an economic strategy for Labour

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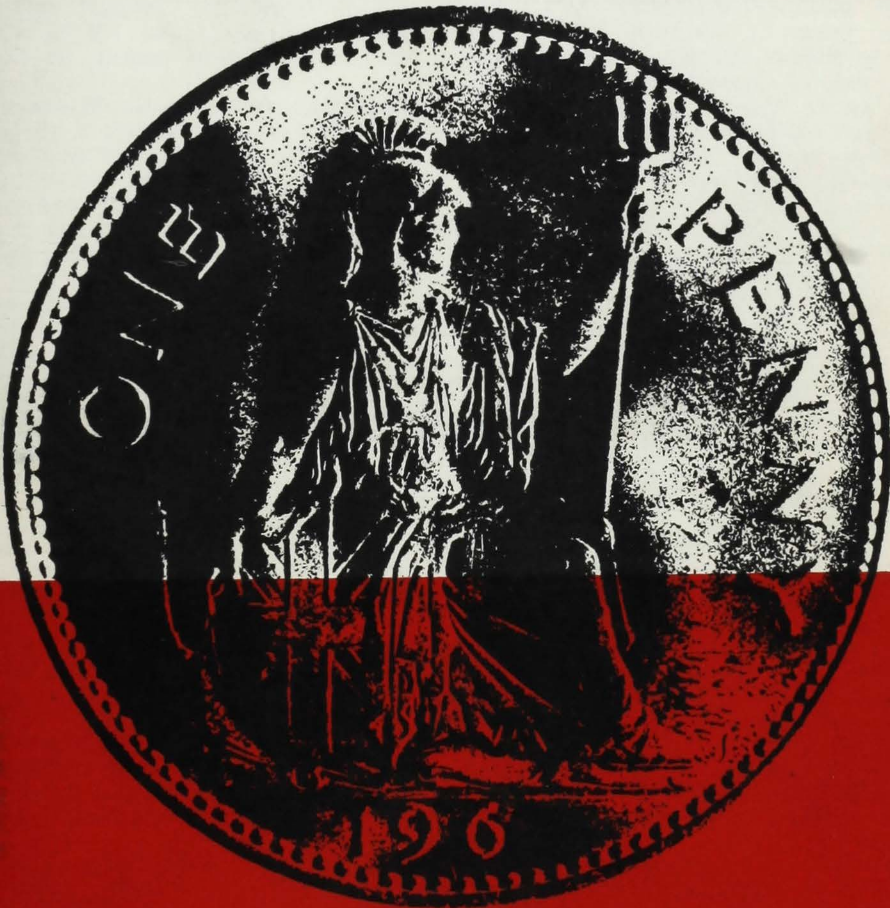

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contents

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1. background to the crises

The "freeze" carries two related meanings. There is the constraint on price and income rises backed by statutory powers that lapse in July, 1967. There is the deflation of demand within the economy, set in motion in July 1966. The deflation is partly a matter of deliberate Government action—not least by severe hire purchase deposit requirements — and partly of the subsequent "confidence" effects on business investment decisions.

Both sets of measures were called into being by a confidence crisis in sterling, rather than by overstrain, or excess demand, in the economy. One part of the policy has arbitrarily checked the rise in money incomes, the other has brought to a halt even the slow growth in real output that was occurring, and brings in its wake growing unemployment and under employment of both men and capital equipment. The situation has very close similarities to the similar currency "confidence" crises of mid 1957 and mid 1961 and their deflationary aftermaths, and this repetition suggests deep seated and unresolved problems in our economy.

To understand the real nature of the problems involved in economic management today and the special needs involved in a policy for renewed growth, we need to outline the economic problems that the Labour Government inherited. For these were not only the complex difficulties associated with the cyclical movement of the economy, inherited as these were at the point of open crisis. They also involved major problems of structural change, both externally and internally.

the cycle

A clearly marked four to five year cycle of production and demand has, with minor variations, operated in the British economy in the last two decades. We are now involved in the fourth such cycle. By now "stop go" is part of our every day vocabulary. The main features of each cycle are shown in the table overleaf. Each typically ran from a slack economy with spare capacity and unemployment. Then there has been an expansion in demand, mainly internal. This may be stimulated by tax reliefs or by lifting previous restraints on consumer credit (as in 1958); it may be helped by state sector investment (house building in 1953, acceleration of local authority and nationalised industry investment in 1963). Expansion can proceed with rapid productivity increases as under used plant and manpower are worked nearer to their capacity. Expansion of consumer durable output is marked. Prices are steady, but as unit costs fall and turnover increases rapidly, there is a sharp increase in profits. At this stage business spending on new plant is relatively low; in consequence the increased profits lead to disproportionately big increases in dividend distribution. Though wage rates rise only slowly, longer hours and payment by results systems push up earnings in the industries most affected by expansion.

The next stage is a somewhat explosive one. As the limits of capacity are reached in a number of sectors the rate of increase in output slows down; but demand accelerates. The mopping up of surplus industrial capacity leads to a wave of capital investment; fears of shortages or higher prices encourage a build up of stocks. This acceleration of demand creates areas of labour shortage and a more rapid climb in wage rates and earnings. It is here, when the real limits to available resources require extreme care in the management of demand, that successive Conservative governments have set the scene for a general election by further tax remissions. No adequate controls were attempted over key sectors, such as construction. There is a dramatic rise in import volume and a violent shift towards balance of payments deficit.

There has followed, after the general election, "corrective" budgets and the deliberate deflation of demand, particularly directed at consumer durables. A regime of higher interest rates and indirect taxes push up the structure of costs and consumer prices. Working industrial plant below its proper capacity involves a marked check to productivity improve-

GO cycles	expansion	peak	STOP stage 1	stage 2	stage 3
1	1948-50	1951	1952		1953
2	1953-54	1955	1956	1957	1958-59
3	1959	1960	1960 (end)	1961	1962-63
4	1963	1964	1965	1966	1967

Stage 1. Deflation of demand; consumer durable recession.
Stage 2. "Confidence" crisis and further deflation of demand.
Stage 3. Private sector investment recession. This stage overlaps with the recommencement of expansion in other sectors.

ment, and unit costs rise. This below capacity working spreads from consumer durables to supply industries such as steel and to distribution. At the same time the settlement of wage demands set off by the rise in profits in the boom, rising prices, a still "tight" labour market, and the "comparability" demands of groups such as public utility workers, whose earnings have lagged, continue to push up wage levels. In consequence, wage costs per unit of output rise most markedly. Thus demand is deflated, but the price level is pushed up by rising costs. Some check to this "cost inflation" comes from Britain's weak comparative cost position, profit margins come under pressure and industry has reluctantly to absorb some of the cost increases. Further wage and salary claims follow; settlements are generally "defensive", that is they do not do more than restore the purchasing power of the wage rate, but with little improvement in productivity this involves further rises in wage costs.

It is at this point in the cycle that the sight of continuing cost and price increases, and the emergence of surplus capacity, leads speculators to the conclusion that devaluation may be resorted to and we have a "confidence" crisis directed against sterling. The Government reacts by further deflation, such as the cutting of public spending, as in earlier cycles, or credit restriction, and directly attacks trade union claims. It is now possible to understand why we have such protracted periods of stagnation, for by this point in the cycle many of the big investment projects launched earlier, during the boom, are completed. The big firms see an economy with severe government curbs on demand and severe surplus capacity emerging; for example, the steel industry in 1967 is expecting to work at only 70 per cent of capacity. Investment spending contracts and a higher level of open unemployment emerges, such as in the winters of 1962-63 and 1966-67.

The cycles have thus contained the classic pattern of boom and slump, but in a modified form. This is partly because of time lags that lead to "offsetting"—one sector's recession offsetting another's expansion. The most important of these is the time lag of private sector investment behind the cycle of consumer durables. This lag is marked both in the expansion period and at the peak, usually it is over one year; for example, there was a consumer durable peak in the first quarter of 1960, the corresponding investment goods peak was in the third quarter of 1961. As we shall see later this pattern has been disturbed by the July 1966 measures, bringing a trough in durables and a decline in investment spending much more closely together. Ironically, the deliberate "offsetting" of the cycle in the private sector by variations in the level of public spending, a crude version of "Keynesian" intervention, has not worked well because it has been subject to excessive time lags of up to two years, thus reinforcing a boom rather than offsetting a recession, as in 1963-64. These lags modify the cycle and help to explain the sequence of rapid and over hectic expansion followed by a *protracted* levelling off in output.

The other modification of the classic picture of the cycle is the near price stability that characterises the expansion phase, and the later sequence of demand inflation followed by the "cost inflation" of the stop phase. One part of the explanation has already been given, that is the pressures that build up suddenly as demand accelerates at the top of the boom, and the cost raising effect of virtually every measure taken by the government in the name of "demand deflation"'. But we must also note the behaviour of both profit incomes and employment incomes in the cycle. In both cases the rate of increase in money incomes is closely related to the rate of growth of real domestic output, but the patterns are different. The regularity of the results is striking. The rate of increase in labour incomes per annum has followed the rate of increase in real domestic product but with a one year time lag and at a rate about 4 per cent per annum higher than the output increase. Over the last decade the increase in labour incomes has almost invariably been within 3 per cent to 5 per cent higher than the increases in real domestic product in the previous year. The 1965 rise in labour income of 7.4 per cent was 2 per cent to 3 per cent lower than might have been expected, since the gross domestic product rose 6 per cent in 1964. Indeed incomes policy may have had more restraining influence than has been acknowledged.

As for profits the formula for the percentage rate of growth of company and public corporation profits that gives a very close fit is 3x—2, where x is the percentage increase in real domestic product in the same year. On this formula the rise in profits from 1961 to 1965 should have been 35 per cent; according to the National Institute of Economic and Social Research's *Economic Review*, November 1966, appendix table 8, the rise in company and public corporation profits from 1961 to 1965 was exactly 35 per cent.

It need hardly be said that these two patterns represent a formula for secular inflation, and that governments have therefore challenged directly the institutional behaviour involved, as well as seeking to break out of the cyclical sequence. But it is also worth pointing out, to the trade unions, the severe limitations the "administered" market economy placed on the prospects for labour incomes. High growth rates, above 3 per cent per annum, tilted income distribution in favour of profits; low growth rates tilted income distribution in favour of labour incomes but, of course, involved a major check to the rise in real income. The barrier to favourable distribution in real terms was evidently present in the administered and monopoly dominated markets of our economy, despite the ability of unions to influence the rate of *money* wage advance. Besides, the persistent internal inflation came up against external limits as comparative costs worsened, and slowed the growth of real output, and incomes, in consequence. During the years of Conservative rule the tax burden falling on profits was considerably eased, and that falling on individual incomes became more regressive.

external structural problems

One important and continuing aspect of our export performance in the last decade and a half has been the steady whittling away of the special position enjoyed by British exports in sterling area markets. In the early post war years a combination of political domination in several of these markets and the major imbalance of world trade and payments enabled sterling area countries to be organised as a discriminatory group. At that time British exports took a 60 per cent share of the manufacturing imports of the rest of the sterling area; half of Britain's exports were going to these countries. For over a decade now, the retreat from colonial rule, and the shift to trade liberalisation, have reduced the special advantages enjoyed by British goods in these markets and Britain's market share has fallen heavily. Our trade relations with the sterling area overlap with the more general problem of the trade payments position in developing countries. In 1965 the rest of the sterling area ran a current balance of payments deficit of nearly £1300 million overall, of which nearly £800 million was with non-sterling area countries. Thus, if we look back we see a slow growth of these markets, and our shrinking share in them. A forward look is hardly more comforting. Even to support "a reasonable minimum rate of economic growth" in most of the less developed sterling countries would require a whole "series of inter-related policy changes" (A. Maizels, "Exports and economic growth in the overseas sterling area, 1960 to 1975" *Economic review*, November 1966).

To this can be added "structural" features of our balance of payments and currency position that have added to the problems of economic management. The permanently high level of military spending overseas, which is running currently at nearly £300 million per annum, is one familiar aspect, which has represented a burden on our balance of payments *of over £2,000 million in the last decade.* There is besides the persistence of heavy capital exports despite the equally persistent inadequacy of our currency reserves. There has been a marked change in the fuel balance towards imported oil which has doubled the volume of fuel imports as compared with a decade ago, these now amount to an import bill of over £600 million a year.

internal structural problems

The structural nature of regional development is by now familiar. Industries and sections of industries that have been contracting their employment (whether through market contraction, or shift to more labour saving techniques) have been regionally concentrated. For instance five major industries in which employment was contracting, accounted for 20 per cent or more of total employment in Scotland and the Northern region in the early 1960s, but only 5 per cent of total employment in London and the South East. Industrial sub-groups with rapidly expanding employment, show marked concentrations in the Midlands and South East and under representation in the industrial structure of the North. The effect on employment has been striking. In the last decade the number of jobs available for men in the UK rose by nearly a million; but over 60 per cent of these extra jobs were in the South East, while employment of men actually contracted in Scotland, the Northern region and Wales. Despite accelerating inter-regional migration, the marked discrepancy in unemployment rates between the regions was until 1964 becoming more pronounced. In 1954 and again in 1964 the unemployment rate was 1 per cent in London and the South East, and 1.1 per cent in the Midlands. But in the North West it rose from 1.5 per cent in 1954 to 2.1 per cent in 1964, in the Northern Region from 2.3 per cent to 3.4 per cent, and in Scotland from 2.8 per cent in 1954 to 3.7 per cent in 1964.

But there are also two inter-related "structural" questions of a more general, and even more fundamental, kind. Put briefly, we have been watching in the 1960s a somewhat belated acceleration towards giant companies. All key sectors of the economy are dominated, or will be shortly, by giant firms wielding considerable market power, and with plants and operations on a scale that requires careful social and economic planning since the economy of whole regions, or at least sub-regions, is affected by them. The entire question of the *social accountability* of these giants is therefore placed on the political and economic agenda. Yet, at the same time, although concentration of firms has gone far enough to represent important elements of monopoly power, or of "oligopoly" and collusive monopoly, it has *not necessarily* overcome the "structural" inheritance of obsolete techniques, small scale and unspecialised plants, locational handicaps and lack of integration of processes. For example, *The Financial Times* recently called British Motor Holdings "an alliance of small companies".

In sector after sector there is a need for major structural upheaval and rationalisation. The steel industry represents simply the *extreme* example of *both* these structural problems, and in its case nationalisation of the main firms, the essential basis for a solution. But socialists must recognise the general nature of the structural developments mentioned here; for they carry with them the vital need for the Government to use state initiative in tackling these two major structural questions.

So far as the process of concentration into giant firms is concerned, in the 1960s British industrial and commercial firms spent over £300 million each year on "take-overs", ten times the level of a decade earlier. Such a figure for "take over" spending is an inadequate measure since outright mergers, and the build up of minority holdings (often the preliminary to "take over") are excluded. In 1960 the Board of Trade found 2,241 industrial companies with assets worth over half a million; "by 1963 this total had been reduced to 2,004 companies through mergers, acquisitions, etc. (*Board of Trade Journal,* 27 August 1965). It seems clear that 1966 and 1967 are going to stand out as years of even more hectic acceleration of take overs. The sectors most affected include clothing and footwear, paper, printing, and publishing, food and drink, furniture, bricks, pottery and glass, and textiles.

The advance of the largest companies is striking. In 1954 the 100 largest industrial and commercial companies accounted for 51 per cent of the net assets of all companies with assets over £0.5 million. The proportion was 57 per cent by 1963. In 1963 firms with assets of over £25 million accounted for 90 per cent of the total assets of companies (over £0.5 million) in the chemical and allied trades. The figure was 81 per cent in metal manufacture, 75 per cent in electrical engineering and in food, drink, and tobacco.

But many of these large firms are unwieldy bags of assets. Besides, a considerable part of the "take over" process represents diversification of interests rather than the prelude to sweeping rationalisation within a particular sector. The structural overhaul of many British industries has barely started. In shipbuilding and aircraft it has needed Government sponsored investigations, and Government backed proposals for reform of the structure, to break through the barriers to change represented by the existing company structure—and even so the process of change has barely begun. For example, the steel industry; in the whole of the post-war period the number of blast furnaces in operation has only fallen from 98 to 66, and the number of separate plants producing blast furnace iron from 53 to 30. By 1965 the average production per plant was only 580,000 tons, although recent cost analyses have shown that costs in plants of this size are likely to be a third higher than in modern plants with three times that capacity. By contrast the British Iron and Steel Federation's Benson Report recently argued that by 1975 blast furnace production should be concentrated in six or seven integrated works, producing a minimum of 2½ million tons of iron per plant. Nationalisation will enable large structural changes to be planned and systematically carried through, in a socially accountable way.

There has been a further unresolved structural problem concerning the organisation and role of the public sector itself. Only now are we moving towards an integrated sectoral view of transport requirements and organisation; the same process has barely begun in the fuel and power field. We are only now, and only slowly, breaking out of the organisational approach to nationalised industries which fixed an arbitrary frontier beyond which they could not move, which subjected them to severe restraints even on their self supply of equipment. The pattern is shifting, and with the nationalisation of the large steel companies will shift more, towards flexible organisation with more elements of "vertical integration" and public competition. The purchasing of the public sector, which provides *nearly £6,000 million of orders a year for the private sector,* has been subordinated to "non-commercial" considerations.

The structure of local administration is hopelessly inadequate for modern economic and social needs. The organisation, and techniques, of central government economic action have needed, and still need, major improvement. The barriers to state sector initiative in the economic field, in forward planning, controls, participation in innovation and development, are only now crumbling. We talk of the "mixed economy" as if it were a static thing, its shape and balance fixed, whereas it is in flux and development, and in many parts of the economy it is only from now on that we will see a "mixed" economy emerge. This is to a large extent true of many aspects of finance, banking, and insurance, including the "take over" game itself, of most sectors of manufacturing, and in terms of "function" of most aspects of price and income determination. Thus Labour inherited not only an inter-related complex of economic problems, but also the historic task of evolving a new strategy in British circumstances, for economic development, for a greatly enhanced role for public sector initiative and for a more accountable economy.

TOOLS FOR PLANNERS

In its first two years of office Labour has been pursuing two different strands of economic policy. On the one hand it has been caught up in the severest balance of payments deficit for fifteen years and has adopted orthodox and relatively arbitrary deflationary measures which bore a close resemblance to those adopted in equivalent circumstances in the two previous cycles. Subsequently, and again matching the experience of earlier cycles, it found itself confronted with a speculative attack on sterling in mid 1966 and met this with further deflationary measures. This deflationary pattern and its consequences are analysed below. (For a strongly critical analysis of these deflationary measures, see John Hughes and Michael Barrett Brown in *Tribune,* 11 June 1965, and of 21 and 28 January 1966.)

But the other strand of Labour's economic measures has been the preparation of the instruments and agencies that are needed for more positive and constructive intervention in the economy. Thus future economic development does not start off from the same basis of inadequate governmental preparation and ill-designed techniques of intervention as in earlier cycles. A range of new techniques exists that can enable a coherent and selective process of forward planning and control to be pursued.

A short list of the major steps taken, some already operative, others still going through Parliament, may help clarify this. The cumulative importance of the new armoury of economic weapons is quickly evident.

1. There has been a marked development and improvement of the administrative machinery required. This is particularly true of the Department of Economic Affairs, and the regional machinery associated with it—the planning councils pushing forward regional studies with the help of the boards grouping together the regional officers of central government departments. There is the statutory constitution of the Prices and Incomes Board, and the constitution of the NEDC on a fully representative basis. The main initiatives of the state in the field of innovation have been grouped under the Ministry of Technology, and agencies such as the National Research and Development Corporation are rapidly extending their interests. The Industrial Training Boards are getting under way, in some cases with very considerable resources from compulsory levies. There has been a much more extensive use of economists in departments where their contribution to policy formation had not previously been in evidence. The Public Corporations are being allowed to develop and diversify their interests more flexibly.

2. The Building Control Act provides a system of direct licensing for use when the resources of the construction industry are subject to overstrain and social and economic priorities have to be signalled. By contrast, in the last cycle, the Conservatives launched a process of expansion that culminated in 1964-65 in severe over commitment of building and construction without having made the neces-

sary input output analyses of their programme to limit such pressure, and without the controls to establish priorities. There has been in recent years notoriously excessive commercial development of shops and offices; this is likely to leave a legacy for many years of higher distributive costs, under capacity use of premises and staff, and an excessive pull on manpower. This is the type of lopsided and erratic development that has to be brought under control. At the same time, the Land Commission will be able to contribute to a planned process of development, and limit private appropriation of the "social increment" involved.

3. The Industrial Development Act represents a major step forward in the approach to industrial location and investment incentives. It transformed the restricted approach of earlier legislation on aid to industrial development, not only by going over to the concept of major continuous development areas, but also by providing for more flexible assistance (including selective provision of loan and risk capital). It has replaced the relatively uncertain and unselective system of "investment allowances" on private investment, by a direct and potentially selective system of investment grants. These grants on new plant and equipment in manufacturing and construction have been set at the level of 25 per cent for 1967-68 outside development areas and 45 per cent in development areas. It is a major error in the current system that the capital grants are extended to the capital investment of oil companies but outright denied to the nationalised fuel and power industries, such as coal and gas, that are in direct competition with oil. Thus the element of protection that the tax system extends to coal at one level (through the fuel oil tax) is taken away again at this other level by unilateral capital subsidy to oil. A Labour Government should not discriminate in favour of a private industry that represents an import burden against public industries that are largely based, or will be, on indigenous supplies.

4. A further major element of selectivity in the system of taxes and subsidies bearing upon industrial costs has been introduced with the selective employment tax. This has so far been used for major revenue raising, rather than as a selective instrument, though the initial approach adopted has the merit of shielding manufacturing industry at this stage from any cost raising impact of the tax, clearly for balance of payments, comparative cost reasons. But it has obvious possibilities as a regionally and industrially selective tax. Its main current defect is the discouragement it gives to the use, particularly by distributive firms, of part time labour instead of full time labour. This is, therefore, discouraging a flexible use of our main labour reserve, part time women's labour, instead of encouraging it.

5. The 1965 Monopolies and Mergers Act introduces specifically a process of supervision over major industrial take overs that might strengthen monopoly positions; it therefore provides the Board of Trade with considerable opportunity of informal negotiation and influence upon the handling of mergers. One of the improvements that could be introduced into present practice would be to bring the Ministry of Labour also into the scrutiny of mergers, at present handled by a committee within the Board of Trade. Besides the directly commercial questions examined there should be a serious attempt made to examine what the effect of the merger would be on the labour force, and what provisions the firms concerned intend to make to minimise the social costs involved in such subsequent rationalisation. The Act also strengthens the range of controls that can be imposed upon firms following an adverse report by the Commission; perhaps most significantly of all it provides for the imposition of statutory price control in such a situation.

6. The Government's approach to the handling of industrial structural change, particularly through mergers, would have been inadequate and not positive in character if it had been limited to the Monopolies Act. But the new development of establishing the Industrial Reorganisation Corporation (IRC), initially with £150 million of capital, has meant

the creation of a very flexible and intelligently contrived agency. With it the financial sector becomes part of the mixed economy, and the public interest can be deployed in the rationalisation and development of the economy from a new direction. The early decision to use the IRC to examine the supply of tele-communications equipment is a good start.

7. The critically important process of rationalising and modernising the steel industry under proper social control can be pressed forward once nationalisation of the major companies has removed the barriers presented by the existing structure and ownership. This is of immense importance in influencing the costs of production in engineering and manufacturing industries, and the locational decisions involved will require the fullest deployment of the new agencies and powers available for shaping regional development. It is an immense task, and it has been helped forward by the establishment of a committee to prepare for the organisational changes needed, in essence a "shadow" board, in advance of vesting date. Of course, the earliest possible vesting date should be adopted. Similarly legislation is urgently needed that can ensure the speedy regrouping of the shipbuilding and the aircraft industry on the lines indicated by the enquiries into these industries. Time is not on our side in handling the basic overhaul of the organisational and industrial structure in sector after sector of the economy. The Government have rightly, launched Royal Commission investigations into local government and the civil service, but these areas of reform are likely to be subject to even more serious time lags. At least on the industrial front, in the field of economic organisation, the maximum effort is needed for *early* results in terms of structural reform. Also conurbation transport authorities, and the proposed freight authority, need some Parliamentary priority, and the maximum administrative preparation prior to legislative change. Integration of delivery services in urban areas, and the rationalisation and improvement of coastal shipping, much of it already owned by various public corporations, ought not to be left out of account at this stage.

8. The Government can use influence exerted by public sector purchasing. This can help take forward planning far beyond mere "indication". By 1965 total public sector purchases of goods and services from private sector firms almost reached £6,000 million a year; this was an increase of about one third in real terms above the rate of purchasing in 1960. Some strengthening of purchasing proceedures has occurred. Local authority "consortia", and the associated design work of the best of these, provide one example. Following the investigation of the Ferranti purchases the Government has moved to secure "equality of information" as to costs where it is negotiating, as with most aviation purchases, with monopoly suppliers. Bulking of orders is extensively practised by government departments acting jointly (thus the Stationary Office is the central buyer for office machinery and equipment, the Ministry of Public Buildings and Works buys furniture and fittings for all departments), *but not so far as can be judged by public corporations acting jointly*. There is much that remains to be done to develop to the full the potential use of purchasing in strengthening forward planning, limiting monopoly expoitation, and increasing efficiency in the supply industries.

In all these ways, then, the Government has done much to develop the agencies and the powers and selective pressures needed for more social control over economic development. This is not to say that these instruments are yet being used effectively. It is not to say that there exists any adequate concept of the priorities required, of the strategy to be used. It is not even to say that the political will exists to make major use of some of these measures. But the importance of having these tools available should not be underestimated. They remove henceforth one of the arguments used to justify the limited and orthodox intervention of the Government in the direction of the economy. Meanwhile orthodox instruments have been used to deflate.

2. the "confidence" crises

There were close similarities between the "confidence" crises of 1957, 1961 and 1966.

In all three the speculative attack on sterling case some time after excess demand in the economy had been most in evidence (1955, early 1960, 1964). In all cases the attack came after the current balance of payments had swung substantially away from the heavy deficits of those cyclical peaks. In all cases the government had in the period between the cyclical peaks and the speculative attack adopted measures to deflate demand; these in all cases had included higher interest rates and credit restraint, and higher indirect taxation. The restraint on demand in the economy had the perverse effect of pushing up both the cost structure and the structure of final prices. This was due to the *direct increase in costs generated by the tax and credit measures*. There was no significant offset to this from improved productivity, as the measures taken led to a much slower rate of productivity improvement.

In all cases the upward push on costs and final prices was strongly reinforced from the direction of labour incomes. The acceleration and greater pressure of claims to be noted at the peak of the cycle, with time lags in settlement, appeared as a sharp increase in wage rates in 1956, 1961 and 1965. With only a limited offset to this pressure from productivity improvement, labour costs per unit of output rise in the first post-peak year at a rate faster than at any other point in the cycle. In the latest cycle this process continued in 1966, and *by mid-1966 wages costs per unit of output in manufacturing were some 10 per cent above the 1964 average*.

In all three cases, therefore, although the stated aim of "corrective" deflationary pressures was to check inflation, *cost* inflationary pressures were more rather than less marked. Moreover, by 1957, 1961, and 1966, there was some margin of capacity and some under employment, rather than much open unemployment, of labour. The failure to improve the comparative cost position, or to stabilise costs and prices, together with the relative ease with which devaluation could have been handled (from a semi-deflated economy), may be seen as major factors precipitating "confidence" crises.

It has also to be recognised that the balance of payments improvement that had occurred between years of peak deficits—namely 1955, 1960, 1964—and the onset of speculative currency attack, did not represent any significant strengthening of the underlying position.

In all three cases, the labour market at the time of the speculative attack was reasonably in balance—without a marked trend—and with a low level of registered unemployment. The slight decline in actual weekly hours worked indicated a marginal easing of pressure as compared with the earlier peak.

handling the crises

Such similarities as there are in the handling of the three crises and the subsequent course of the economy must now be considered.

In all three cases, the reaction to the speculative attack was one of high short term interest rates and a further deflation in demand. In 1957 this took the form primarily of a limitation on public expenditure, and public investment; in 1961 of indirect tax measures and some check to public expenditure; in 1966 of indirect taxation, some curtailment of public investment, and sharp consumer credit restrictions.

In all three cases the shift in expectations caused by the further deflationary pressure on demand was followed by a curtailment of the rate of private sector investment. There was also a significant fall in the labour requirement of manufacturing industry. In 1958 and 1962 there was a fall of 3 per cent in total hours worked by all operatives.

In the two earlier cycles, the consequent recession following the speculative crisis was prolonged. In both cases the time intervals were almost identical. Unemployment increased and reached its highest point one and a half years later, industrial output did not rise again perceptibily until between one and a half to one and three quarter years later, and manufacturing investment did not rise again perceptibly until two and a half years later. There are, however, a number of reasons why unemployment is increasing far more swiftly on this occasion than in the two previous cycles:

1. In the two previous cycles the main phase of consumer durable recession occurred earlier, *before* the speculative crisis. Consequently, the earlier fall in consumer durables had partly offset the peak of the investment boom (1961, 1956-57). The *expansion* of consumer durables was already in evidence in the period after the speculative crisis, and helped to limit the extent of the recession in demand. For example, passenger car output rose from 860,000 in 1957 to 1,050,000 in 1958 and from 1,004,000 in 1961 to 1,250,000 in 1962. On this occasion, the contrary is the case; instead of the different timing of consumer durable and private investment recessions leading to "offsetting" during the period of deflation, the Government measures have severely affected consumer durables and the two recessions may coincide in 1967.

2. Private investment only fell moderately in 1958-59, and with a considerable time lag.. The speculative crisis in 1961 coincided with the peak in the investment cycle, which was strongly marked; thus although the contraction in private investment went farther in that cycle it took some time to develop. Thus manufacturing investment in the first quarter of 1962 was identical with that in the first quarter of 1961. On this occasion, the level of manufacturing investment has been almost level since the beginning of 1965, and a fall below the level of the last eighteen months or more is likely to be soon apparent.

3. Although probably of less importance, the introduction of the selective employment tax (SET) may also have some employment effect. This is not so much a matter of its restraining effect on consumer demand. The SET White Paper argued that it would have the effect of "encouraging economy in the use of labour in services . . . thereby making more labour available for the expansion of manufacturing industry". In so far as SET does encourage such economy in the use of labour in service trades, it might be expected to be particularly in evidence at the present time, for example, in distribution where total consumer demand is falling, and pressure on margins is intense, and perhaps to make even more noticeable the normal seasonal contraction in demand for labour in the service trades in the early months of the year.

4. The removal of the import surcharge by reducing the degree of protection afforded home industries competing with imports may provide a further, even if minor, depressing effect on industry's labour requirements early in 1967. It should be anticipated, therefore, that unemployment in the early months of 1967 will run at levels similar to the earlier cyclical peaks of the first quarter of 1959 and the first quarter of 1963. However, in contrast to the experience then there is at present *no reason* to expect a sharp and sustained *reduction* in employment rates. Unless a re-expansion of consumer durables commences *very early* in 1967, or there is a *major* re-expansion of private investment decisions, a plateau (seasonally adjusted) of high unemployment approaching two thirds of a million (for the UK) is the most likely outcome after the first quarter of 1967.

In the two previous cycles, output per man (and per man hour) did not resume a rapid rate of advance until the industrial output expansion became strongly marked (that is *after* the first quarters of 1959 and 1963 respectively). The slow rate of progress during the period of deflation, and the rapid advance in the period of expansion, are characteristic of both cycles. If we take manufacturing productivity—output per man hour (OMH) —at 100 in 1957, it had only risen to 103 by the first quarter of 1959, but rose to 110 by the first quarter of 1960. Likewise, if we take 1961 as 100, it only rose to 105 by the first quarter of 1963 and then rose to 114 by the first quarter of 1964. The slow rate of increase in productivity during the deflationary period did at least have the consequence that unemployment rose less than might have been the case. If OMH at the present time were to rise more than 2 per cent to 3 per cent per annum, the unemployment level in 1967 would be correspondingly higher than anticipated above.

The consequence of the slow rise in productivity in the earlier deflations was an inadequate productivity "offset" to increases in costs during the phase of stagnation. Consequently *the trend of costs and prices was upwards,* despite the constraint that more depressed markets may have exercised on both wage determination and price fixing, and even despite sharply reduced import prices in 1957-58. From 1957 to the first quarter of 1959 "final" prices rose 3.4 per cent; again, from 1961 to the first quarter of 1963, "final" prices rose 3.8 per cent (retail prices actually rose 6 per cent).

By contrast, the *trend of prices was much more favourable in the first year of re-expansion* despite a less favourable trend in import prices at that point in both the earlier cycles. In the year of expansion from the first quarter of 1959 "final" prices *fell* 0.8 per cent; in the year following the first quarter of 1963 they rose only 1.8 per cent.

The analysis suggests forcibly that *early re-expansion* of the economy should be the objective of the Government at the present time. Such a restoration of economic growth is needed if unemployment is to be prevented from running at a socially damaging and economically wasteful level. And such a restoration of growth offers a better prospect of cost reductions and price stability than our present surplus capacity and slow productivity improvement.

3. expansion

BALANCE OF PAYMENTS

Are balance of payments considerations an obstacle to early expansion?

There is little evidence that the underlying balance of payments situation on current account has improved as a result of the measures taken in the last two years. In 1965 as in 1961 the improvement in the trade balance, after allowing for the temporary effect of the import surcharge, appeared as slightly less than the decline in the rate of the build up of stocks. In 1961 the trade balance as compared with the previous year was up £255 million, but stock build was down £272 million. In 1965 the trade balance as compared with the previous year, was up £213 million, taking into account the effect of the import surcharge, which is estimated at £60 million whereas stock build was down £218 million. Given this evidence of the relation between shifts in the trade balance and in stock build, these figures hardly suggest anything more than "level pegging", though it should be noted that the gross domestic product (GDP) in real terms is estimated to have increased 2.7 per cent in 1965 as compared with only 1.8 per cent in 1961.

Provisionally export volume in 1966 shows only a 3 to 4 per cent rise over the previous year though the rise in export volume late in 1966 may represent a welcome improvement. The further improvement in the balance of payments still appears to be largely associated with the recent decline in imports, that is it is at the expense of economic growth. Nevertheless, it can be argued that an early re-expansion of industrial output is urgently required if there is not to be excessive under use of manpower and plant; it would be much better from the point of view of stability of costs and prices (and therefore our comparative cost position) than a more protracted deflation; and is not likely to affect the balance of payments adversely, if the re-expansion is selectively handled.

The contrast in terms of productivity growth, and price trend, between the period of deflation and the initial stages of expansion has been clearly shown. Over the last decade *all* the years in which manufacturing output stagnated or grew slowly have been associated with an OMH rise of between 1 per cent and 3 per cent. All the years in which manufacturing output rose 4 per cent or more have been associated with an OMH rise of 5 per cent to $5\frac{1}{2}$ per cent per annum.

On the side of wages, the initial expansion phase, because it is associated with more stable prices and higher unemployment levels than normal, has characteristically also seen only a slow rate of increase in wage rates.

To assess the extent to which balance of payments considerations require a prolonged stagnation of the economy, it is also necessary to judge the impact on the balance of payments of a renewal of growth. In the first place this requires an examination of the previous cycles, in particular of the expansion phase in each. This is shown in the table below.

THE EXPANSION YEARS

	1952-55	1958-60	1962-64
balance of payments (£ million)			
at the start	+163	+336	+101
following year	+145	+136	+107
"peak" year	—155	—275	—393
increase over the expansion phase			
gross domestic product	+12%	+10%	+10%
manufacturing output	+20%	+15%	+13%
consumer expenditure	+13%	+ 9%	+ 9%

The three recovery phases were quite similar in scale. In the last two the rise in GPD was 10 per cent, in manufacturing output from 13 per cent to 15 per cent, and in personal consumption it was 9 per cent. Only the 1958 cycle started from an exceptionally strong balance of payments position on current account. That was by its nature transient, as it owed much to the sharp fall in import prices of raw materials and some foods, which in its turn—but with time lags—lowered the purchasing power of primary producers; thus 1959 exports to the overseas sterling area fell and this helps to explain the more evident deterioration in the balance of payments in the first year of recovery in that cycle.

With the exception of 1959, for which a specific reason has been advanced, the experience has been that *the balance of payments is relatively stable in the first year of the recovery phase.* The deterioration is concentrated mainly on the second year; this is evidently associated with lack of control of aggregate demand, the tendency for demand to accelerate, because, for example, private investment revives just when capacity reserves are being exhausted. Therefore the balance of payments problem associated with recovery is very much a matter of the degree of selectivity and control operating in the subsequent stages of recovery. This means that balance of payments considerations should *not* be seen as a barrier to very early recovery of a respectable growth rate but that they must be seen as requiring the development of more selective and ramified influence over all sectors of demand during the early period of re-expansion to lay the basis for controlled and sustained growth. This is the point where the stop go cycle has to be changed into more planned growth. The following immediate policy conclusions might be drawn from this.

1. There is no reason to expect that re-expansion would produce a marked deterioration in the current balance of payments. It is therefore reasonable to aim at preventing excessive under use of capacity, excessive unemployment, and a loss of real output and wealth in 1967. As the likely rise in OMH in manufacturing under recovery conditions is *over* 5 *per cent per annum,* the expansion of manufacturing would need to be of the order of at least 6 per cent in 1967 to enable a slow contraction in unemployment rates. It would be reasonable, therefore to aim at a GPD increase for 1967 compared with 1966 of 4 per cent heavily concentrated (for reasons discussed below) on manufacturing and construction. Given the level of output to be expected by the last quarter of 1966, this may well imply a 10 per cent increase in manufacturing output from beginning to end of the year, and 6 per cent to 7 per cent for the increase in manufacturing output on average in 1967 over 1966.

2. This would be compatible, on the evidence of previous cycles, with little overall increase in the total hours worked in manufacturing. It has already been pointed out that the trend of unit costs and final prices should be particularly favourable in this phase. Unemployment rates could be expected first to stabilise and then fall gently. The re-deployment of manpower would depend on the priorities established for the re-expansion of demand. The improvement in the comparative cost position that could be expected, and available margins of capacity, should assist the growth in exports.

3. Priorities for growth should be chosen which are likely to bring most medium run benefit to our comparative cost position and which reduce the import requirement involved in a given expansion of output. The first of these considerations points to the urgency of proceeding with major structural re-organisation of important industries such as ship building and steel. This also involves a deliberate deployment of *strong* fiscal inducements to *time* private investment now; the techniques for handling this with minimum cost to the Exchequer are outlined later on. There should also be a controlled phasing of certain public investment projects; investment in gas distribution geared to North Sea gas should be accelerated. Care should be taken to see that public investment is not building up to a 1968 peak, but is deployed in 1967 and then committed to a more modest rate of advance in 1968. The bunching of electricity investment currently is a help in this. Unfortunately *steel* investment, unless the Ministry of Power proceeds urgently to back given investment projects, is likely to show the wrong timing.

4. The notion of reducing the import requirements attached to any given increase in output is largely a matter of taking seriously input output analysis. *Economic Trends* (August 1966) showed the primary input of imports in 1963 as 16 per cent of output. However, certain sectors show much lower rates of import input per unit of output. The most important are engineering and allied industries, 10 per cent, construction 11 per cent, and gas, electricity and water, 6 per cent. The latter may have changed with increased use of oil as a base material, but will fall again with substitution of natural gas. Thus, a recovery heavily based on engineering products and expansion of construction has a relatively low import content. This, it should be pointed out, means that the import content of re-expansion in consumer durables is not high. Unfortunately the 1963 input output tables show that the import content of gross domestic fixed capital formation was higher, 15 per cent, thus maximum attention would need to be given to helping British manufacturers meet capital goods orders, so that ordering of imports of capital goods from abroad is limited.

5. It may be argued that although the primary increase in demand may be concentrated on sectors showing low import content to output, the secondary effect will be felt through increased consumer incomes. The import content of personal expenditure in 1963 was as high as 19 per cent. This has some important implications. Firstly, in the expansion phase of previous cycles, personal consumption increased by $4\frac{1}{2}$ per cent per annum in constant prices. Input output figures indicating the "marginal" propensity to import are not available, but it may well be higher than the average rate mentioned above. Besides, in relation to *factor cost* consumption, imports of goods and services account for 22 per cent of consumer expenditure. Some limit at the margin has been set by the imposition of a £50 foreign travel allowance; this limit should be retained.

Secondly, the rate of growth of personal consumption should be restrained. This is more likely to be in evidence than in previous cycles, since there is a sharper pressure directed against money increases in earned income. Besides this, marginal tax rates are higher; the income tax has been biting into lower levels of real income. It is not suggested that there should be major cuts in indirect tax rates, as have been used in earlier cycles, but the tax structure must be made less regressive and permit a faster increase in the real income of low income households. Currently, if consumer expenditure rose 4.5 per cent in real terms in 1967 as compared with 1966, and assuming the import content of increased expenditure was 20 per cent, there would be a £200 million per annum increase in imports. But if the rise were restrained to 3 per cent, this might reduce the imports involved by £60 to £70 million as compared with the figure just given, so the increase would be of the order of £130 million.

Approximately a 4 per cent increase in GDP in 1967 over 1966 would mean an additional output expenditure of £1,200 million at constant prices. If this were made up of about £600 million of non-consumer expenditure with an import content of 12 per cent and about £600 million of consumer expenditure, the total increase in imports implied might be little more than £200 million. The increase in export volume could be expected to exceed that.

The Central Statistical Office should make a more elaborate household expenditure survey than usual, in conjunction with other sources of information, in order to attempt to build up a more adequate analysis of the import content of consumer expenditure, so far as possible by income (or expenditure) groups, and by region. It may well be, for instance, that the "marginal propensity" to import goods and services when incomes rise is higher in the South East region and lower in the North, so that a given increase in consumer incomes might pull in fewer imports in the latter region.

But subsequent expansion of the economy, beyond 1967, involves wider problems of managing growth and the balance of payments. For the last decade an average growth rate of less than 3 per cent per annum is all that import and export trends would allow, without the current payments balance deteriorating. The Labour Government would be failing, in face of the unsatisfied social needs in our economy, if it tacitly accepted this and worked within such a slow growth rate. An average growth rate of less than 3 per cent in the later 1960s would limit the rise in personal consumption per head to little more than 1 per cent, given the rise in the dependent population and the associated rise in social investment needs. That would scarcely be the base on which to build a "consent" incomes policy.

The urgent need then is to improve comparative costs significantly during the later 1960s (supporting the growth rate en route, if need be, by specific short term measures to strengthen the payments balance and reserves) to make feasible a higher average growth rate. The real choice, here, is between a combination of policies aimed at sharply increasing efficiency and stabilising or lowering prices, or on the other hand devaluation.

For the first of these alternatives, a strong emphasis on the structural reorganisation of British industry, and a significant improvement in the Government's own economic management of prices and incomes, and tax structures and credit costs that affect cost levels is needed. Improvement in our comparative cost position cannot be built out of prolonged deflation, with its depressive effect on industrial investment, and the defensive emphasis it encourages on job retention and demarcation on the part of workers. Reflation, we have argued, offers a better short term prospect of cost and price stabilisation and reduction than does continued under capacity operation of the economy. But beyond this we cannot expect a further development of prices and incomes, important as this is, to take all the strain of adjustment in our comparative costs; what can be aimed at in incomes policy is discussed in a later section. It must be emphasised that this strategy for higher growth rates and a stronger foreign trade position *must* aim at significant structural reforms in industry in the *medium* and the longer run. This means using state power and influence to accelerate and push through within a framework of social accountability, major structural changes that will concentrate production in large specialised firms able to take fuller advantage of large scale economies and access to advanced techniques in every aspect of management, production, research, and marketing. This must be supplemented by more emphasis on standardisation and improved utilisation of labour and plant to reinforce the reduction in unit costs. It requires also more extensive participation by state agencies in research and development, and in subsequent production and commercial exploitation of innovations, to accelerate the introduction of new techniques into standard industrial practice.

If Labour policy cannot reach out to such a strategy then it would be better to devalue than to succumb to slow and uncertain growth. *Both* policies, structural reform and devaluation, assume that export demand and our demand for manufactured imports is responsive to comparative prices. Devaluation works by creating a profit inflation in exports (and home substitutes for imports), thus redirecting business effort in these directions. If such profit expectations were confident enough more business investment would be export orientated, and the competitive advantage might be prolonged. The short run income distribution effects would on the whole be adverse to wage and other non-property incomes, though the rise in output would make possible some short run growth in real income for production workers. A moderate devaluation, say 15 per cent, would not imply major internal price increases, least of all in the near future when a high rate of productivity increase is possible. Our indigenous agriculture and fuel supplies (coal, natural gas) would become more competitive; some of our "invisible" earnings, such as shipping, should improve. But price controls and selective subsidies would be needed for some time to ease the impact of devaluation on final prices.

By contrast the alternative strategy, that is argued for here, requires a considerable pressure on home costs and profit margins, and offers profit advance mainly as a consequence of rationalisation. Its short run income distribution effects are not adverse to earned income. It emphasises public sector initiative and leadership in reorganisation whereas devaluation relies on the market mechanism mainly to signal a change of direction to business.

But if structural reform is preferred to devaluation, there has to be a readiness to strengthen our balance of payments position through short run measures, rather than allow external factors, such as the likely check to growth in the USA this year, to slow our growth. Of these short run measures the most important one within our own direct control is a rapid and continuing reduction in our overseas military expenditure; it is critically important that major savings here should accrue by 1968-69. The other short run defences for our payments and reserve position might include the following:

1. Prepare a system of import quotas for use at a later stage if the planned domestic expansion is checked by balance of payments deterioration. These should then be used early, and moderately, rather than late and severely. The likelihood of such measures being used may cause a speculative increase in imports at a certain point, hence the case for acting promptly and having the administrative system ready to hand.

2. Part of British residents' holdings of overseas portfolio assets should be compulsorily acquired, on reasonably generous terms, to help increase the available degree of liquidity. Possibly about £1,000 million might be the required amount. This should not be seen as an alternative to the negotiation of long term loans to replace some of the short term borrowing that has been necessary in recent years. But long term loans are somewhat inflexible, and at current interest rates expensive.

3. The indirect tax structure could be modified to increase the profitability and attractiveness of exports (remission of indirect taxes falling on exported goods is acceptable within GATT). The most important indirect tax falling on business costs and not yet rebated at all to exporters is *local authority rates*. There would not appear to be any objections in principle, nor any administrative problems in practice, if firms were to receive rebate of their local authority rate payments in proportion to their export turnover. This is not to suggest any element of "de-rating", but rebates by the central government to the firms. A more complex measure would be the adoption of a value added tax, to be fully rebated on exports. This would be likely to generate "cost push" effects which would offset its value as an export aid, unless some other tax falling upon the structure of business costs were reduced, such as the incidence and level of SET.

4. Full support should be given to a positive conclusion to the Kennedy Round in the form of tariff reductions; at least an extensive range of interim reductions should be sought. This is important if the trade diversion effects of the Common Market's external tariff are to be reduced.

5. Britain should pursue its multilateral initiative to lower international short term interest rates. It should be possible to make progress here if in the first place Britain and America will co-operate over the lowering of short term rates. A lowering of these rates by, say, 2 per cent could result from an elementary exercise in central bank co-operation, without involving any marked changes in the existing interest rate differentials, as between different centres. This would ease the current account burden of the UK and allow a more flexible internal monetary policy.

6 The Government should use a strengthened Companies Act, the Econo-

mic Development Councils (EDCs), and direct enquiries pursued wherever state agencies are major purchasers, to probe the firms and sectors of industry that are standing outside the export effort or contributing inadequately to it. The leverage of purchasing should be used to require firms anxious to secure major government contracts to show vigour in exporting; the Industrial Reorganisation Corporation (IRC) should be used where undue fragmentation of firms and small plant size and lack of specialisation are the main barrier to immediate participation in exports.

But such steps are only adjuncts to a wider strategy for the overhaul of the economy. The next three sections attempt to indicate what a short to medium run programme of action might look like on three important fronts, consumer durable industries, investment strategy, and the future deployment of incomes policy.

CONSUMER DURABLES

The consumer durable industries, and notably among them, the motor industry, have experienced peculiarly unstable market conditions for more than a decade. The home market shows a strongly marked four to five year cycle of activity, and marked seasonal variations. These cyclical patterns instead of being "offset" by state intervention (such as changes in hire purchase terms and purchase tax) have been accentuated by them.

To take the case of motors, the three cycles of passenger car output (in the early 1950s, late 1950s to 1961, and subsequently) show an almost identical fluctuation. In the "trough" years output was 20 per cent below the long run trend of passenger car output; in the "peak" years in each cycle it was 16 to 17 per cent above the trend. But although the proportions have remained so similar the *scale* of the industry and its importance in the economy have been greatly increased. The same proportional fluctuation is now about three times as large in output terms as in the cycle of the early 1950s. There is every reason, therefore, to be more concerned with damping the cyclical and other instabilities of these industries.

The case for closer attention to planning and stabilisation in this sector rests not only on the growing scale of their instability. Extensive surplus capacity much of the time, and short run pressure on total capacity at others, has adverse economic effects. It is likely to be associated with less capital intensive methods of work, and the retention of obsolete equipment. Demand inflation involves severe disruption of the economies of large scale flow production. The reliance of the industry on labour intensive techniques and the exposure to sharp cyclical changes in markets have damaging effects on "wage drift". The consumer durables industries need additional labour in the expansion phase and to attract it through high earnings opportunities, to compensate for the insecurity of both earnings and employment.

current needs and opportunities

For the motor industry the July deflationary measures accentuated both seasonal and cyclical troughs in the last half of 1966. For *household* durables, the first half of each year represents the seasonal trough in sales. Retail organisations selling mainly to working class families, where the HP curb on demand is particularly apparent, were showing sales in the fourth quarter of 1966 running some 40 per cent lower than a year earlier. Thus, severe reductions in retail turnover in household durables, with the consequent impact on production, are to be expected in the early part of 1967. Removal of the import surcharge is likely to increase the downward pressure on home production. If there is a strong economic case for reflation of economic activity, the handling of consumer durable industries, especially the motor industry, in the context of a planned expansion of the economy should be examined in some detail.

The current degree of surplus capacity in the consumer durable industries may well represent a serious disruption of their productive efficiency. Earlier studies of government induced recessions in consumer durables have shown the consequences of such disruption. These included reduced ability of manufacturers to forecast sales and to plan production schedules; cost increases from interruptions in production schedules, stocking of materials and finished goods, and added production and distribution costs as manufacturers attempt to meet the changed market, through wider product range, model changes and increased sales promotion per unit. The conclusion of such studies has been that undue reliance on restrictions falling on durables may reduce productive efficiency in these industries, resulting in inflated costs and prices for the consumer at home and a loss of competitive power in overseas markets. The substantial recent rises in home market car prices is, as the *Financial Times* rightly said, "a short term solution to a crisis brought on by the dislocation of previous months" (4 February 1967).

A number of measures are needed to remedy this situation:

1. There should be a cost and efficiency study immediately, initiated by the DEA, to attempt to assess the degree of capacity use in durables below which unit costs rise more sharply and problems of short run adjustment multiply. Such a study, however provisional its conclusions, would be a valuable aid to policy.

2. There should be a readiness to adjust the temporary tax and hire purchase measures to enable the consumer durable industries to move up from levels of capacity operation that are uneconomic towards a level that does not seriously hamper productive efficiency. This might, in practice, be about 85 per cent of "normal" capacity.

3. As there would be no economic benefits from a speculative postponement of purchases by consumers till after the April budget (such postponement would intensify seasonal contraction in household durables), there should be a clear statement by the Government on its short run tax and HP intentions towards consumer durables. It would be advantageous to remove the purchase tax "regulator" surcharge at once on durables, but to state that no further reduction in purchase tax would take place in the April budget. On the other hand, the surcharge of tax on petrol should, for balance of payments reasons and encouragement of economy in use, be maintained and consolidated in the April budget as the new "normal" rate. Some easing of HP terms is likely to be immediately justified for household durables. As the normal car purchasing peak is March and April, further improvements in HP terms should only occur at a later date, possibly in June or July; this would help offset seasonal contraction in sales.

4. After some attempt has been made to move consumer durables to a less damaging degree of under capacity operation, it should be made clear to the industries concerned that further domestic relaxations beyond this point will directly depend on export effort and performance. This "payment by results" approach should not be too rigidly linked to an arbitrary "target", since the conditions met in export markets are far from uniform year to year. But the DEA and Board of Trade should discuss in detail with manufacturers the market position and potential in all major markets, and satisfy themselves that a significantly increased export effort is being made before further easing of home market restraints occurs. The IRC should be used to overcome the small scale and fragmentation of organisation in household durables; without this much of this sector may not be internationally competitive.

5. There needs to be a more co-ordinated approach to exports. The erratic performance of specific markets, entry barriers, and the growing pressure of trade diversion effects, must all enhance the degree of risk attaching to production, design, and capacity which is geared primarily to the requirements of export markets. For all these reasons, the

Government should satisfy itself that systematic market research is being undertaken on overseas markets, to improve the reliability and security of forecasting, and forward planning of exports. What is important is that the British firms concerned should work as a consortium in such market analysis (along with the relevant government departments) to reduce both gaps in coverage and uneconomic overlapping and duplication of work, and that the information should be available to all the firms concerned. Since major inroads into specific markets require a considerable commitment to sales and servicing networks in the countries concerned, the Board of Trade should specifically review such activity (or lack of it). It should directly encourage co-operation in such marketing "investment" by British companies where there would be evident economies and benefits (or direct mergers to overcome fragmented marketing). It should review the aid that can be given to such development by the state, such as lower interest rate loans through the ECGD or other credit agencies.

6. The Government should also be prepared to initiate, sponsor, and financially aid, reseach, design, and development work aimed at producing models more specifically related to the requirements of major markets overseas. In part such work and associated development contracts might be able to link with co-operation between Ministries, such as Overseas Development, with the forward planning of developing countries. Thus, the development of a tough easily maintained car for assembly in developing countries might be relevant. There should be a much more extensive involvement of the Ministry of Technology in the major development work of these industries. In the case of television this is clearly related to the timing and handling of colour television. In motors there is a long list of very important developments which should be guided, influenced and accelerated by Ministerial participation in research, sharing of risks, such as in National Research and Development Corporation (NRDC) projects, and development contracts. One of the most obvious of these is the development of an efficient electric car for town use which offers the multiple advantages of reduction in import requirements of oil, reduced levels of noise and air pollution, and some aid in easing congestion through better use of road space. Such a development would also have very significant export potential. There is also urgent need for establishing design standards that incorporate a higher degree of car safety ; this should go along with the more stringent setting and application of safety standards by the Ministry of Transport. Similarly, with development work to reduce the pollution caused by petrol and diesel engines, and the development of more stringent Ministry of Transport minimum standards. The Ministry of Technology might consider what further could be done, perhaps by substantial design awards, to reward firms who make major advances in fuel economy. Virtually all the subjects mentioned here have considerable balance of payments or direct export implications to them.

7. The economic ministries should consider what measures to take for more efficient deployment of consumer durable, and especially motor industry, resources in current production. Emphasis should be placed on encouraging capital intensive systems of production as the basis for future capacity expansion in the next phase of advance. It has earlier been argued that considerable scope exists for a shift to greater capital intensity, as the unstable development of recent years has acted as a barrier to investment in more advanced and less labour intensive methods. The Ministry of Technology and DEA might follow up the preliminary study of costs and efficiency suggested earlier by investigation into the state of technology in the major car and other durable goods plants. Such a study might usefully embrace not only actual cost comparisons of the yield to be obtained from various types of plant, etc., but also a study of quality control on which for cars there may be a case for introducing permanently a measure of independent supervision. In conjunction with such a study the direction in

which more selective fiscal pressures might be taken should become apparent. It may be that for certain types of equipment the life assumed for tax purposes does not enable a rapid enough process of writing off, given the insecurity of the economic climate in these industries. Perhaps more variation in the rates of capital grant are called for. Consideration might also be given to introducing SET charges and offsetting those by higher rates of capital grant on plant and machinery. This could be managed so that no net increase in costs occurred; but as the *relative* prices of labour and capital equipment to the firms would change a "substitution" effect would be produced, that is, profit maximisation would now be secured by choice of a more capital intensive technique than hitherto.

8. There should be a serious attempt made by the Ministry of Labour to establish in conjunction with all major plants in these industries a system of manpower budgeting. All plants should draw up firm plans as to manpower requirements for the immediate period ahead, and outline plans for longer periods; there might need to be penalties for non co-operation. There should be notification of any change in planned requirements, so that adjustments can be made, for example, in recruitment rates, in the way that throws least strain on the workers directly involved and on the labour market of the region concerned. Needless to say this process would be helped if the government, on its side, were to co-operate by limiting the severity of the short period adjustments it requires of the industry, and wherever possible making such adjustments with the maximum degree of consultation with industry.

9. There should be further study of the seasonal patterns of production and sales in the consumer durable industries. Greater economies could be achieved by the pursuit of measures to limit the range of seasonal fluctuation. One obvious possibility would be the introduction of *regular* seasonal variation in the HP terms used. In the case of most household durables there is a very marked seasonal peak to sales in the fourth quarter of each year; by contrast first quarter sales may be between a third and a half lower. Better loading of distribution and production might be achieved by a lower HP requirement in the first part of each year and a tighter HP control operating in the fourth quarter. For motors, the seasonal pattern is different. For passenger cars there is a very marked seasonal peak in March/April, and much lower levels of purchasing from August to December. For example, if the "normal" HP rates prevailing are 25 per cent down for a maximum contract length of two and a half years for passenger cars, this rate might be the actual HP used in January/February and in mid-May to July; but it could be adjusted so that a more stringent rate (say, 33 per cent down, with 2 years to pay) might operate from March to mid-May, and a less stringent rate (say, 20 per cent down with 3 years to pay) might operate for purchases in August/December. Government intervention to vary HP terms could then be conducted in terms of varying the "normal" rate, which would alter the whole structure of seasonally adjusted HP terms. All too frequently in recent cycles (as in the current one) the most severe HP terms are applied during the period of seasonal slack in sales.

10. Where bulk contracts are being placed firms should be encouraged to give larger rebates to orders that involve long period contracts with planned delivery rates, especially if these fall outside the seasonal peaks in demand. More attention should be given to the integration and forward planning of *public sector* ordering, with planned phasing of delivery dates. In the case of motors this could yield substantial economies in the public sector if linked to integrated arrangements for maintenance, transport pools, and concentration of public orders on a limited number of car and lorry types. This is really outside the consumer durable field as it applies to commercial vehicles. But much light van production is closely linked to car production. The Government should use these large public contracts to secure more favourable

terms for the public sector, while directly helping the manufacturers to plan and phase their production.

INVESTMENT STRATEGY

Government statements about investment recently have been insufferably complacent, especially those emanating from the Board of Trade. It is, therefore, worth clarifying what is happening. In the last cycle the investment "peak" never appeared, but was flattened off. From the peak in 1957 to the next peak in 1961 there was an increase in manufacturing investment of over 20 per cent in real terms, but from 1961 to 1965 there was no increase at all. In recent years the long period growth of manufacturing investment seems to have come to a halt. Another way of looking at recent performance is to relate manufacturing investment to the "gross product" (or value added) of manufacturing as shown in the table below.

MANUFACTURING INVESTMENT AS PERCENTAGE OF "GROSS PRODUCT" OF MANUFACTURING

year	peak	trough
1957	14%	
1959		11.5%
1961	15%	
1963		11.5%
1965	12.5%	

The 10 per cent decline expected in 1967 is likely to push the proportion of manufacturing investment to "gross product" well down below that in previous investment troughs.

What is emerging is very far below the modest investment estimates of the National Plan. This stated (p59) that manufacturing investment needed to *average* 25 per cent above the 1964 level for the whole period to 1970 to achieve the capacity, etc., required for planned levels of ourput, and, one must add, to help lower unit costs to strengthen our comparative cost position. In fact 1965-66 were only 10 per cent above the 1964 level, and 1967 might well be back to the 1964 level. This would mean either abandoning the National Plan projections or envisaging a level of manufacturing investment in 1968-70 averaging over 40 per cent above the 1964 level. The latter would imply such a violent expansion from the current projections for 1967 that it clearly would invite inflationary and balance of payments pressures, and imply an acute problem of economic management if a repetition of "stop go" were to be avoided. On top of all this, one must see even the National Plan projections as modest ones by comparison with other "high investment" economies.

This is not the only sector of investment that must cause deep concern. The national Plan's assessment of social investment in the later 1960s was relatively restrictive and conventional. It is quite evident that a major re-assessment of the pattern of fuel and power industry investment is called for. And there has never been any adequate overall survey of commercial investment, and its consequences; it is virtually certain, however, that the cumulative effect of one speculative development programme after another has been to provide a quite excessive expansion in shop capacity. In "real" terms turnover in Britain's shops can only be expected to grow slowly in the latter 1960s (probably by less than 15 per cent from 1964 to 1970); thus wasteful and cost raising surplus capacity has most likely been created. Equally, there has been until very recently, confusion as to the criteria to be applied to transport investment. Here, disintegrated operation (and hence overlapping of routes, a high proportion of empty running and so on), inadequate forward planning and market research, unselective traffic management, and patchiness in public works and urban development have all inter-acted.

Thus in investment policy there are outstanding problems of management, including criteria in choice between alternative projects, the inducements to use and the selectivity with which they should be applied, location, and phasing. The last named point involves not just a short run matching of demand to the capacity of supply industries, but also the need for some firm decisions as to the desired rate of growth of capacity in the supply industries, such as construction, and machine tools.

manufacturing investment

In all the previous cycles the investment cycle has lagged between a year and eighteen months behind the consumer durable cycle. This pattern implies a decline in investment in 1967, and a sharp revival later in 1968 (probably when other sectors are nearer capacity working). The Government should *strive very hard to break the cyclical pattern*, particularly by encouraging cost reducing forms of investment as well as selective increases in capacity within the framework of the National Plan. Among the steps that should be taken urgently:

1. The DEA should check where investment decisions are falling short of the capacity (and emphasis on cost reduction) needed for the attainment of the National Plan by 1970.

2. This, of course, implies that a realistic re-appraisal of the Plan itself is being pursued so that at least the main sectoral projections and main social priorities have been reworked. This has to be a continuing process if a "credibility gap" is not to develop.

3. The system of capital grants should be used more selectively and with far more emphasis on encouraging the retiming of investment to bring it forward into 1967 and early 1968. The stepping up of the standard rate of grant from 20 per cent to 25 per cent for 1967-68 is inadequate. Its effect, if any, may be a bunching later in 1968, and it may *succeed only in giving more subsidy without any guarantee that a higher level of investment results*. Thus if a firm's manufacturing investment fell to 80 per cent of its 1966 level, it would still receive as large an investment grant as before. For an investment fall of less than 20 per cent firms are being paid a *bigger* subsidy for investing *less*! It is an ill-contrived use of taxpayer's money. What might be more effective would be to *lower* the standard rate of capital grant (say to 15 per cent) but to offer a 40 per cent rate of grant at the *margin* on all investment by a firm in excess of, say, 80 per cent of its average investment in the previous two years. This high marginal rate should only be guaranteed on actual spending up to mid-1968. This would cost the Exchequer less than the present method unless it were highly successful, and would be a much sharper investment incentive. It would only cost more where investment rose to one third above the 1965-66 level. This is on the assumption that, as now, investment in development areas carries a capital grant 20 per cent higher still than the standard rate.

4. The capital grants should, logically, either be withdrawn from oil industry investment and investment in electrical generating equipment by firms for their own use, etc., or extended to the nationalised fuel and power industries. The latter suggestion is equivalent to a continuing process of capital write off; it would be an obvious way of easing the transitional problems of coal and sharpening the price cutting appeal of gas. An economist must be less enthusiastic about capital grants to electricity supply without the quid pro quo of more realistic pricing of electricity used at peak periods.

5. There should be extended use of the development contract system and of direct government participation (mainly via the Ministry of Technology and its associated agencies) where innovations and major development work are at stake or might otherwise be retarded. The National Research Development Corporation (which, inter alia, has a hand in hovercraft development) "on present estimates" does not expect to be committed until "early 1968" up to the limit of its present borrowing powers. Those borrowing powers are limited at present to £25 million. This is ludicrously retrictive. Nor it is yet clear that the Atomic Energy Authority is diversifying on any significant scale. This is certainly

the right moment to give selective encouragement to the further rationalisation and strengthening of the machine tool industry, possibly in conjunction with the IRC.

6. Where the slack in home orders for capital goods industries is leading to uneconomic under capacity operation, further measures should be taken to strengthen the position of the industries affected. There may be limited possibilities of supporting the production of certain standard types of equipment for stock by advancing low cost or interest free credit. It is certainly the point in the cycle where in "opportunity cost" terms (that is, measured by the alternative uses of men and machines that could have been enjoyed) selective programmes of "tied aid" to developing countries represent least burden on the economy. The Ministry of Overseas Development should be encouraged to place contracts selectively with under employed capital goods industries, but *not* at soft prices.

7. Within the development areas, the Board of Trade should use vigorously the additional powers and flexibility given it by the Industrial Development Act. The sharp rise in the unemployment rate in major development areas adds additional reason for a new emphasis to be given to developing initiative by public agencies. The Act enables the Board of Trade to participate not only by advancing fixed interest loans, but also by taking an equity stake. There should be more readiness to develop "mixed" enterprises on this basis, including partnership with public corporations that are diversifying into manufacturing, services and construction.

8. As suggested earlier, the buying power of the public sector, properly used, can be a major instrument for influencing the behaviour of the private sector. Improved co-ordination and aggregation of purchasing, its relation to forward planning of public sector programmes, should enable contracts to be used in a positive way. Longer term contracts enabling supply firms to plan their own development more certainly and over longer periods should be linked to direct discussion with these firms as to their investment programmes, the rate of expansion of their capacity, their willingness to introduce cost saving innovations in plant, etc. If need be the additional carrot of credit availabililty on favourable terms should be used. Public purchasing is particularly important for the building and contracting industries. Plant and machinery purchases by the public sector, mainly the public corporations and the post office, have been running at nearly £1,000 million a year. This is the moment in the economic cycle when public purchasing has most influence, and could be most positively used. This would mean deliberately strengthening the purchasing departments involved.

social investment

However what has been said above about the relatively low "opportunity cost" at this point in the cycle of an extension of aid, in terms of current output, for developing countries, applies also to at least part of the social investment programme in some areas of the country. For example, the "cost" of accelerating the Scottish housing programme is in economic terms, measuring alternatives foregone, relatively low at present. But in any case the urgency of social priorities in the social investment field is such that the needs of lower income groups not least in housing and amenities, simply have to be given priority.

Among the measures that should be taken in construction and social investment are:

1. Use the Industrial Re-organisation Corporation to expedite and rationalise the use of the most effective types of system building in housing and other construction. Use the IRC and the development contract system not only to expedite and improve local authority housing (the low standards of heat insulation in our houses are an example of profligate waste), but also to guarantee the provision of new housing for owner-occupiers in the lower price range.

2. This would be helped by the establishment of a national building corporation, able to undertake the largest public contracts. This could be developed as a joint enterprise operated by a number of public corporations; the nucleus of it could best be formed by commercial take over of one or two large construction companies.

3. At the same time the Ministry of Public Building and the Ministry of Housing and Local Government should not only continue to encourage local authorities to form "consortia" for design and purchasing. They should also encourage the formation of *joint* "direct labour" departments by the authorities concerned, so that larger scale and more specialised and flexible operation can be ensured. The Ministries should build up an expert advisory service to help this process forward.

4. As well as the acceleration of the local authority housing programme, and improved efficiency and lower costs in public works projects that these measures could ensure, a more selective approach should be adopted towards private house building. Social priorities should be signalled here. For instance, the arrangements proposed for bringing direct fiscal relief to the lower paid owner occupier, which shield him from the cost of high interest rates, should be brought forward not postponed. At the same time relief on interest payments within the income tax system should be limited. The licensing system could be strengthened; if it were brought down to a £10,000 limit it would include the most expensive type of houses. As indicated earlier, a much more critical eye needs to be cast, probably at regional level, at the cumulative effects of commercial development programmes, particularly in generating chronic surplus capacity in distribution.

5. As the NEDC report on "Construction" advocated in 1964, a five year forward programme for the construction industries should be built up. Firms in the construction industry should be encouraged by the variety of means discussed earlier, to increase their capacity and improve their operational efficiency to ensure that the programme of forward demand can be met. This by itself is not enough, as the mishandling by the Conservatives of the last construction boom showed. It is vitally important that the input requirements of these programmes in terms of building materials, and types of manpower, are carefully assessed. A sectoral development programme for building materials is made easier to secure by the significant state sector that is being built up from NCB and other brickworks, and from the constructional steel subsidiaries of the nationalised steel companies. There is obviously, too, a strong case for the various publicly owned construction firms envisaged above interesting themselves in cement production.

Taken in combination these measures would be the beginning of a more coherent investment strategy. Besides these, there would need to be a much stronger sectoral review of investment criteria and decisions in transport (where the 1965 White Paper is a hopeful first step) and in fuel and power. These, and the main shape of a ten year reconstruction programme for the steel industry would have to be related to regional development needs. So, too, would the fundamental re-grouping of shipbuilding, which needs to be given urgent attention (including legislative priority). The status of regional development plans is as yet obscure. What is clear is that if the present Ministerial study groups looking at Severnside and Humberside development demonstrate the need to site new urban industrial complexes there, and re-shape the infrastructure of these areas, powerful development authorities will be needed. And in all this public sector initiative, a powerful public sector, a whole range of new public authorities and enterprises, must play a crucial role.

THE FUTURE OF INCOMES POLICY

This section explores the policy developments needed in the next phase of the economic cycle. It is assumed that by the end of the period of "severe restraint" of incomes, July, 1967, a substantial reflation of the economy will have begun. The argument centres, therefore, on the "expansion phase" ahead of us. It is treated as self evident that in the future development of incomes policy there must be an associated emphasis on policies that work upon prices and productivity.

Some account is, however, needed of the experience of incomes policy in the last two years. It is important to emphasise that the incomes policy was launched at the most difficult point in the economic cycle—in terms of rapidly rising wage costs and at the same time an absence of "real" wage improvements. Incomes policy has to be viewed in relation to the institutions and "criteria" that have been developed so far, hence the need to look back as well as forward.

the cycle

The period of deflation has pushed up the cost structure, partly because of higher rates of indirect taxation, partly from the low or negligible rate of improvement in OMH, which provides an inadequate offset to rising wage costs. Part of this pressure is absorbed in narrowed profit margins. The statutory restraints operating on incomes, and to a lesser extent on prices, are restricting the "cost push" consequences of orthodox demand deflation slightly more than in this phase of previous cycles. The period of deflation has also involved the cessation of improvements in earned income in "real" terms. Post tax disposable real income of wage earners may well not have risen since 1964; the national income data for 1965 indeed suggests a slight fall as compared with 1964. Pre-tax wage incomes were 6 per cent higher in 1965 than in 1964, salary incomes rose 8.5 per cent. Retail prices were 4.7 per cent higher than in 1964. Pre-tax, the rise in wages and salaries combined was 7.4 per cent after current transfers, but this was moderated to 5 per cent after direct tax and national insurance contributions. It looks as if total wage earners' disposable income, after tax, fell about 1 per cent in real terms from 1964 to 1965; salary incomes perhaps rose about 1 per cent. It is probably significant that consumer spending on food in 1965, at constant prices, was no higher than in 1964; this was without precedent. Over the previous decade even the deflationary periods had shown an annual rise in constant prices of at least 1 per cent per annum. There is little, as yet, to show to this year's union conferences as the fruits of participation in incomes policy. However, compelling the argument about national necessity, it has to be recognised how persistently the protraction of deflation undermines the basis of "consent".

Thus the economic climate in which incomes policy developed could hardly have been more unkind. The economic "achievements" of the policy could satisfy none of the participants. Yet we emerge from this period with some important institutional and political developments. The Prices and Incomes Board (PIB) is now established on a statutory basis. For the first time, at least in principle, the scrutiny of price determination by statutory agency has been added to our national procedures for public accountability. There is now a very widespread recognition among trade union and TUC leaders that some form of "managed" incomes policy is essential and that price and income determination cannot simply be left to "market forces". The TUC most recently of all, has been prepared to envisage the development of a systematic and independent assessment of the position of the economy, as an adjunct to its own more positive initiative in surveying wage and salary claims. It really stands on the edge of an even more momentous development, that of a co-ordinated trade union incomes policy.

The unanimous TUC statement of 23 November 1966 may be more significant than all that has gone before; it certainly represents a transformation and development of trade union wage policies that might have seemed unrealistic to expect two years ago. Given the stress and division that the economic pressures of the last two years necessarily generated, the outcome is quite hopeful.

The next phase in the economic cycle, let us call it the expansion phase, is by contrast *the most favourable* part of the cycle for the development of a co-ordinated incomes policy based on a wide measure of consent. *The danger perhaps is that its special features might lead to a misleading sense of well being and achievement.* It is "favourable" because characteristically it is a period with a high rate of productivity increase and near price stability, thus meeting Government requirements; because it is a period of almost stable prices and rising real earnings, thus not putting great strain on trade union co-operation; and because it is a period of rapid increase in OMH, higher levels of capacity utilisation, and consequently greater profitability and an improvement in business confidence.

However, we have to recall that each of the last four expansion phases of this type led on to a much more critical phase. The experience of previous cycles may be some guide, at least to the circumstances of the first year of expansion. Once demand enables a marked expansion of output to take place, OMH in manufacturing will rise 5 per cent to 6 per cent per annum. This is likely to mean that the high level of registered unemployment would fall only slowly, but labour utilisation at work would improve markedly. The return to better levels of capacity utilisation will bring sharp improvements to profits. The rise in wage rates is likely to be moderated, partly by price stability, partly by the state of the labour market, although wage bargaining is likely to respond to the *direction* in which demand for labour is moving as well as its level. The cyclical "bonus" of rapid productivity improvement means that unit labour costs are more likely to fall than to rise. Hence the disproportionate swing to profits experienced at this point in previous cycles.

Subsequently, aggregate demand has accelerated at the point where reserves of capacity have been used up, investment expansion, both in stocks and fixed capital, playing some part in demand pressure. Subsequently, too, trade union bargaining pressure has become more aggressive; the disproportionate swing to profits, as well as the emergence of excess demand for labour, may play a part in this.

escaping from the cyclical pattern

If incomes policy is directly to contribute to an escape from earlier cyclical patterns, particular attention should be directed in the next phase to industrial costs, efficiency, price levels and profit margins. For if there is a sharply increased rate of accumulation of profits, and an accompanying sharp rise in dividend distribution, it will become increasingly difficult to restrain the rate of money wage and salary increases.

Evidence of previous cycles cannot be disregarded; industrial and commercial profits increased significantly faster than the real national product; in the cyclical period of fast growth of the national product the importance of this hardly needs emphasis. There has been a clear tendency in the past cycles for dividend distribution to increase even more sharply. One can see a number of reasons for this. For instance, tax reliefs or additional investment subsidies reduce net tax payments; thus post-tax profits rise faster than total profits. This was markedly so in the last cycle and will apply again as the result of increased investment grants. Besides this, because private investment falls at least proportionately to turnover, there is less retention of profits needed to help in the finance of investment. The results have been striking.

Between 1958 and 1960 industrial and commercial companies increased their dividend distribution on ordinary and preference shares by 45 per cent, whereas the total national wages bill rose only 10 per cent. Small wonder that Mr. Selwyn Lloyd's attempts to restrain wage and salary increases from 1961 encountered such trade union resistance. In the more recent cycle, dividends increased by 42 *per cent from* 1962 *to* 1965, whereas the wage bill rose by 18 per cent.

The implication is clear, even if Corporation Tax moderates the increase in dividend distribution this time. The profits trends to be expected could exert a violent pressure on the "consent" basis of incomes policy. It is certainly not enough to meet this by the general statement that if profit increases are too precipitate some fiscal measures may follow. *This approach in any case means that prices rise more than they would have done if direct scrutiny and pressure had been directed at them.* The question of price control therefore arises sharply. But also this is the phase in the cycle (particularly, say, 1968-9) when a deliberate pressure to moderate dividend increases is more than justified. It might be worth thinking of a norm here, for instance, that dividend increases from 1967 to 1970 should not exceed either the "norm" established for wages and salaries over the same period; *or half* the proportionate rate of increase in post tax profits of the company concerned. There might be some need to make those norms relate to a base period of three years initially (1964-66) rather than a single year such as 1966, because of the different timing and severity of deflationary pressure on different companies in the last two years.

pricing norms

In the case of incomes, the general criteria to be applied to wages and salaries have been given sharper focus by the use of "norms". Initially the norm invoked was one ostensibly related to the average rate of increase of productivity to be expected from the economy. The problems involved in such an approach are examined later. But in a number of ways *prices might be a more useful subject for productivity norms than earned incomes.*

Part of the case for reviewing the criteria to be applied to prices stems from the special features of the next phase in the cycle, when the aim of policy should be to secure a *fall* in the prices of a wide range of manufactured goods. Overall price stability cannot be secured without such falls. But it rests also on the inadequacy to date of PIB analysis of prices. The PIB has not been helped by the indeterminacy of the April 1965 White Paper. For instance, in paragraph 10 of the White Paper, dealing with price reduction by enterprises, there is a reference to the situation "where output per employee is increasing faster than the rate of increase in wages and salaries". The reference is simply to the rate at which productivity "is" rising, not to any notional rate of improvement that *should* be achieved. Note too that the wording does not indicate how far short run cyclical factors should be taken into account when estimating the rate of productivity increase; an enterprise which shows an average rate of improvement of around 3 per cent per annum might nevertheless achieve twice that rate of increase in the expansion phase. Which of these is the PIB to treat as relevant, and who is collating and assessing the relevant information? Elsewhere in the White Paper it is implied that enterprises may be able to raise their prices "if output per employee cannot be increased sufficiently", but no provision is made for the systematic assessment of what *is* possible. The consequences are seen in PIB reports. For instance, paragraph 52 on the report on *Prices of bread and flour* states without any qualification that where increases in cost "due to factors lying outside the control of the industry" had occurred "the industry would be justified in seeking to recover the increases in costs from the consumer". This report did not raise clearly the question of offsetting costs through specific rates of productivity improvement. Although the PIB has shown a welcome readiness to criticise institutional arrangements that hamper productivity improvement, there has not been any tendency for its reports to lead to any clear yardsticks as to the rates of productivity improvement, and therefore offset to cost increases or *prima facie* case for price reduction, to be expected in specific industries.

There is, consequently, a case for considerably refining and sharpening the so far indefinite criteria for price review.

Such revision should particularly take into account the very rapid advances in OMH that many industries will secure during the expansion phase. This approach calls for "norms" to apply to specific industries although this is emphatically *not* a case where, as with incomes, an overall norm is relevant.

At this point in the cycle there should not be too much stress on medium or long run average rates of productivity improvement, since it is the more rapid advance in productivity in the next two years that is of particular interest. But it is worth recalling that recent empirical study indicated a widespread tendency for industry to pass wage and salary increases on into final prices with no more than a 2 per cent per annum allowance for productivity improvement (*Economic Review,* November 1964). It is not only vital to plan for and achieve higher rates of productivity improvement, *but also to see that these higher rates are the ones assumed by firms when re-appraising their prices.* One might put it this way: within the incomes policy it is as important that firms scale up their estimate of productivity improvement as that trade unions scale down the money wage increases they aim for. The form that such development of pricing criteria should take might include:

1. A norm of the rate of productivity improvement should be set, after consultation with, for example, the relevant EDC, for each major industry, and within that for major product groups. This procedure already operates in the case of agriculture. The 1966 agricultural price review states "it has now been agreed with the Farmers' Unions to adopt for annual review purposes a revised figure of £30 million for review commodities as an indication of the annual rate of gain in agricultural efficiency". The Ministry of Agriculture could doubtless say what percentage rate this involves in assumed productivity improvement, possibly between 4 per cent and 5 per cent per annum.

2. So far as possible, this process should be based on "consent", that is on the maximum participation of representative agencies such as EDCs, the Textile Council, etc. One starting point for estimating these norms should be the rates of productivity improvement for each industry that were put forward in the "National Plan". These estimates were arrived at after extensive surveys and discussions, but would obviously need to be reviewed. The more positive the Government can be about the rate of growth expected in particular years, the more scope there is for year by year forecasts as well as long period averaging.

3. These estimates of productivity advance should stimulate firms to revise their particular assumptions when examining input costs and revising prices in the home market.

4. These productivity price norms should be taken into account in PIB price reviews, just as up to now the PIB have been influenced by the incomes norm in their assessment of wage and salary settlements. The Government's statutory delaying powers on price increase, which need strengthening, should also in practice take these norms into account.

5. For such an approach to be workable would require the provision of more extensive information about the accounts and performance of firms. The revised Companies Act may assist this, but if EDCs have difficulty in obtaining adequate information, consideration should be given to providing a statutory base for such information through a strengthened version of the Development Councils Act, and/or strengthened PIB powers.

6. Such an approach would provide an improved check in the course of time; for instance it would be possible to discover whether a particular industry has been underestimating the productivity improvement in its field, and this, even with a time lag, would have its effects on price review. Individual firms would have every incentive to try to beat the norm in order to improve their profitability.

7. The subsequent development of this approach could include the assessment of

echnical standards of performance that could be attained by firms using up to date equipment. The Iron and Steel Board used such an approach in improving their technique of maximum price control in the late 1950s. Clearly, price review agencies such as the PIB should be reluctant to concede price increases where efficiency is less than it might be. But to pursue this approach vigorously would require more stress on operational efficiency assessment by EDCs and possibly the development of operational research units attached to the PIB.

income norms?

It is equally important to review the handling of "norms" for incomes. The original approach left important questions unresolved. The norm of 3½ per cent per annum was derived from an estimate of the average rate of productivity advance; it consequently appeared to be potentially related to a rate of *real* income increase. However, deflation with its check to productivity advance and higher rates of taxation meant that so far we have been going through a period when the norm could not be *both* a money norm and a real incomes norm. This left in the air the question of what, in fact, the Government's objective was in the short period in "real income" terms. Roughly speaking any wage earning group whose income in 1965 rose only 3½ per cent above the level of 1964 suffered a *fall* in real disposable income of nearly 3 per cent. *The 3½ per cent money income norm could hardly be acceptable in bargaining terms under such conditions.* Since then we have moved to a nil norm which involves about the same rate of fall in real income (or at least the purchasing power of the wage rate) as the 3½ per cent would have involved in 1965. *Thus, so far, we had had a negative norm in real wage terms. Consequently the basis of "consent" to the money norm has been eroding rapidly.*

In the next phase it is possible to envisage a positive real income norm. It is *not*, however, possible to equate the real income norm and the money income norm, even if there is near stabilisation of industrial and commercial prices. Until 1972 there is a steady rise in the proportion of dependent population to working population. *Economic trends* estimates the ratio change to be from 100 working population to 61 dependent population in 1964, to 100 working population to 74 dependent population in 1972. Therefore, if output per person employed rose 20 per cent over this period, real income per head could only rise about 11 per cent. This emerges as a problem of fiscal transfers and redistribution. Thus although it *might* be possible for the apparent purchasing power of wage rates to rise in line with their monetary value, there would have to be heavier direct taxation to finance transfers.

long term agreements

One point where the confusion over norms is seen at its most damaging is in the continued resistance in official thinking to the use of cost of living adjustment clauses in long term agreements. This was a feature of Treasury thinking during the period of Conservative governments, for example, in evidence to the National Incomes Commission (NIC) the Treasury argued that "in built inflationary features such as escalator clauses should be avoided". It has also been given prominence so far by the PIB, for example, in relation to the printing wage agreements. There is a problem of choice here, for the Government, which cannot be avoided:

Does it want to see the negotiation of long term (two to four year) agreements in a high proportion of our industry, and if so, does it want the wage rate increments negotiated within the agreement to be relatively moderate or relatively high?

If incomes policy is set in the context of a more planned advance in output and real income, long term settlements might fit better into forward planning of the economy than the old technique of undated settlements. Industries benefit in knowing well ahead what major elements in their wage and salary bills will be. Firmer prices can be quoted and fixed price contracts undertaken with fewer elements of risk, such as in cases where there are relatively long periods of construction. This is *especially* important in the coming period.

In past cycles there has been a tendency for the time intervals between claims to shorten, and the advance secured to accelerate, once high levels of demand and capacity operation are reached. One way of improving the handling of income determination as the economy moves on through a more planned expansion would be to have most sectors subject to long term agreements. This sets limits to short term manipulation of labour market demand conditions by unions, and the subsequent process of intensified pressure on claims through invidious comparisons. It would, besides, make the process of TUC and PIB review of claims and settlements more manageable, *yet the official doctrine with its resistance to cost of living clauses in agreements, is actively preventing the negotiation of new long term agreements.* For union experience, especially in the last two to three years, is that anyone signing a long term agreement without adequate cost of living revision clauses was really giving hostages to fortune. The membership will be highly intolerant of further long term agreements unless they enable major advances to be underpinned by some sort of cost of living guarantee. The Government's approach has put us in the position that few long term agreements will be contemplated, just when it would be most advantageous that they should be the predominant form of industry wide bargains. Seen against the present posture of "severe restraint", *a moderate* long term agreement in money terms might well seem acceptable *if* there were adequate guarantees written into the agreement, to ensure the *real* wage bargain that has been struck is a positive one.

One can understand the objection to the traditional sliding scale arrangements. Could the Government discuss, with the TUC in particular, some new form of protection against erosion of long term settlements by rising prices? Without being too ambitious, if the "threshold" for upward adjustment of the bargained rates were to be a 2 per cent per annum rise in retail prices, this might provide a basis for future progress. The Government would be set the not over ambitious target of keeping retail price increases below the threshold, and would have this added reason to be vigorous in its pursuit of price stability. Retail prices rose less than 2 per cent per annum in the expansion years 1959, 1960, and by 2 per cent in 1963. The trade unions would have built in guarantees that would underpin in real terms the main part of the money wage advances negotiated, and in return would be more ready to negotiate long term agreements around the "norm" of money income increase. If such settlements can be struck, then the task of the Government in holding price increases below the threshold is eased. Industrialists would have more certainty about their wage and salary bills than under either the old system of undated settlements or sliding scale agreements of the traditional kind. *This would represent a move towards guaranteeing a real income advance at a somewhat lower level than the money wage rate norm.*

the low paid

If incomes policy is to exercise a progressive function socially, its concern for a disproportionate improvement in the real income of the lowest paid has to be clearly demonstrated. This is not likely to be carried far enough if the approach is predominantly in terms of money wage rates; partly because wage structures are rigid and resistant to rapid levelling up and narrowing of differentials, partly because such an approach is cost inflationary and this would set limits to the rate of advance.

The need, instead, is for a number of measures that together make up a programme of social justice for the low paid and for low income households. The TUC should be brought into discussions to establish the lines of approach that attract most support (for any given additional commitment of resources). The emphasis, then, should be on evolving a co-ordinated programme that respects the priorities felt by the unions representing such workers. Among the measures to be considered the following should receive attention:

1. In terms of social justice, it is now urgent that the Government should pay attention to the tax burden falling on low income households, and should set out deliberately to improve their position.

It is not adequately recognised how the tax burden on low income households has risen disproportionately in recent years. The studies on the impact of taxes on different income groups of households reveal this clearly. The information is to be found in *Economic trends*, November 1962, February 1964, and August 1966. Taking, for instance, the households consisting of two adults and two children, for the higher income groups surveyed the tax burden, as a percentage of original income, has remained constant in recent years at about one quarter of original income. But for the lower income households surveyed, the tax burden rose from about 22 per cent of original income in 1957 to 24 per cent of original income in 1962 and to 27 per cent in 1964. To enable the comparison with 1957 to be accurate, the minor item of indirect taxes on intermediate products (which was only recorded in late years) has been omitted. Taxes as a proportion of original income are between three and four per cent higher than stated if this further category of taxation is included. It should be noted that there was no equivalent improvement in benefits received for these income groups. This is a direct indictment of Conservative regressive taxation policies. But *the burden of the most regressive taxes has continued to mount in the first years of Labour government*. For instance, the National Income data show that the yield of the most regressive taxes (national insurance contributions by employed persons, beer, tobacco, and local rates) was 11 *per cent higher in* 1965 *than in* 1964. We must assume that the position of the households with low earned incomes, such as the group noted above, has worsened in terms of tax burden.

It is particularly in its concern with the overlapping groups of low paid workers and low income households that the Government needs to link together consciously its taxation policies (and benefits) and its incomes policy. From the point of view of social justice, *and* as a check to cost inflationary pressures, it is necessary to raise the living standards of low income households through changes in the incidence of taxes and benefits, as well as encouraging more rapid advance in the earnings of low paid workers. But this approach must be bold enough to capture the confidence and support of low paid workers and their representatives. Already a major reform of the family allowance system involving considerable changes in the incidence of benefits and tax allowances is being widely discussed. This is the type of change that can have a substantial effect in improving the position of low income households. To some extent so is the proposal for giving mortgage interest rate relief to lower income households. These are the kind of measures that should be reviewed in discussions with the TUC. It would be useful if in conjunction with such an approach the Government were to measure periodically the advance in the *real social income* of lower income households. It should have in mind some "norm" for the rate at which this should advance; for example, this might be higher than the money wage and salary norm that happens to be in operation.

2. The Government might usefully review the role and actual operation of the *wages councils*. It is impossible to justify the permanently inferior position of so many workers in these trades. In earnings per hour, men in agriculture receive only two thirds of the manufacturing average, and a number of wage council trades within manufacturing and outside

it have earnings per hour for men only between 75 per cent and 85 per cent of the manufacturing average. Thus statutory wage fixing seems to have lost track of a yardstick, a social principle, that could help close the gap. If the gap is to be closed a serious use of systematic inter-industry comparisons of pay for equivalent work in other industries and in wage council trades should be organised. Perhaps there should be the equivalent of a "pay research unit" that could periodically survey the relative position of workers in a specific wage council industry and that of workers doing equivalent work elsewhere. Here again, there is a case for opening serious discussions with the interest groups concerned, and the economic implications of such a transition for the industries concerned would need study.

3. A re-appraisal of the statutory wage fixing process in wage council trades would raise sharply the question of the yardstick for the treatment of women workers. Some unions (notably the engineering confederation unions) have begun in recent collective bargains the slow process of closing the gap between the woman's rate and the man's rate. The time has come for the Government to commit itself in principle to equal pay for equal work for men and women. The principle is in any case involved in Common Market entry. Earlier in the post war period the transition to equal pay was made by various occupational grades in the public sector. It is increasingly invidious in terms of social policy that women *manual* workers should be denied what other occupational grades have secured. Necessarily the transition would have to be protracted, but this is no reason for not building the *principle* of equal pay into the next phase of incomes policy.

4. The TUC and CBI should be encouraged to set up joint teams to scrutinise and report on areas of low wage rates and low weekly earnings in the industries covered by normal collective bargaining machinery. The PIB has already been asked to report on a major area of such low wages in the public sector. One function of the incomes policy should be to identify the parts of the economy, or regions, or occupations, where there is a vicious circle of low pay and low productivity, and then to set in motion a process of reform. But until a careful study has been made of the specific features associated with low pay in different industries, the criteria to be applied are likely to be insufficiently precise. For instance, the long term agreement in engineering introduced, though as one reads it only *temporarily,* until the last wage rate advance under the agreement, a minimum earnings guarantee. Can such an approach be used more widely to give a differential rate of earnings advance to those at the bottom of the earnings structure?

For all these reasons the approach to the low paid is an area of policy which invites the deliberate use of discussions with the TUC to help formulate priorities, to widen the area of "consent" to Government initiatives, and to stress that at certain points Government initiative in social policy may be a superior alternative to exclusive emphasis on bargaining for particular sections. The more the Government succeeds in making the widespread existence of low incomes, and inadequate living standards for many families, a matter of felt social concern, the more possible it becomes to develop a public opinion that will support a measure of income redistribution (or a slower growth in higher money incomes) to enable poverty to be tackled.

manpower planning

The relationship between incomes policy and manpower planning has to be developed. An unplanned labour market involves acute shortages of specific types of labour, or of labour to particular industries, or in certain locations. The price mechanism then comes into play to "correct" this imbalance by "signalling" the existence of shortages through marked increases in pay, etc. The comparisons that other groups make when they become conscious of the shift in earning differentials may lead on to a wider and persistent upward pressure on the wage structure. Incomes policy somewhat cautiously had to recognise that securing, or preventing, a "change in the distribution of manpower" might constitute a case for exceptional pay increase.

Ideally, what has to be attempted is to improve forward planning of manpower requirements to the point where there are significantly fewer problems of manpower redeployment that can only be dealt with through disproportionate pay increases. Incomes policy cannot start out from the *effects* of an unplanned system, and simply take the pattern of demand for manpower as "given". It must seek to tackle the prime *causes* of such imbalance in demand and supply. Otherwise, the disruptive pressures generated will not be containable within the slow overall rate of advance of money incomes that our comparative cost position dictates. What seems called for now is an inter-departmental enquiry into manpower planning and its implications for administration and policy. For this is the weakest and least developed of our approaches to planning. The Manpower Research Unit has only a staff of 30, mostly clerical.

1. A significant improvement is needed in the flow of information. We are in the absurd position that firms are not even required to notify their current manpower requirements and surpluses let alone provide forward estimates as a guide to economic control. Ten years ago we were in much the same position so far as information on stockbuilding and investment decisions were concerned.

2. Much of this information needs to be correlated regionally. This means that the Ministry of Labour local services have to be drastically reorganised, and new functions performed. Reliable regional occupational surveys are necessary, as was glaringly obvious from the first manpower survey in 1961 (*Ministry of Labour Gazette*, February 1962). Location of industry policy has to be much more directly associated with planned regional development; it is very doubtful if the Departmental straddle of responsibility as between the Board of Trade and the DEA can be justified.

3. A similar problem of information, agencies, and their co-ordination exists industry by industry. It is not helped by the distinction between non-statutory EDCs and statutory Industrial Training Boards (ITB) though this split could be lessened. What is needed is the identification of potential shortages, or surpluses, of specific types of manpower. This links dynamically with pending organisational and structural changes, and technical changes, in each particular industry. Accelerated structural change will transform the pattern of labour requirements in such industries as coal, steel and shipbuilding. The recognition of specific problems of labour supply may hasten the search for alternative techniques of production which require a different labour input; such as skilled building labour or "industrialised" building methods.

4. Given the constraint that the labour supply may place upon growth rates in the economy in the next few years, a stress on the need for investment to be labour saving in character is justifiable. The imposition of SET, and the use of investment grants in manufacturing and construction, provide some inducement; by making labour costs per hour higher and capital costs lower they encourage the choice of investment that economises in the use of labour. But it is interesting to note that the combined effect of SET and investment grants so far only operates in building and construction. If this is an accident, it is a happy one, since that sector needs to be pushed towards new capital intensive techniques. But the objects and incidence, of these combined taxes and subsidies could usefully be reviewed. Where a continuing problem of labour supply can be identified, the tax cum subsidy could be used to signal to firms the need for labour saving techniques.

Unless some combination of such measures is attempted, the Labour market supply demand pressures will continue to put the incomes policy under strain.

Since one cannot hope for too much advance in this difficult field in the short run, it might be necessary to identify certain sectors (such as building and construction) where labour supply and earnings drift have been problems of major concern in recent years. A concerted attempt might then be made to develop positive manpower policies which overcome, or mitigate, the imbalance in demand and supply in a specific sector, by means other than arbitrary short run checks to demand, such as were applied to construction in 1965.

special cases

There remain two main "special cases" which have not been discussed. They may well overlap in practice. One is the rationalisation of wage structures, the other is that complex of procedural and job regulation agreements that goes by the name of productivity bargaining.

It is a characteristic feature of the public sector, that in it the systematisation of wage structures proceeds until they become, typically, national in coverage and relatively effective in controlling actual earnings. The coal industry, with its achievement of a national day wage agreement a decade after nationalisation, and a national agreement for contract workers twenty years after, is a case in point. The steel industry will present the same need, in the near future. It is also true of the large firms in the private sector, that for various reasons they are pushed in the same direction. But industry wide wage structures in the private sector are generally primitive, or virtually non-existent. The position is well known and the consequences in terms of "earnings drift" are familiar.

There is every reason, therefore, for incomes policy to recognise that bargaining settlements that produce a coherent wage structure for a large firm, or even more for an industry, are worth paying a relatively high price for. Since such bargains normally contain "no worsening" provisions they may initially appear expensive in their "levelling up". But the longer run benefits from removing anomalies and checking subsequent earnings drift justify the deliberate encouragement of such bargains. Doubtless the creation of an effective wages structure in engineering would be the biggest prize (and the least likely), but there are other industries, such as steel, where wage structure rationalisation would be important. It is worth noting that the April 1965 White Paper did not specify such a bargaining process as constituting an exceptional case. On the other hand, the February 1965 White Paper *Machinery of Prices and Incomes Policy,* did envisage the PIB investigating "cases . . . in which an overhaul of the pay structure seems to be indicated for economic or social reasons". The PIB has, in practice, been particularly skilful in analysing wage structures and making positive proposals in connection with them, notably in its report on Industrial Civil Servants. This is an aspect of incomes policy in which further and more ambitious public initiative, using the PIB but perhaps also approaching directly the parties involved and encouraging rationalisation talks would be appropriate.

The second special case is that of productivity bargaining, which is already the subject of a large and rapidly growing special literature. One feature of such agreements is that they represent a significant extension of the subject area of collective bargaining, and in many cases an elaboration of its proceedures, not least important being the wider use of joint regulation at plant level within the framework of the "master" agreement. Another feature is the particular stress placed on manpower utilisation, and even more than that, on manpower planning at plant and firm level. The British Oxygen agreement is an important example. There may also be an associated rationalisation of wage structures, job evaluation analysis, and so on.

Such "master agreements", covering revised procedural and substantive provisions, and with stress on a continuing process of joint scrutiny of manpower requirements and utilisation, fit in well with the obvious needs of large capit intensive integrated process industries where they are largely to be found. They also fit in well with the need for comprehensive manpower planning, and for the processes of industrial change to be handled within the framework of bargaining and joint regulation, in place of both "managerial prerogatives" and traditional forms of unilateral control by workers, especially craftsmen. Since this is such a significant, potentially far reaching departure, the Government should encourage a continuing and independent assessment of what is being achieved through these new patterns of industrial relations. The Fairfields shipyard provides an example where a project of social research, studying the new pattern of relations, is proceeding. The "genuineness" and the special characteristics of productivity agreements should be studied in practice over a period of time.

It is, then, optimistic but not necessarily far fetched to suggest that the main innovations in collective bargaining agreements in recent years may be directly helpful to the further pursuit of planned growth and more efficient deployment of resources. The technique of the long term industry wide bargain may be valuable, as has been suggested earlier, in fitting bargaining in to a policy for planned growth and price stability. The new series of "master agreements" that have been evolved by a number of firms in our most capital intensive sectors to meet a whole series of industrial relations and labour utilisation problems represent a modern development of bargaining which directly encourages a continuing stress on manpower planning and regularised union participation from plant level upwards.

consent

It is evident that the policy will operate more effectively in the long run if it is based on a sufficient degree of *consent* for the main industrial parties involved to be active in its practical elaboration. The new found intention of the TUC to institute its own regular appraisal of the economy and its own estimate of what this should imply for incomes creates an initial basis for more effective consultation. If there is to be an annual trade union review of policy, with a specially convened conference of union executives, the pressure to embark on discussions with the character if not the title of negotiations is enhanced. Enough has already been said to indicate that certainly in the approach to policy for the low paid, and in the handling of manpower planning, the Government should be thinking comprehensively and seeking to involve the representatives of labour and capital.

Incomes policy originally bore the *form* of a policy of consent. In practice, the drafting appears to have been almost entirely on Government initiative, and acquiescence might be a more accurate word for the position of the other parties. The expansion phase and the new TUC initiative make it possible to envisage an incomes policy that is evolved from a much more penetrating process of joint discussion, horse trading, and an eventual set of agreements based on compromise. We ought not to *aim* at anything less than an incomes policy founded on a continuing process of consent.

Meanwhile, the PIB has been filling the gaps left through the limited development of such national bargaining and consent. It has been interpreting and developing policy in a way that was originally conceived as being primarily the function of the tripartite NEDC. This was because of the extreme indeterminacy and ambiguity of the April 1965 criteria concerning wage comparisons. Paras 12 and 13 of the White Paper indicate that "less weight than hitherto will have to be given" to "comparisons with levels or trends of income in other employment", but para 15 (iv) made pay that is "seriously out of line . . . with the level . . . for similar work" one of the grounds for exceptional pay increase. The PIB is left with a scope for interpretation that the US Supreme Court might envy. This was a likely development during the period of deflation, since consent dwindled to "reluctant acquiescence" and discussions were more productive of disagreement than agreement. But it is intrisically better, if one can, to widen the area of tripartite agreement and tripartite interpretation of the general principles of the *Declaration of intent*. But if the PIB is to be, as the Machinery White Paper originally envisaged, a special agency to investigate and report on cases *under criteria laid down and interpreted by the* NEDC, its independence of expression should not be restricted.

If incomes policy succeeds in moving back from dictation to a wide area of consent, it will have fewer enforcement problems. The period of statutory dictation in the field of wages and salaries, and of prices, is likely to make the TUC and CBI anxious to demonstrate that a system of voluntary co-operation is workable. The TUC probably sees this vetting process as one way of getting member unions to accept the enhanced role, and continuing initiative of the TUC in incomes policy; it may be one step towards a co-ordinated union policy.

If there is any tendency for particular unions and employers to break away from the norms established for incomes and prices, the Government may find it has more *non-statutory weapons* at its disposal than might appear. It would need to make it understood that if firms raised prices to compensate for pay increases that went outside the criteria of the incomes policy a number of measures might be taken. The most important, especially where there are sizeable elements of consumer goodwill involved in the market, is investigation and publicity. If this is not adequate, there may be an effective pressure that can be applied by public competition, for instance, this *could* have been done to bring road haulage to heel, by altering the directives given to the Transport Holding Company and its subsidiaries; and this will be a more important technique as time goes on, not least through the steel subsidiaries. In a number of sectors, public sector orders are an important part of the order book of firms, and the public in its role as purchaser could be directly resistant to higher prices. The more open the economy, the greater the possibilities of seeking alternative sources of supply, but in any case this would not be a situation where the worship of "buy British" rules would apply.

presentation

The final point is a simple one. It is the need to relate all these aspects of incomes policy together, and to develop this and present it consciously and coherently as a strategic whole. One of the things most needed is the publication of periodic progress reports to the nation, which should review and embrace the whole field of relevant subjects so that, for example, improved social benefits are connected with the incomes policy) and explain the main objects being pursued, and why they are important. All we have to show so far are a series of White Papers and PIB reports, and similar specialist material. None of it represents a comprehensive review. None of it is presented also in popular form. The TUC, until its last statement, had been equally remiss, so that communication problems have been particularly acute. Even if it may be argued that over the last year, the more and better the communication the greater the resultant disagreement, this is not the way to approach future opportunities. What is needed is:

1. Annual reports on the prices and incomes policy put forward by the Government, or better still by the (tripartite) NEDC. These might appear in two versions, just as the National Plan did, a full version with detailed documentation and a popular version.

2. The PIB should be encouraged either to present its published reports in a "popular" as well as a full version (as was done with the Geddes report on shipbuilding), or to improve the layout and general presentation of its reports so that they command a wider audience.

There is, in short, an enormous and continuing job of social education to be done if the incomes policy is to introduce a measure of social accountability. That job has barely begun yet.

4. economic management and socialisation

Our economy is not simply a "mixed" one. It is one that should be embarking upon a prolonged transition to a more socialised framework. There are many on the left who discount the prospects of making significant progress towards a socialised economy under a Labour Government whose only major commitments to the nationalisation of a whole industry are steel and port transport. But to put the matter this way grossly under estimates the role that the extension of other forms of public enterprise may play, and does not distinguish the main features of a socialist orientation in general economic strategy.

Labour has to "manage" the economy. It may choose to do so in ways that barely disturb the balance as between capitalist and socialist elements. But in its economic management it has the *opportunity* of extending the elements of socialisation in *both* sectors of the economy. This it should consciously seek to do; and socialists in the Labour movement should press for this strategic sense of direction; there will be powerful enough "lobbies" pulling the other way. The distinguishing features of a socialising trend in economic policy are outlined below.

extension of social need

The extension of "social need" as the basis for demand (and therefore the pattern of output and use of resources) in place of an "ability to pay" based upon the existing maldistribution of property, wealth, income and opportunity.

A major part of this involves remedying past neglect in providing social investment and higher current spending to meet collective needs. One can instance social investment in education, health services, and the provision of an improved environment, physical and cultural. Neglect of these collective wants has been the hallmark of our capitalist society until the point has been reached where it is clear that such neglect holds back and impoverishes the whole community. Thus capital spending on the health services in the decade to 1964 accounted for less than one quarter of one per cent of our national expenditure; in the same period over three times as much money was spent on investment in retail distribution.

Another part of this involves satisfying basic individual needs, as for example, housing. For whom are the houses to be built, will it be left to "the market"? Or will social priorities be identified and resources directed towards satisfying them? Will we advance to the conception of a "national minimum" standard of housing, such as we now enforce for education, and how fast? How far will building be required to operate within a framework of organisation and control that establishes social priorities?

We have also to demand that taxation and benefits should be progressively redistributed to shift the final pattern of disposable income. The regressive bias of taxation policy and the pattern of distribution of real income during the years of Conservative government have been analysed elsewhere (see, for instance, John Hughes, *Plan for Incomes,* Fabian research series 247; Peter Townsend, *Poverty, socialism and Labour in power,* Fabian tract 371). As was argued earlier the opening years of Labour administration have continued the disproportionate increase in the most regressive taxes, although they have also begun a more progressive treatment of social benefits. There is still no inescapable and progressive system of taxation falling on individual property. The more firmly taxes, subsidies, and benefit policies are directed at reducing in equality, the more significant the change in the pattern of expenditure and investment decisions that would emerge from forward planning estimates.

There is an external aspect. A socialising emphasis of priority for social needs rather than "ability to pay" ought to extend from our own community to developing low income countries and should be concerned with the strengthening of their socialist sectors. Even though our payments position may set some limits to this, increasing emphasis on our responsibilities in a poverty stricken world is needed. Could not the Government organise and campaign for a *voluntary* increase in the income tax rate, for those who opt for it, to be entirely devoted to aid to developing countries, with matching contributions from the state?

measuring social costs and benefits

The introduction of social costs and benefits into the accounts, and therefore the commercial calculations and policy decisions of firms is required.

This is necessary if the pursuit by firms of profits (or for social enterprises, "surpluses") is not to lead to serious maldistribution of resources, social damage, and waste of social capital. Socialists are familiar with the argument that there can be a conflict between what is best for the community and what appears most profitable, which business therefore desires to do, or "cheapest" and therefore wins the contract. A good deal of this conflict stems from a faulty pricing system that does not signal in business accounts the costs or benefits involved for the community in particular decisions and choice.

"Socialising" the accounts can be done in a variety of ways. To take one example. If industrial location decisions are taken simply on a narrow accounting basis which ignores the impact of the firm's decisions on the region concerned and on other regions immense damage can be done. The long continued decline of important regions in Britain, and the growing problems of congestion, urban sprawl, in the Midlands and South East are familiar results. A combination of administrative restraints on development in some areas, and tax inducements such as high capital grants, loan facilities, and so on in others has been used already to change firms' plans for future location. As we learn to develop coherent plans for future location, as we learn to develop coherent plans for regional development, these measures will have to be taken further, made more selective, and reinforced by the direct initiative of public enterprises.

A further important example should be noted. Until recently, provision of industrial training has depended on the decisions of firms, so that only where firms saw training schemes as directly advantageous to their own commercial operations did they proceed. Other firms lived parasitically, relying on recruiting skilled workers trained by others. Chronic inadequacy in training provision has been the result in many sectors: for instance the NEDC report on the constructional industries made it clear that the large civil engineering contractors did very little towards training in skills. The Industrial Training Act has intervened and resolved the problem by financing industrial training through compulsory levies imposed on all firms, with financial aid given towards training schemes of firms which meet prescribed standards. This measure was put through by a Conservative government under pressure of sheer economic necessity; the principle it has adopted is a socialist one, and it is being left to the Labour Government to see that backward industries and firms are driven by the measure to make the provision that is socially necessary. For instance in recent years one third of the girls aged 15-17 entering the labour force went into the distributive trades; so did a sixth of the boys. Very few of these have so far received any adequate training or further education. Distribution is likely to provide the acid test as to whether the existing Industrial Training Act is strong enough to overcome employer resistance where virtually an entire industry has been accustomed to live parasitically upon the juvenile labour market. There are many other fields where the socialist technique of the compulsory levy used to finance common services, and administered by bodies with statutory powers, could be adopted. It would be a valuable development in the research field, and in statistical and marketing services.

A slightly different procedure has been used in dealing with compensation for redundancy. The Redundancy Payments Act is a further example of the socialist principle of requiring firms to recognise and provide for the social costs of their actions, although it does not go far enough. In this case, financial obligations are imposed by statute on firms, and tribunals are set up to see that firms do not escape from their obligations, but there is also a considerable element of state financial contribution. Here, again, the technique of imposing a statutory minimum commitment on firms could be extended, to include, for example, sick pay.

It would be useful to have from the Government, for the Labour Party, a comprehensive review of all the ways in which the community has intervened by introducing social costs and benefits into firms' accounts, and by direct administrative controls, such as industrial development certificates, to ensure that economic decisions take account of the community's wider economic interests. It would be useful, too, to examine the variety of techniques applied, from tax inducement to tax levy, from statutory direct controls to "social surplus accounting" aimed at weighing the respective merits of alternative projects. Such a review would help to demonstrate how far this socialising process has been taken, to argue the general principles and techniques involved, and to prepare the way for a further extension of the principle. That further extension certainly ought to involve a strengthening of the positive planning of a decent environment, and ought to extend the compulsory levy system in industry to finance the expansion of industrial and market research, technical information and advice services and an improvement in statistical information.

democracy and accountabillity

Without an extension of accountability, democratic participation in, and control over, economic institutions and decision taking, the first two elements of socialisation discussed may merely imply a more tolerable capitalism, calling in elements of socialist rationality to limit the damage caused by its own "free" operation. Rationalised long term planning without the creation and extension of various forms of social scrutiny, accountability, and outright control, must carry the danger of the domination of our community by the giant corporations and their sort of corporate institutions and administrative approach.

So far, Labour has made some advance on this front by introducing two processes of socially controlled investigation and some elements of direct control over the price fixing of capitalist industry. The Prices and Incomes Act puts on a statutory basis the process of PIB investigation of pricing, and provides a temporary standstill, although the main emphasis is still on the pressure of public opinion, and in the future, one hopes, public competition, and pressure exerted by public purchasing, to ensure compliance. The 1965 Monopolies Act goes farther in providing for statutory price control after investigation of a monopoly. This is an important beginning which could be greatly strengthened by emphasis by public purchasing departments on full access to information on costs and efficiency in supply firms. The potential part that could be played by public purchasing, which was indicated earlier in this pamphlet, can hardly be overstated.

It is also important to improve the existing legislation dealing with monopoly. The 1965 measure should only be viewed as an interim step; it would certainly be important to widen the definition of a monopoly to cover, for example, a number of situations involving the de facto absence of competition, and *to require all such firms to register and to supply a wider and more penetrating range of information about their activities,* including information on costs, investment rates, research, and so on, than required by the Companies Act. It is high time that use was made of the 1965 Act's clauses enabling a wider process of "general" references to be pursued. There should also be provision for appointing public directors to the boards of companies in a monopolistic position as trustees of the public interest. After all, a considerable number of people with experience and position in private industry sit as part time members of public boards, with some (ill-defined) "trustee" role.

More generally, the information statutorily required from firms should be extended. Apart from the modest development in this direction contained in the current Companies Bill, there is need, as has been argued, for much more positive information about manpower requirements. There is room for a considerable extension of "workshop" rights, to ensure that firms are required to inform and negotiate with trade unions representing their workers on such matters as changes in manpower requirements; nor can the unrestricted right of firms to discipline workers, limited only by union strength, be expected to survive for long. If at this point we demand more positive participation by workers' representatives in "managerial" functions, we have to take seriously the training and educational needs implied; there is no reason why industrial training funds should not be used to increase dramatically the programmes of day release and other courses aimed at training shop stewards, lay trade union officers, and others.

At industry level, there seems no reason to perpetuate the present clumsy arrangement of separate voluntary EDCs and the *ad hoc* statutory industrial training boards, and other *ad hoc* bodies, such as industrial research organisations. The required pattern to strengthen and integrate both planning and social accountability at industry level was established long ago with the 1948 Development Councils Act. This provided for tripartite statutory bodies with levy raising powers for the specific functions necessary if industries are to have adequate industry-wide servicing. Resistance by the trade associations led to a retreat from this approach. What is now needed is an amended version of that Act, to take further the range of powers and initiatives that such bodies could adopt, and adapt their functions to modern planning requirements. The provisions for establishing such bodies in any industry where a considerable body of opinion supports its formation should be strengthened and direct financial inducements, of state support to the industrial budgets of such development councils, provided as well. Provision should be made to incorporate industrial training boards within the single statutory body, and for the transfer of industrial research work to them.

Nor, of course, should Labour innovate and experiment with increased social accountability only in relation to the private sector. The time is long overdue for a considerable extension of the functions of the Select Committee on Nationalised Industries, in particular to enable it to review specific aspects of nationalised industry operation across the whole field, as well as examining the industries one by one; it needs an expert staff. This becomes a more pressing need as the sector of public enterprise becomes larger and more diversified. The need for more direct representative democracy and accountability in the management of regional economic bodies must largely await the sweeping reform of local government; but that development must be envisaged and prepared for.

Finally, the whole process of planned development, with its conscious choice of priorities, must be seen as being in an important sense a massive exercise in social accountability and democratic discussion. This process must rest upon the firm foundation of a powerful sector of public enterprise, flexible in its organisation, and directly involved in the main areas of industrial innovation. This sector may well be reinforced not only by the familiar process of nationalisation, as with steel, but also in new forms, such as powerful regional development agencies able to supervise and positively intervene in the areas where the most rapid and widespread structural changes have to be pushed through. It is the right moment for the Labour movement to be thinking of an economic and social strategy that can tilt the balance of our economy towards a more socialised and a more democratic and accountable system.

fabian society

The Fabian Society exists to further socialist education and research. It is affiliated to the Labour Party, both nationally and locally, and embraces all shades of Socialist opinion within its ranks—left, right and centre.

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