.3 thousand fall on one household on average. There is on average CZK 76.5 thousand on sight deposits, CZK 74.8 thousand on time and savings accounts, and CZK 65.8 thousand as saving in building societies, all per household. Also investment in funds grew markedly, reaching CZK 35 thousand per household. Population's savings in form of life insurance are nearly as high; their share in insurance companies' technical reserves is CZK 33.3 thousand per household. Lower volumes of savings per household are still reported for another product supported by the state, i.e. supplementary pension insurance: the average hitherto savings per household together with the state contributions amount to CZK 24.7 thousand. Substantially lower volumes of households' savings are in form of foreign currency deposits (CZK 17.2 thousand on average), money kept at home (according to an estimate less than CZK 10 thousand), and from direct investment in securities (about CZK 4 thousand).

⁷ Common statistics of the UIC CR and AKAT on investment in foreign funds are already available for this period.