Labour and Sterling

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In any survey and analysis of the world system in which a Labour Government in Britain has had to work since 1964 we must start from the fact that Britain has become a rather weak member in the second rank of capitalist powers increasingly dominated by United States capital but still dominating the economies of a group of small and far less developed countries. Once the workshop and then the banker for the greatest empire in the world, British capitalism had for long tried to reconcile the roles of banker and trader. For the banker, the rate of return is the crucial question; for the trader, the growth of his trade. Since the war the City has flourished and industry has declined. Sterling devaluation spells the collapse of a long struggle to revive London's banking role but it spells more than that.

The Crisis of the Sterling Bankers

Through the whole period from 1955 high interest rates (never below 4½%) were attracting funds to the City of London which could then be invested abroad for an even higher long term return. By 1960 the outward flow of long term capital exceeded £ 400 million with only

£ 150 million flowing in from outside. The gap was plugged as usual by short-term borrowing.

Mr. Heath claims that there was an aggregate surplus on the Balance of Payments during the years of Tory rule. There was on current account a small average annual surplus but on capital account there was a large annual deficit. We may summarise the balance of payments on average and in the three years of heaviest deficit between 1952 and 1965.

	Annual Average 1952-64	1955	1960	1964	1965-66
Balance on Goods	— 177	— 313	— 408	— 543	— 216
Balance on Services	+ 190	+ 129	+ 174	+ 167	+ 176
Net Property Income	+ 282	+ 174	+ 242	+ 416	+ 409
Government Spending	— 239	— 138	— 283	— 433	— 453
Net Capital Account	— 165	— 122	— 192	— 368	— 174
Deficit met by Short-Term Money	110	277	467	761	258

It can be seen that while on average over the period of Tory rule there was just a balance of goods and services taken together and property income from overseas just exceeded Government spending, the net outflow of long term capital had still to be largely covered by short-term money.

In the years of maximum deficit, however, all three of the major deficit items grew—the deficit on exports of goods, the increase in government overseas spending, nearly two-thirds of which is military, and the net outflow of capital. Although the average annual increase of borrowing at £ 110 million may not seeem large, the figures of nearly £ 300 million, nearly £ 500 million and finally nearly £ 800 million in the deficit years show the gathering seriousness of the crisis. There are thus two parts to the problem—first the worsening imbalance in export and import of goods, which in the three worst years accounts for more than half of the total deficit. Second, there is the steady increase of short-term debt by over £ 100 million every year. These are the two parts of the balance of payments crisis that faced the Labour Government. The short term loans could easily be withdrawn and were in fact withdrawn at the first whisper of doubt about the possibility of maintaining the value of sterling in relation to other currencies. What could the Government do?

Let us set down the Country's Financial Assets and Liabilities side by side as they stood in December 1964.

Item	Assets	Liabilities	
Long Term			
Inter-Govt. Loans	817	1649	
Private Investment	9420	4075	
of which: Portfolio	3600	1500	
Companies Direct (excl. oil)	4520	1825	
Oil Companies	1300	750	
Long Term Total	10250	5950	= Net 4300
Short Term			
Trade Credit	691	142	
Banking — Sterling currency	1178	4634	
— Non-Sterling	1626	1856	
I.M.F. Account	696	881	
Government Portfolio	470	—	
Gold and Reserves	827	—	
Short Term Total	5475	7500	= Net — 1125
Long Term and Short Term	15725	13450	= Net 2275

There was an overall positive balance of over £ 200 million, but the short term balance was in deficit, even though, it must be remembered, this was after borrowing nearly £ 900 million from the International Monetary Fund. The Government had another £ 470 million in its portfolio of securities, a large part of which could be—and were in the event—disposed of; but the short term deficit remained and it only needed a swing from credit to debit of the traders, who buy and sell sterling from day to day for paying their bills, to start a further run on the pound. Much of the sterling currency debt of the London banks is held officially by foreign governments as reserves for their currencies and they were unlikely to try suddenly to change these from sterling into other currencies; but non-government holders would certainly try to get out of sterling in a major crisis.

The obvious course for the Government would appear to have been to realise some of the long term assets that had been built up overseas and in this way to meet the short term debt. But here there was a snag. These assets were largely in private hands. Moreover, two-thirds were directly invested by companies, including the oil companies, in subsidiaries and branches overseas. Nevertheless, £ 3600 million were in private portfolios, that is investments by persons and institutions in companies abroad; and these could have been nationalised and sold to meet the debt. In fact discussions are now being held by the Government with Investment Trusts with a view to persuading them to realise some of

their overseas holdings and pass the dollars to the Government. Such voluntary methods of realising private assets abroad are very unlikely to be adequate. Yet it is clear that for the Labour Government to have made compulsory purchases would have raised the whole question of the confidence of the City and of the foreign bankers. Even if foreign exchange controls could have been imposed quickly enough and foreign assets could have been frozen, the process of Government intervention could not have stopped there. The demand of the Left for nationalising the private foreign portfolio would have required in effect nationalising the whole banking system to prevent wholesale withdrawals of capital from Britain. Nor could intervention have been stopped at this point. Of course the withdrawal of capital takes no single piece of machinery or equipment with it, but the short term effect on trade credit would have required Government control over foreign trade as well.

There is an evident conflict here between the City's banking role and the needs of British industry; but the conflict lies in the whole structure of British capitalism. If the functions of the City of London were replaced by Government control of foreign trade and finance, there would not only be a loss of some £250 million a year—the City's contribution from banking, insurance and other services to the Balance of Payments—but huge problems of restructuring would still face British industry. For it is the City bankers who finance British industry both at home and in their operations overseas and it is increasingly British industry itself that requires the outflow of capital each year, which we have seen be so large a part of the cause of the balance of payments deficits. To compete with their opposite numbers in the United States and West Germany, British firms have had both to increase their hold on sources of oil and other industrial raw materials and to establish subsidiaries in their competitor's own markets overseas.

The international company is the driving force of modern capitalism. To succour its vast operations there must be a surplus on the balance of payments in the country from which it originates. Such a surplus can only be found either from a direct surplus of the home country's exports over imports, or from the repatriation of earning from overseas operations or, as we have just seen, from short term borrowing. The very increase in the operations of overseas subsidiaries may tend to reduce direct exports by U.K. companies and their earnings overseas may be required for reinvestment overseas. If this happens, short term borrowing must increasingly be relied upon.

This is what happened in Britain in the last fifteen years but it would be missing an important aspect of the truth if we failed to recognise that the trick—the bankers' confidence trick of borrowing short and lending long—very nearly came off. If we combine the capital

account and the property income and government accounts in the balance of payments, that is by separating these from the private goods and services accounts, there really was a capital and income balance; but it was not large enough to pay for the military and other government overseas expenditure that such a balance involved. Let us take three periods since 1958 and set down side by side the flows each way of income from property and investment both from ploughing back of that income and from fresh capital (plus = flow in to Britain; minus = flow out).

Flows in £ms	Year 1958 (Income	Investment)	Average 1959-64 (Income	Investment)	Average 1965-66 (Income	Investment)
British Income from Abroad and Investment Going Abroad	+ 684	— 294	+ 739	— 342	+ 970	— 412
Foreign Income from Britain and Investment in Britain	— 389	+ 104	— 435	+ 195	— 562	+ 212
Income and Investment Balance	+ 295	— 190	+ 304	— 140	+ 408	— 200
Government Transfers	+ 3	— 77	0	— 107	0	— 155
Military Expenditure	+ 52	— 173	+ 38	— 224	+ 25	— 295
Combined Balance	— 90		— 136		— 217	

The overall figures for investment include not only Government loans to foreign countries but also the repayment by the Government of foreign loans made to Britain. Without the suspension of repayments on the American loan in 1965 there would have been an even worse balance in the last two years. The other element in the apparent improvement was the sale by the Government of some £ 200 million of its own portfolio of foreign investment in those years.

The fact must here be faced that even if the overseas military expenditure had been sharply cut back by the Government, it would have been necessary to increase the item of Government transfers. For these are the grants made to ex-colonial lands, not only to replace their dependence on British military expenditure as in Malta or Aden but to help finance their economic development in such a way as to encourage them to go on buying British goods.

This analysis of the role of capital movements in the sterling crisis indicates at once the difficulties facing a government that was committed to remaining within the boundaries of the mixed economy. It also precisely illustrates the position of British capital. Since the war British capital investment has been built up overseas not only in the old fields of oil and raw material extraction, but even more today in the new fields

of manufacturing plants mainly in the other advanced industrial lands and even in the U.S.A. By these means British capitalism tries to retain its dominating role. For many years, even after the war, the resources for its export of capital were found from the earnings of the colonial lands themselves which had by virtue of membership of the sterling area to bank in London. The self governing lands spent their own earnings but the earnings of the colonies could be used to balance Britain's deficits. Now only Malaysia and the oil states remain to supply the resources for the City's long term investments. Hence the need to preserve the imperial role East of Suez at so great a cost. The cost of course is paid by the tax payer; the benefits reaped by the investors. To preserve British capitalism and the imperial role the Government was in fact forced to borrow again and again from the United States and the other capitalist bankers. Devaluation of the pound in November 1967 marked the final downgrading of British capitalism from the first rank to at best the leader of the client states. The confidence trick could be maintained no longer. It is because some businessmen thought that a Tory Government might have kept it up longer that anger has mounted against the Labour Government. But the fundamental facts underlying the crisis of sterling are to be found in the interrelationship between the banking role of the City and the decline of British industry.

The Decline of British Industry

In 1950 British industry was not backward except in relation to the United States. British exporters still provided over a quarter of the manufactured exports of industrial lands, nearly as much as did the United States. By 1964 the British share had been halved, while U.S. and West Germany exporters were providing over 20% each. In the decade after 1955 exports of British manufactures rose by about 3% a year while imports of foreign manufactures rose annually by 9%. The result is that by 1967 manufactured imports into Britain were equal to three-quarters of manufactured exports; imports of machinery and transport equipment to half of the exports of these items—and these are Britain's stock in trade par excellence.

What had happened? It is not difficult to see from the available figures that investment in new equipment had proceeded faster on the Continent than in Britain. With productivity rising in U.K. manufacturing industry very much more slowly (by 37% between 1955 and 1966) than elsewhere (50% in the U.S. and 67% in West Germany), increased wage costs per unit of output were pushing at British prices. Indeed, British firms which export on average nearly a fifth of their output had been forced to squeeze their profit margins in the export

market. This can be seen from the fact that whereas U.K. manufactured export prices rose by 27% between 1955 and 1966 (well ahead of the figures for all other advanced industrial countries of around 15%), this rise was much less than the rise over the same period in all home costs (36%).

Not only were British manufactures becoming uncompetitive but it was evident that British capital exports were failing to obtain similar rates of return to those of their competitors, at least to those of the U.S.

We may follow E. V. Morgan's figures of Net Income/Assets Ratios for U.K. and U.S. Companies in the five years 1958-62.

Where Invested	Rate of Return	
	U.K. Companies	U.S. Companies
Domestic Rates in U.K.	7.8	—
in U.S.A.	—	9.1.
Foreign Investment - All Countries	7.9	10.2
in U.S.A.	6.6	—
in U.K.	—	12.5
in E.E.C.	8.9	14.2
in Australia	7.2	11.5
in India	8.8	11.9
Foreign Investment — All Industries	7.9	10.2
in Mining	12.1	10.9
in Manufacture	7.4	10.1
in Other	7.7	14.1

It will be seen that the rates of return on U.S. capital were higher both in domestic investment and in foreign investment than those on U.K. capital; in addition the rate of return on U.S. capital invested abroad was higher than on U.S. capital invested at home, while there was little difference in the two rates on U.K. capital. Rates of return on British capital at home were declining steadily throughout the 1950s. Between 1954 and 1958 net income as a percentage of net assets for quoted companies in manufacturing fell from 19% to 15%; there was a slight recovery in 1960 but by 1962 the figure was 12%. In the engineering industry the fall between 1954 and 1962 was from 21% to 11% and in vehicles from 25% to 10%.

British industry was evidently caught in a pincers movement. U.S. and German firms were not only challenging the profits of British firms operating overseas; they were also challenging them in their own home market. United States firms were investing in their British subsidiaries throughout the 1950s at a rate of at least £ 100 million a year and the resulting production was yielding a rate of return on capital twice as high as that enjoyed by British firms.

The power of United States capital depends on its enormous technological superiority. To compete in the world market any other producer requires lower levels of wages until his technology catches up. If his technology improves haltingly and productivity is stagnant or rises slowly, not only are wages threatened but so is his whole competitive position. And if only some producers in any country improve their technology so that their higher productivity allows higher wages but some industrial sectors or parts of the country lag behind, the tension between different wage levels becomes serious. If this happens in a situation where there is tendency for imports to rise faster than exports, then wage increases in some sectors, plus credit released for electoral purposes, can easily push overall demand ahead of productivity and pull in huge waves of additional imports.

This brings us to a further problem facing British capitalism at the end of the 1950s. The power of British trade unions in conditions of full employment to raise wages ahead of productivity must here be noted. In the late 1940s and early 1950s real wages undoubtedly lagged behind the rise in output per man. Profits boomed. From 1954 to 1960 hourly earnings in manufacturing industry in Britain discounted for price increases, i.e. real earnings rose ahead of output per man hour. Profits were reduced. In West Germany and the U.S.A. by contrast productivity rose faster than real earnings over these years. Profits in these two countries boomed and investment in new plant and equipment leapt ahead.

The figures are most revealing:

Earning and Output Per Man Hour in Manufacturing Industry

	1953	1960	1963	1966	1966 as % of 1962
U.K.					
Hourly Wage Rates	100	140	162	194	124
Hourly Earnings	100	155	176	220	128
Retail Prices	100	121	133	149	114
Real Earnings	100	128	132	147	112
O.M.H.	100	120	131	147	119
U.S.A.					
Hourly Earnings	100	129	141	155	114
Retail Prices	100	110	115	122	108
Real Earnings	100	117	123	127	105
O.M.H.	100	125	140	154	114
West Germany					
Hourly Earnings	100	158	210	267	137
Retail Prices	100	111	120	132	114
Real Earnings	100	141	275	202	121
O.M.H.	100	142	161	186	123

The problem of rising earnings in relation to productivity was exacerbated for British industry by the nature of the Tory election booms in the "never-had-it-so-good" 1950s. The share of the national income going into private consumption was raised in the boom at the expense of the public services. When the release of credit for private consumption had pulled in excessive imports and upset the balance of payments, a severe check was administered to all economic activity. The result was not only a Stop-Go cycle of current demand but a series of checks to company investment plans. The share of the national product going to new investment was thus held back.

We may compare Britain's performance in the 1950s with that of other countries.

Country	Gross Domestic Investment as % of G.N.P.		Rates of Growth O.M.H.	
	Total	Machinery and Equipment Only	Total	Industry
Norway	26.4	15.5	3.2	2.0
Canada	24.8	8.3	2.0	1.7
Netherlands	24.2	11.0	3.7	4.4
West Germany	24.0	11.1	5.3	5.7
Sweden	21.3	7.5	—	—
Italy	20.8	9.0	4.1	5.0
France	19.1	8.1	3.9	4.0
U.S.A.	19.1	7.2	2.1	2.2
Denmark	18.1	9.0	2.3	—
Belgium	16.5	7.3	2.5	3.5
U.K.	15.4	7.4	1.9	2.1

Just as growth is a cumulative process, so is decline. Once the British industrial base at home was weakened by the failure to invest a large enough proportion of the national product in new plant and equipment, exports became less competitive, imports flowed in; when at the same time British capitalism was proceeding to build up its overseas operations and to support these with military bases, the strain on the balance of payments became serious enough. But every new check to growth while the balance was righted—after 1955, after 1960 and again after 1964—each new wave of short term borrowing from abroad at higher and higher interest rates only worsened the competitive position of industry at home. When demand is held back at home, investment in new plant stops. By contrast the surplus of exports from West Germany made possible continuous growth which created the opportunity for further investment in new plant and so for still more competitive exports until West Germany's payments surplus could easily finance the outflow of West German capital for the foreign operations of West German firms.

Response of British Industry to the Crisis

There can be no doubt that 1960 marked a turning point for British capitalism. Up till then British industry had been shielded by a combination of factors—the slow recovery of the defeated nations, the inflow of public and private capital including not only investments of U.S. firms but the dollar earnings of the Colonies, the fall in import prices, the spending of wartime accumulations of reserves by the developing lands. At the same time the City of London had succeeded in moving very near to full sterling convertibility and in re-establishing itself as the second, if not the first, financial centre of the world. The British balance of payments crisis of 1960 revealed the exposed position of the British economy. West German exports of manufactures had surpassed those of Britain in 1958 while Japan and Italy were steadily increasing their shares. Partly as a result of the recovery of the defeated nations, world prices of food and raw materials were once more rising. The overseas countries of the Sterling Area were beginning to run deficits of their own to add to Britain's deficit. The "never-had-it-so-good" pre-election boom provided by the Macmillan Government in 1959, with consumption increased ahead of output, only added the last straw.

The responses of British capitalism to this critical situation can be equally clearly dated from 1960. Some of these may be regarded as deliberately planned, most as the natural reactions of capitalists in a competitive situation. The two obvious competitive reactions were first the sudden increase in mergers and take-overs that can be dated back to 1959 and second, renewed expansion of overseas investment by British companies.

What resulted from this process of merger and take-over and foreign investment was that the largest companies in Britain achieved an even more dominating position in the economy than before.

If we examine the companies which had achieved a figure of £ 25 million of net assets by 1963 in the sectors of manufacturing, distribution and construction (excluding oil, shipping, and insurance for which similar figures are not available) we obtain the following picture:

Type of Company (by Asset size in 1963)	*Net Assets*		*Average Income*	*New Capital raised annually*
	1957	1963	1958-63	1958-63
All Quoted Companies (in £m)	10.219	15.640	2386	313
of which (as % of all)				
Top 12 Companies	22	19	19	24
Next 104 Companies	34	40	36	56
Remaining 1800	44	41	45	[illegible]
Fastest Growing 42 of the Top 116	11	10	17	45
Top 7 U.S. Companies	3	3.5	4.25	1.75

Although the twelve giants have lost some of their dominance, the top 116 had even by 1963 raised their share of all company assets to nearly 60% of the total and had in the process taken 90% of the new capital raised in the previous seven years. The fastest growing third of the top 116 took nearly half the new capital and almost doubled their share of the assets. If we were to include the giant oil and shipping companies, as the lists published by *The Times Review of Industry* do, there is no doubt that we could say that the top 120 companies in Britain own a half of all the assets and probably account for nearly two-thirds of all home sales; fifty companies including the oil and shipping companies account for perhaps half of the sales.

But even these giant firms remain uncompetitive in the world market. It is first of all evident that the seven top United States Companies operating in Britain have a much larger share of the income than of the net assets. Indeed their income assets ratio is about double that of the other large companies. A study of the *Fortune* magazine lists of top companies shows, moreover, that British companies net assets are not smaller on average in most industries (automobiles are the exception) than those of their United States counterparts. But their sales are very much smaller, since their sales assets ratios in every field of industry are only about half those of the United States companies. The sales per employee are relatively lower still. In other words the technology of the U.K. companies is still much behind that of the giant United States companies.

We need now to note the implication of this great concentration of capital in the largest companies which are those that have become most internationalised. First, over a fifth of the annual net British company capital investment (i.e. excluding the investment of foreign company capital in Britain and excluding depreciation provisions) has in recent years been invested outside the country. This is a sum equal to the net annual investment of all the nationalised industries.

Studies made at the Department of Applied Economics in Cambridge have suggested that in 1961 the net worth of overseas subsidiaries and branches was already equal to just under a fifth of the total net worth of all British companies.

Secondly, the result of this great wave of overseas investments is that many of the largest British companies are selling nearly as much in foreign markets as at home not mainly through direct exports but through their subsidiary companies.

A few examples will serve to illustrate the point. They are taken from those amongst the top 100 companies which happen to publish their export and turnover figures by home and overseas markets.

Distribution of Certain Large British Company Sales at Home and Overseas
(in million pounds)

Company	Year	Total Sales	Home Market	Direct Export	Sales from Overseas Subsidiaries
I.C.I.	1963	625	325	115	184
G.K.N.	1966	330	214	22	94
B.I.C.C.	1966	299	155	46	98
English Electric	1966	270	174	47	49
A.E.I.	1966	265	137	48	80
Metal Box	1966	141	96	8	37
G.E.C.	1963	122	85	19	28
Albright & Wilson	1965	96	54	18	24
Reckitt & Colman	1964	96	36	6	54
British Oxygen	1966	95	43	8	44
Glaxo	1966/7	70	24	13	33

It cannot certainly be argued that the exports of such firms are lower than they would otherwise have been had they not established overseas subsidiaries. The Reddaway Report on the Effects of U.K. Direct Investment Overseas took a fairly favourable view of the export effect, since it seemed likely that in most cases overseas markets would have been lost if subsidiaries had not been established. The picture varies from industry to industry. We have Dunning's estimates (*Moorgate and Wall Street*, Autumn 1966) of the share of exports as a proportion of output in the U.K. for leading overseas investors and for all companies to judge by.

Industry	Total Exports from U.K. 1964	Exports as % of all Firms	Firms U.K. Output for Leading Investors
	£m	%	%
Non-Elect Engineering	862	29.2	19.2
Vehicles	658	33.4	28.1
Textiles	420	17.7	16.0
Chemicals	412	13.8	13.7
Electrical Engineering	315	19.8	21.7
Food, Drink, Tobacco	251	4.3	15.9
Paper etc.	50	6.1	4.1

Dunning surprisingly draws the conclusion from this Table that the leading investors contribute neither more nor less to export from their output than others. It is hard to see how he reaches this conclusion.

If we take from the *Times* List of The Top 300 U.K. Companies those which publish their turnover and exports sales and compare them with national totals we certainly find that the largest companies make a surprisingly small contribution to exports. While the top 45 companies

probably provide nearly a half of all sales at home they provide less than a quarter of all exports.

Thus a listing of the total Assets, Sales and Exports of groups of U.K. Companies according to their size (figures in £m) reveals the following picture.

Companies by Size	Net Assets	Turnover (*incl. overseas*)	Exports of goods and services
Top 45 giving turnover figures	11,811	15,840	1,470
Next 155 giving turnover figures	4,641	8,760	673
Remaining Companies	11,448	(11,400)[1]	4,787
Total	27,900	(36,000)[1]	6,930

The fact is that the largest British firms have come to rely on the medium and smaller companies to supply the exports for the balance of payments. What has still to be made clear are the reasons for the giant companies continuing with their overseas investment although as we saw earlier the return to capital is no higher than at home. The explanation is bound up in the whole analysis of the role of the international company in modern capitalism. Given the nature of the capitalist world market and the lines of production into which industrial investment is attracted inside that market, there was nothing else they could do. The reasons for the growth of the international company include control of raw materials, the planning of flows through all the stages of production, flexibility and the spreading of risks among different plants, the detection of technical innovations at an early stage of research and development, above all the establishment of a large captive market for long runs of production, which only advertising on an international scale can guarantee. Included in this last point must be the claim to participate in world cartels and agreements for fixing prices and sharing markets.

Labour and the Crisis of the World Economy

As is becoming very evident, a major crisis is developing for the first time since the war in the whole world economy. Up to 1966 world production and world trade, at least in manufacturing, had grown at unprecedented rates — in the last eight years respectively averaging in volume 7% and 8% a year. In such circumstances it was not difficult

[1] The figures in brackets are a guess; total final output at home was about £ 37,00 million but this includes imports and taxes on expenditure and excludes sales abroad by British companies subsidiaries.

even for a backward British industry to increase exports at an average 4% a year. By 1967 the main forces that had sustained this growth were becoming worked out. They may be rapidly listed.

There was first the recovery of the defeated nations and the increase in trade inside Western Europe engendered by the transfer of manpower from agriculture to industry and the internal exchange of goods within the European Economic Community. By 1967 the transfer of manpower and the tariff cuts which had produced this result were complete. Secondly there had been the huge outflow of capital both public and private from the United States associated with a great increase in overseas military spending. Since the surplus of United States exports over imports did not suffice to finance these flows, the United States began from 1958 onwards to run a steady balance of payments deficit of around $ 3 billions a year. This was financed by sales of gold which reduced the stock of gold in Fort Knox by 1962 to the level it had been in 1920. Attempts were therefore made in 1962 by the U.S. Government to reduce its overseas spending and to repatriate more of U.S. private company overseas earnings. But the war in Viet Nam once more raised the level of U.S. military spending overseas and several countries led by France began to convert their dollar reserves into gold.

A crisis of liquidity, as the reserves of the great trading nations are called, arose. Gold was still being produced at the rate of over $ 1 billion a year but the possibility of gold being revalued in terms of the dollar led to nearly all of the new production in the capitalist world being offset by private hoarding. For a time Soviet and Chinese sales of gold to pay for imports of grain kept the gold reserves rising. In 1966 they actually began to fall for the first time since the war. The deficits on Britain's balance of payments in 1963, 1964, 1965 and 1966 provided some increase in available sterling. More important, an increase in 1965 of $ 2 billion in the reserve quotas of the International Monetary Fund improved the situation for a time. The hard fact remained in 1967 that world liquidity, which had been the equivalent of the value of over seven months of world trade movements in 1958, was down by 1967 to the equivalent of only three months' trading. Without new forms of credit, trade was being strangled. What was equally serious, the underdeveloped primary producing countries had hardly increased their reserves — the Sterling Area countries not at all — over their holdings in 1956. Reserves of the less developed countries were equivalent in 1967 to less than three months of their trading and most of these reserves were held by just five comparatively small countries — Venezuela, Israel, Saudi Arabia, Malaysia and Thailand. But a third of Britain's trade is still with the Sterling Area countries and a half of that with the less developed ones, of which only Malaysia and Kuwait count any reserves.

A very real danger arose in 1966 when the three greatest trading nations, the United States, Britain and West Germany, simultaneously began to pursue policies designed to reduce their own balance of payments deficits without putting anything in the place of the finance these deficits had provided for other countries' trade. The danger was of a succession of beggar-my-neighbour policies of the kind experienced in 1931. The danger this time was not of competitive tariff-raising; this is now precluded by the General Agreement on Tariff and Trade. There was still, and is still, a danger of beggar-my-neighbour deflationary policies, combined here and there with devaluation. If several large countries try to balance their payments by increasing their exports and reducing their imports through deflationary measures the net result is almost bound to be a general reduction in the trade of all of them and thus in the trade of all other countries. This is what happened in 1931 and it can happen again.

How far was realisation of this danger which Mr. Wilson expressed at the T.U.C. Conference in 1965 the reason for the Labour Government's vacillating attempts between 1964 and 1967 to avoid either sharp deflation or devaluation? Were there no alternatives open to the Government when it came to power and was faced by a balance of payments deficit of some £ 800 millions?

The Rake's Progress

Harold Wilson in opposition had always argued that Tory Stop-Go and all that it implied could be avoided by the use of physical controls — the steering wheel in place of the alternation of brake and accelerator. "Ruthless discrimination will be practised" he promised in the spring of 1964 so that "growth should not be stopped when imports threatened to rise too fast...Essential industries will be encouraged, those of lower priority will be held back". The 1964 Labour Party Manifesto had proposed long term trade agreements with Commonwealth countries to build stability into our foreign trade. The 1966 Manifesto had argued for a "concerted world effort...to enable overseas countries to earn the foreign exchange essential for their development programmes...international commodity agreements and arrangements for finance for increasing and stabilising the export earnings of primary producing countries".

Mr. Wilson himself had spoken at the 1963 Labour Party Conference on "Labour and the Scientific Revolution" in the following terms;

> "The Stop-Go economy of the last 12 years failed because the expansionary phases had not created growth in those industries which could provide a permanent breakthrough in Britain's export trade or a lasting saving in imports... Monetary

> planning is not enough. What are needed are structural changes in British industry and we are not going to achieve those on the basis of pre-election spurts every four years in our industry, or of hope of selling the overspill of the affluent society in the highly developed markets of Western Europe. What we need are new industries and it will be the job of the next Government to see that we get them... When we set up new industries based on science there need be no argument about location, no costly bribes to private enterprise to go here rather than there. We shall provide the enterprise and we shall decide where it goes". (*The Times*, 2-10-63).

What happened? We had first Mr Wilson's commitment at a Mansion House banquet in the City of London that "Sterling would be kept riding high". Devaluation was ruled out but there was still the promised alternative to deflation and "Stop-Go" stagnation. By 1964 the size of the payments deficit would have required physical controls on imports, on foreign exchange movements and on building and investment at home.

In large part the crisis in the balance of payments was due to heavy overseas military expenditure and a huge outflow of capital in the months before Labour took office. But these were in turn related to the requirements of an international economic, political and military system which imposed constraints on Britain's freedom to act. To deal with the problems of debt and deficit in any radical way would as we shall see have involved an immediate confrontation, not only with this international system but also with those elements of it — the British financial institutions and large firms — through which Labour intended to act in order to modernise the economy. The very institutions that would be forced to give up their private interests to the will of an elected government were the only institutions through which the economy could be managed unless socialist institutions were created to replace them. And it was of course just this option of the creation of socialist institutions which the Labour leadership had given up in advance. What was intended as a compromise became first a constraint and finally a capitulation. The elected Government could direct and manage everyone and everything else, but not capital.

The immediate form of the payments crisis was an increasing imbalance between exports and imports particularly with respect to manufactured goods. In fact a system of international division of labour in the advanced capitalist world means that the import of manufactured goods is always growing. On top of this it was clear that British industry was no longer fully competitive with the newer industries on the continent of Europe and in Japan, and this ironically was due to a failure of investment because

of the Stop-Go policies imposed as a reaction to previous balance of payments crises. Devaluation would have corrected the immediate competitive situation. But those on the Left who advocated devaluation did so as part of a package of proposals for direct physical intervention in the economy by the government.

In the event, the Government in 1964 neither devalued nor deflated. The import surcharge of 15 per cent in 1964, reduced to 10% in 1965, and abolished in 1966, was no alternative to devaluation. It was designed to reduce imports but did nothing to expand exports. A small increase in interest rates, an attempt at income restraint, and a massive loan took the place of deflation until this was finally accepted in July 1966. Labour's commitments to increase pensions, remove health charges and expand school building and public sector housing were fulfilled. But no corresponding cuts were made in the private sector and among the rich. Thus, with fully utilised resources and only a very modest increase in productivity from investment in the last years of Tory rule, it was inevitable that imports would be pulled in again faster than exports could rise.

The deflationary measures of July 1966 were designed to cut back *all* spending by a credit squeeze and a stop on wages. But the Government was caught once more, as previous Tory Governments had been, by the fact that the very measures taken to deflate — increased interest rates and taxes on consumption — only served to raise prices. Moreover, reduced sales in the home market raised unit costs and checked the investment plans of firms trying to expand in export markets. It was clear that exports were failing to catch up with imports. The gap between them widened steadily in the last quarter of 1966 and the first half of 1967. This was *before* the Suez closure and the dock strikes.

The first mistake in Labour's policies lay in supposing that it is possible to increase efficiency with programmes which retard overall growth. The attempt to sustain investment in the regions of high unemployment while holding back growth elsewhere could never succeed. Firms that don't intend to increase their capacity anyway, because of the depressed market, are not going to invest anywhere despite the extra grants offered in the "black" regions. All that the grants do is to provide private industry with a gift for doing what it would have done anyway. And what it will not do is in effect not done by anyone.

The second and far more serious mistake was to suppose that it was possible to reconcile the needs of the low-paid and the pensioners with so-called incentives to management and private capital; the growth of the public sector with avoidance of cuts in the private sector; economic growth for raising living standards at home with the preservation of the pound as a world currency and the City of London as its custodian. To pursue any one set of policies realistically would have meant rejecting the other

set. It was this fact of choice that was hidden by the idea of a political consensus in an undifferentiated "New Britain".

The facts intervened. In the autumn of 1967 unemployment was already running at above 3% for men and at 2.4% overall. The public sector which had played a crucial part in the relatively expansive and progressive phase of British new capitalism, was being rapidly run down and out. In 1960 employment for men in coal, on the railways, in gas, water, and electricity undertakings and in the steel industry, amounted to 11½% of all male employment. By 1964 this had been reduced to just over 10% and after three years of Labour Government to less than 9%. By 1971 it will have fallen to 7½%, given current proposals for reducing the mining industry and rationalising steel. This melting away of the public sector meant a return to the old callous pre-war labour and manning policy in key sectors of the economy. The long losses of the wage freeze and of rising prices combined with these other factors to make it inevitable that the Governments policies for rationalisation and "spare capacity" were resisted.

This resistance led to strikes in the docks and elsewhere which were of course very damaging to the economy and which provoked a new general crisis. But these strikes were not accidents, they were the inevitable result of the real economic policy being followed. Only policies which actually provided new jobs, less inequality and more control over the conditions of their working lives could have won the co-operation of the workers whose livelihood was threatened. In fact the Government was creating fewer jobs, more inequality and less union control over conditions of work. It is enough to point out that the major conflicts have been between the Government and the Unions, and not between the Government and the employers.

So the British economy had not grown. Production was stagnant but imports were continuing to rise. No alternative trading arrangement had been made with Communist and other trading partners, in the Commonwealth and elsewhere, who were planning their economies and could have entered planned trade agreements. Devaluation was finally forced upon the government.

The Effects of Devaluation

Devaluation by itself solves nothing; it provides the opportunity for a solution — or rather for different solutions of Britain's crisis. Combined with physical controls over the home market and over foreign exchange movements it could have been used by the Labour Government at any time from November 1964 onward to prepare the way for a socialist

solution. Three years later it is being combined with deflation and cuts in Government spending in an attempt at a capitalist solution. Since devaluation means that the prices of our imports rise as well as the prices of our exports falling in terms of foreign currencies, it is evidently on the balance between the two effects that devaluation will be judged by any person or by any company.

For most exporters a 15% devaluation means that costs can be expected to rise by only about 5% (or 7% including the loss of the export rebate) so that they should be able to cut their foreign prices by up to 8%. Whether they will or will not depends on how much extra they can hope to sell by lowering the prices of their particular products. British exporters have had their prices squeezed in foreign markets recently and many have probably been making little or no profit on their exports. They may be expected to raise their profit margins now, but the 8% improvement in their competitive position only puts them back where they were in 1963. This is because since then productivity in West Germany for example has risen by just over 8% faster than it has in Britain. What is more, we have to face the fact that growth in the world market is slowing down and every increase in the sales of British firms must from now on be almost entirely at the expense of foreign firms.

Consensus politics were only possible in a viable British economy working within an expanding capitalist world market. They were undermined by the failing strength of the British economy: a crisis of the world market would deliver the *coup de grâce*. What then is the prospect, writing as we do at the end of 1967? If new plans are quickly put into operation for increasing world liquidity and world trade maintains its expansion, and if exactly the right balance is found between home and foreign demand for British industry to expand at minimum unit costs, with minimal labour troubles, then exports would probably rise rapidly and a large surplus would be established on the balance of payments at least by 1969. A home based boom could follow in 1970 in time for the next election. But even in these most favourable conditions, we should not forget that the result would be a very sharp change in the division of the national product between capital and labour. Profits would boom while real earnings would be held back by the rising price of imported foods. Higher food prices and cuts in government spending, predicated to allow for increased exports, would hit particularly hard at pensioners and other lower income groups.

These most favourable assumptions, which are being widely made by the economists, are based on most uncertain foundations. The new plans for increased world liquidity are in abeyance until the U.S. Government reduces its payments deficit, a reduction which in itself will worsen the liquidity position. Gold might still be revalued if the deficit is not reduced.

Although this would increase world liquid reserves it would not help Britain, which has no gold, and the competitive revaluations that followed might leave Britain where she had been before November 1967. Even if nothing more serious happens in the next year or so the devaluation of the pound has greatly weakened the purchasing power of all the other Sterling Area countries. The value of their reserves is reduced and they may have much more difficulty than British industry in benefitting by extra sales for their primary products in world markets. This especially applies to the less developed countries, which have been important markets for British exports.

The assumption that the balance of home and foreign demand can be got just right is more doubtful even than the assumption about the growth of the world market. The reason for having such doubts is that the only measures which the Government is allowing itself to use to reduce home demand, in order to make room for meeting new export orders, all cut into wages and into the demand of the poor while leaving capital and the demand of the rich unscathed. These measures — of cutting government expenditure on the social services and of freezing wages — are the only weapons in the Government's armoury since it refuses to use discriminatory physical controls. We have already seen that income restraint was not at any point used to discriminate in favour even of the lower paid worker. If Mr. Jenkins now introduces what is called "selectivity" in the social services it will not be to give greater help to the poorest, but to cut the whole bill without the poorest suffering any *extra* loss. This has always been the objection of socialists to selectivity — rent rebate schemes, payment for prescriptions etc. — that it was an excuse for general cuts in the public services and would inevitably lead to the re-emergence of two services, one for the poor and one for the rich.

A continuing wage freeze and cuts in social services might just be tolerated a little longer, if production for export began at once to take up the slack. No one, however, believes that this will happen quickly. The cuts are to come first and the export-led expansion is to follow. Some increases in output at home may soon occur to replace higher cost imports, but the prospect of a high level of unemployment for many months seems assured. This is partly because of the rapid rundown that is planned for manpower in at least three industries — steel, coal and the railways. The last two of these are particularly labour intensive and located in regions where without special government intervention there will be no export industries or import substituting industries.

If unemployment at least in the "black" regions is added to frozen wages and social service cuts, then a major collision of Government and Labour is inevitable. If general unemployment can be held down then the Government might get by with a continuation only of the minor

battles that have marked its progress since taking office. It could take on the miners and the steel workers separately as it has taken on and defeated one by one the seamen, the dockers, the busmen, the railwaymen. It can hardly hope, however, to avoid a still further straining of loyalties and still further spread of the mood of anger and the sense of betrayal that is now rife throughout the Labour Movement.

Conditions will not be propitious for co-operation between Unions, government and employers in the massive redeployment and retraining which modernisation and rationalisation imply. Whatever agreements are reached at the top will be challenged down below if the fear of unemployment is strong and Mr. Callaghan's threat of the need for a wider margin of resources is fulfilled. It is hard to believe that, without using the physical controls we have suggested, the Government could manage a deteriorating situation after devaluation in any other way than by the most ruthless capitalist measures. The Unions would have to be divided and their power broken. The Left would be finally alienated from the Government and the basis for a new coalition government would exist. What can still save the Labour Party as it now exists is only the revival of world trade and a series of lucky strokes (not strikes!) in getting the balance of home and foreign demand exactly right at every stage.

Conclusion on a Programme of Demands for the Labour Movement

It would be wholly unrealistic to suppose that the present Labour Government can be moved to change its policies in the immediate future. On the other hand, it would be fatal for the Left to retreat into local actions for local gains and for local groups of workers, without holding out an overall alternative programme to advance the understanding and confidence of the movement in its future. There is a special danger that local militancy inside certain Unions, and particularly inside those in advanced sectors of the economy, could very well be reconciled — as the Unions in the USA have become reconciled — with policies that are opposed to the interest of the majority of the people.

It would be only too easy for some sections of British Trade Unions to follow the American path, to support industrial modernisation only to allow British capital to try to catch up with U.S. capital at its own game, to improve the position of workers in the more advanced sectors at the expense of the rest, to become even more tied into the emphasis on the production of private goods at the expense of public services. It is the danger of this division between different groups of workers in the more and the less advanced sectors of industry that makes the establishment of united action so essential. The demands which are put forward from

the Left must always have the aim first of uniting the widest range of support from the ranks of Labour and secondly of being seen to make real cuts into the power of capital. No programme which does not include a tax on private wealth and a corresponding expansion of public investment, into industry as well as services, can hope to meet such requirements.

But an effective response from the whole Labour Movement would have to go further. It would need to be two-pronged — on the one hand demanding the extension of workers' control over the processes and costing of production and particularly over the sharing of work as automation reduces labour requirements and creates higher profits in the most advanced industrial sectors; on the other hand, demanding that controls be placed upon private industry — partly physical controls over building and investment and foreign exchange, partly controls that would be imposed as a condition of state assistance — control over prices for example and control over the investment of pension and insurance funds and the much more discriminating use of grants and loans to industry in relation to performance in research, export markets, location, reduced hours of work for the same pay, educational and retraining provision etc.

Finally, the very backwardness of British industry, especially in relation to the United States, demands a special response from Labour, if further American domination is to be avoided. On the one hand, wider trade associations would have to be established with other countries, not as in E.E.C. through supranational and exclusive agreements, but through specially planned joint development projects to find wide enough markets to challenge American technological domination in certain fields; on the other hand, Labour's promised science-based industries under public control would have to be directed to meeting precisely those needs which U.S. capitalism most neglects — the health services and low cost housing for example.

Above all in a period of rapidly increasing mechanisation the major task of Labour must be to bear witness to its historic claim that the object of production should be not commodities but man, that it is not the quantity of goods but the quality of life that matters, and particularly in the human relationships at work which must still occupy the greater part of men's lives.

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