Policy Assessment

The present policy debate in Britain is focused almost exclusively on the immediate prospects for recovery. Government ministers, who initially made a virtue of ignoring the short-term consequences of their policies, have recently been seen poring over economic indicators for a sign of an upturn. The strategy which they were convinced would secure economic growth in the long run is in total disarray, their faith in the simple principles of controlling the money supply and minimising government interference in the economy undermined by events. Every minor hiccup in the monthly series for industrial production is now liable to be interpreted as the beginnings of sustained recovery.

Yet the country remains in a deep and prolonged slump. Output growth of 1 or 2% this year would not radically alter the position. Recovery will only truly be under way once unemployment begins to come down and, as in the past, this requires output to grow by at least 3% a year. In reality, there is no serious prospect of economic recovery in the short or longer term unless policies change. Though inflation may come down, unemployment will remain high and in all probability will go on rising, albeit at a slower rate than in the recent past. Manufacturing output will remain extremely depressed and many more plants will be closed and jobs lost in the next few years. Profits will continue to be low irrespective of wage moderation and investment will fall far short of long-term needs. The government will continue to be short of money for spending on social programmes and local authorities will remain under extreme financial pressure.

At the same time, however, there is the prospect in the medium term of reasonable growth in real wages for those who remain in employment. As in the past, North Sea oil production may well provide the resources to protect real incomes against the effects of industrial decline. Revenue from the North Sea should enable the government to avoid having to raise taxes much above their present level to pay the costs of supporting a growing number of unemployed, so long as other elements of public expenditure are kept down. The burden of industrial decline will therefore continue to fall on those out of work and there is every prospect of a deepening division between these, the minority, living in social deprivation, and the majority in jobs who will continue to enjoy rising living standards. Prolonged stagnation will have created 'two nations' with a vengeance, and although in strictly economic terms it may represent a viable scenario, from a wider point of view the consequences could be disastrous.

It is the prospect of this outcome which makes a change in government policy of vital importance. But the formulation and pursuit of an alternative strategy now present far greater difficulties than used to be the case a few years ago. Not only has the industrial base of the economy been severely weakened since the present government took office, but more importantly most other industrial countries are also suffering recession and the prospects for sustained world economic recovery are bleak. Under these conditions, competition for market shares is now intense and any attempt by one country to steal a march over others is hotly contested. At the same time, short-term capital flows have vastly increased in scale and the need to avoid speculative pressure building up against a currency has become more important. Accordingly, governments both in Britain and elsewhere have become more constrained in their choice of policies. The difficulty of pursuing a radically different strategy from those followed elsewhere is amply demonstrated by the problems encountered by the Mitterrand government in France in its pursuit of expansionary policies.

Although there is considerable scope for reflation in Britain in view of the balance of payments surplus on current account which has been secured by extreme deflation, any significant expansion would run the risk of undermining financial confidence both at home and overseas. In the absence of exchange controls, the danger of initiating an uncontrollable fall in sterling and unleashing renewed inflationary pressure is a very real one. The problem is compounded by the lack of reliable estimates about the present balance of payments position. Official estimates of the size of current account surplus and the scale of capital outflows are subject to a substantial margin of error because of the Civil Service dispute last year. The likely size of balance of payments flows in the short term is therefore even more uncertain than usual.

Provided that exchange controls were re-imposed and other measures taken to minimise the risk of exchange rate collapse (possibly including joining the EMS at a suitably low rate), it would be possible to engineer a substantial reflation. Indeed anything but a substantial reflation would have an insignificant effect on the economic problems which Britain now faces. Even proposals from Conservative MPs for a budget giveaway of £4 or 5 billion which the Chancellor rejected in March would have added less than 2% to output, nowhere near enough to have much effect on unemployment. This government, or its successor, could give away as much as £7-8 billion a year (at 1982 prices) for three or four years in the form of higher public spending and lower taxes without running into serious balance of payments problems. The effects would be wholly beneficial: more income and jobs in depressed areas, a recovery in manufacturing output, fewer plant closures and some reduction in unemployment, without much risk of accelerating inflation. The fact that large-scale reflation would eliminate Britain's balance of payments surplus would, moreover, be an incidental benefit to our trading partners, since it would give them more export earnings to ease their difficulties in coping with high import fuel bills.

But though reflation on this scale might give a few years of reasonable growth and might start to bring down unemployment, it is not in itself capable of generating sustained recovery. It would scarcely improve export growth or slow down import penetration. Once Britain's balance of payments is again in deficit the growth of domestic expenditure will be constrained, as in the past, by inadequate trade performance in manufacturing. Reflation may check industrial decline but it will not of itself put the process into reverse. Strategies for recovery need to be judged as much in terms of their ability to accomplish this task as in terms of their likely effect on output and employment in the short term.

Recently the belief has grown up that in the long term industrial decline, or deindustrialisation, will even be beneficial for Britain. This is a belief which has probably gained credibility in large measure because it is still the case that only a minority of people have been directly affected by the collapse of industry which has taken place over the past few years.

There is a widening debate among industrial and social commentators about the possibility that Western countries are moving towards a new specialisation in the world economy as 'post-industrial' societies. The argument is that as traditional manufacturing shifts to developing countries, mature high-income economies are becoming centres for services and technology. Traditional industrial jobs are disappearing but, provided we adapt and adjust, a leisure- and knowledge-based society could be the eventual reward. Britain must give up industry, suggested an article in the *Guardian* on 15 March last, just as 150 years ago it put itself at the forefront of industrialisation by giving up agriculture.*

In our view, and most emphatically, the analogy is false. If Britain gives up industry as well as agriculture it will become a really poor country, especially when North Sea oil and gas run down. This is not a point of principle or abstract theory – we do not assume that in general industry is a necessary source of wealth for every country. Nor do we deny that there are new specialisations in services and technology from which Britain can and must seek to profit. There is no obvious reason why services and technology should remain a monopoly of rich countries (Third World brain-power could be as cheap and efficient as Third World labour-power). But our main point is a strictly empirical one. The loss of traditional industries has already made Britain a depressed and divided country. If manufacturing continues to be squeezed out of both home and overseas markets at anything like the past rate, there is no plausible growth rate of earnings from the export of services and technology that will rescue Britain from severe recession within the next two decades. On the contrary the trends imply that the living standards of a growing fraction of the population will deteriorate, the more so in the 1990s when offshore oil and gas production eventually goes into decline.

Problems of unemployment, poverty and dereliction are already serious enough to make policies to tackle social consequences an urgent priority. The burden of unemployment can be spread to some extent by work-sharing and by giving priority to jobs for people who have suffered long-term unemployment. But we must be clear that work-sharing and job-creation schemes will mainly entail redistribution of work and income rather than any net increase in the amount of both to be shared out.

It will be hard to avoid making existing jobs more insecure and low-paid. For example, the Layard scheme, which has attracted much political support of late, involves subsidising new, but not existing, jobs filled by people previously unemployed for a long time. If put into effect it would give a competitive advantage to those businesses expanding employment in this way and force other firms to close. The number of net jobs created would be considerably less than the number subsidised and the main effect would probably be less to reduce the level of unemployment than to increase the number of people experiencing spells of being out of work.

An effective assault on the social problems associated with unemployment and dereliction must include a large increase in spending and rehabilitation of the infrastructure and provision of community services as well as a proper level of social security benefits for all those in need – the

* John Atkin, 'Where the jobs will be in Europe in 2,000 AD'.

elderly and incapacitated as well as the unemployed. Unless this is accompanied by growth of national income it will require higher tax rates (at least in the long run) and it will tend to increase inflation. In fact the growth of public spending up to the mid 1970s marked a past attempt to tackle many of the social problems which have since been so much aggravated. The attempt in the 1960s and 1970s was abortive mainly because it was not underpinned by sustainable economic growth.

Industrial regeneration, the precondition for economic recovery in Britain in the 1980s and for survival when oil and gas run out, is plainly difficult to achieve. It requires greatly improved trends in Britain's external trade at a time when all Western countries are in difficulty and extremely sensitive to any policies which they suspect might weaken their position. Within the European Community, the member-states, instead of working towards co-ordinated policies of expansion which would be universally beneficial, are pre-occupied with hotly contesting the smallest economic advantage – whether it be a question of fish or wine, or 2% on agricultural prices, a few hundreds of millions of pounds on the Community Budget, a devaluation or the sale of indexed bonds by a national government. In this atmosphere ambitious policies to restore economic growth and regenerate industry would be hard to push through.

This does not mean that leaving the European Community would allow Britain to pursue independent policies without fear of sanction. Retaliation, whether in response to devaluation, import controls or support for domestic industry, now appears all too likely, irrespective of whether or not Britain remains inside the Community.

We continue to believe that the UK government ought to try very hard to remedy the adverse trends of Britain's non-oil trade in order to sustain growth of domestic spending and production. We strongly support reflation, devaluation of sterling *and* restraints on import penetration. So long as Britain avoids trade surpluses such policies will not harm other countries overall. Indeed they will be significantly less damaging than the highly restrictive policies pursued by the present government, which have ensured that the foreign exchange earnings from the North Sea have gone to accumulate a balance of payments surplus and have so depressed world trade.

If the international situation is an impediment, then it should be the primary aim of foreign policy to ameliorate that situation. Britain should support reflation by all countries, especially those in Western Europe. It should argue for schemes to make world expansion easier, such as energy and financial agreements between Europe and OPEC or industrial trade agreements with Japan and the Third World. Britain should also defend the right of itself and others to regulate their trade and external payments, so long as they avoid surpluses, if this will help to improve their internal economic situation.

The most crucial point, as we have stressed for many years past, is the imperative need to change trends in trade. We hope that any readers who doubt this will pay particular attention to Chapter 1 where we set out in more detail how the trends of trade are condemning Britain to chronic stagnation and show just how difficult the task of procuring a long-term economic recovery is likely to be.