The Economic Club of New York

Britain Back in Business

Nigel Lawson
Chancellor of the Exchequer

April 10, 1986

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Mr. Chairman and Members of the Economic Club of New York, it is a very great privilege to have been invited to address you this evening.

You have had many illustrious speakers in the 79 years of the Club's existence, including Presidents and Prime Ministers. To be the second Chancellor of the Exchequer to be invited in 4 years is a great honor.

Last time I was here at the Plaza Hotel was on the 22nd September last year when, along with my 4 fellow Finance Ministers of the G5, and our respective Central Bank Governors, we came to an arrangement which I think was generally agreed to have been both successful and beneficial.

But whilst I would be happy in due course to answer questions on either that or any other matter which triggers your attention at the present time, I felt that in my opening remarks I might do best to let you know, from the horse's mouth, how the British economy is doing and what our prospects look like.

So let me tonight take you through some of the problems we faced when we first took office in 1979, seven years ago, our approach to them, and the results.

The dismal experience of the 70s had shown very clearly that Britain's chronic secular increase in inflation and unemployment with low growth could be corrected only by a long-term strategy based on firm commitment to sound money and to letting free markets work. Industrial power had to be removed from union leaders whose prime concern was political change not economic progress, and government had to be withdrawn from its over-pervasive presence in industry and commerce.

I am not sure whether the extent to which we are transforming the British economy and society is yet fully appreciated in the United States, so let me contrast some of the old popular perceptions with the new reality.

SICK MAN OF EUROPE?

First, take the old view that Britain is the sick man of Europe, it used to be true. From 1873 to 1982 we were at the bottom of the European growth table. But in 1983 we were top, second in 1984 and in 1985, last year we were back on top again.

For 3 decades the UK grew less strongly, and went into recession more deeply, than its major European competitors. In the 1980s the story has been different. Since the turnaround from the last recession we have out-performed the European average on almost every measure - even including employment. Let’s look at the evidence.

Take economic growth - Growth in gross domestic product. Since our economy turned round in the first half of 1981, 5 years ago, the UK has grown at an annual rate of around 3%. France in the same period has grown at 1½% a year and West Germany at 1¾%.

Then employment - As in the rest of Europe, we have lost a large number of jobs - and I’ll come back to that. But in the UK, unlike in France and Germany, we are now seeing employment rising again on a significant scale. Since 1983, the number of people in work in France is down by about 350,000; in Italy up by 100,000; and Germany up by less than 200,000; but in Britain up by over 600,000. We have created more jobs in the UK than in the rest of the European community put together.

What of investment? Since the trough of the recession 5 years ago UK investment has grown by 4½% a year. German investment has fallen by 1/4% a year while in France investment has fallen by almost 1% a year.

And Productivity - the same picture. For years Britain was overmanned and inefficient, and productivity was sluggish. But over the past 5 years, manufacturing productivity in Britain has risen 51/2% a year. For Germany and France the figure is around 4%.

Throughout the 60s and 70s profitability in British industry was declining. Indeed, in the years of corporatism and collectivism, profit seemed sometimes a dirty word. Here too the picture is transformed. The real rate of return for all companies last year was the highest for 25 years. Even for non North Sea Companies it was the highest for 12 years.

We are now entering the 6th successive year of economic recovery - the longest upswing since the war - with output expected to rise by a further 3%, and inflation to fall to 31/2%.

So for 5 years now we have out-performed our 2 major European competitors in terms of most of the conventional economic yardsticks. That is one measure of the turn-around we have succeeded in achieving. The days when Britain was the sick man of Europe have gone for good.

Inflation: Of course, the price of this sustained growth might have been a resurgence of inflation. But, on the contrary, here too we have turned a corner.

For 20 years, our inflation rate was higher than in most other major industrial countries. Throughout the 1970's UK inflation averaged around 14% a year - half as much again as the average of our major competitors. It had tended to increase from cycle to cycle and from government to government. Persistent attempts were made to deal with it by statutory wage and price controls to the neglect of firm fiscal and monetary policy.

We have preferred the old-fashioned route of sound money and financial discipline. We have directed fiscal and monetary policy to the conquest of inflation. Inflation has averaged 5% over the past 212 years; almost eh same as the OECD average, and within the next few months I expect to see it down to 31/2%. We have broken decisively the pattern of rising inflation rates and demonstrated that high inflation is not inevitable in the UK. So both on output and on inflation the story is one of substantial progress.

Dependent on Oil? Some would have you believe that this turn-around is due not to any benefits of government policy but to the discovery and build-up of North Sea Oil. Well, the recent fall in the oil price has given the lie direct to that.

Over half of the value of that oil has disappeared virtually overnight, with a prospective loss of revenue to the Government of almost 8,000,000,000 a year 0 4% of total tax revenues. If we had been an oil dependant economy, that would have been a catastrophe. The pound would have collapsed, interest rates would have gone through the roof and investment plans would have been slashed. But instead, what happened? Virtually nothing. No crisis. No run on the pound. No scurrying to the IMF for an emergency loan. In fact, it’s been business as usual.

There is not great mystery in this. True, Britain is currently the world’s 4th largest oil producer after the Soviet Union, the US and Saudi Arabia. But oil was only about 5% of our national output even before the price fall. The vast Bulk of our economy produces other goods and services, and does so pretty successfully. What the 5% which is oil loses on the swings, the 95%, which is not oil, gains on the roundabouts.

And let me make one thing absolutely clear. There is no question whatever of the United Kingdom cutting back its oil production in an attempt to secure a higher price. The outstanding success of the UK sector of the North Sea has been based on the fact that it is the freest oil province in the world, in which decisions on levels of output are a matter for the companies and not for the Government, and that is how it will remain. It is in the interest neither of the UK nor the world at large to curb UK oil production in an attempt to keep the price artificially high.
Oil Revenues Frittered Away? There are some who would tell you, not so much that the economy is dependent on oil but that, as a country, we have frittered away the advantages of buoyant oil revenues while the price has been high. But the plain fact is that oil has helped us to build up a stock of net overseas assets which at some $130,000,000,000 is now second only to that of Japan. When we took office in 1979, the UK's net overseas assets were under $20,000,000,000.

Far from frittering away North Sea revenues, we have invested much of them overseas. And that investment will yield a steadily rising flow of income and foreign exchange over the years ahead.

The coal strike - It is worth adding that the fall in the oil price is not the only shock we have been strong enough to survive unscathed. Many of you will know that in 1984/85 we suffered a year-long coal strike.

The National Union of Mineworkers went on strike in spring 1984 on the pretext of preserving the number of jobs in the coal industry. They sought to argue that coal mines should not be closed o economic grounds but only if they we physically exhausted.

You are no doubt aware of the threat the Miners' Union had posed to successive UK Governments in the previous 15 years. Rightly or wrongly, the miners had been regarded as largely instrumental in bringing down Edward heath's Government in 1974 and it was assumed that the National Union of Mineworkers was invincible.

But it was not. One third of the miners stayed at work throughout the strike, protesting that they had not been given an opportunity to vote on whether to strike or not. Members of the union successfully brought legal actions against it for failing to observe their basic rights.

And the government was able to withstand the threat, coal stocks were at a high level, and most important of all, we were financially strong enough to withstand the cost of the strike. That cost was substantial; an extra $6,000,000,000 borrowing by the public sector; $5,000,000,000 off the balance of payments surplus; and almost 11/2% off national output for a year. But we were successfully able to resist the strike for 12 long months until it eventually collapsed in the spring of last year - and to do so without any major problems in the financial markets or any halt to economic growth.

Relation? I ought to say explicitly that this renewed strength of the British economy has not been brought about by anything which could remotely be called reflation. Far from it.

Over the last 7 years, we have halved the annual rate of increase in spending power in the economy, measured in money terms. That has squeezed most o the inflation out of the system while allowing the economy to expand in real terms at a steady and sustained rate.

We have substantially reduced the public sector borrowing requirement - that is, the total deficit not only of central and local government but also the borrowing of the state-owned corporations. As a proportion of our nation income, it has come down from over 5% to under 2%.

Rolling Back the Public Sector - this has been accompanied by a rolling back of the frontiers of the state which is central to our whole policy. The history of Britain from the 1940s to the 1970s was one of increasing nationalization and socialization. That is something we set out, quite deliberately, to reverse. We greatly admire the success of free enterprise in the United States, not just in economic terms but as a way of life. You may be surprised how far we have gone in emulating it.

Take public expenditure for example. I have just come from international meetings in Washington where, among other things, we have compared notes on the trends in our various countries. Did you know that, comparing this year with the average from 1975 to 1982, general government expenditure as a proportion of GDP has increased by 2.7% in the US but - admittedly from a much higher base - by only 0.3% in the UK? That is what official IMF figures show.

The challenge is not just to control more effectively the spending which has to be in the public sector - though we are certainly doing that. It is to get some things out of the public sector altogether. In particular to return to the private sector many of the hitherto state-owned industries - something which has come to be known as privatization, where we can claim to have led the world.

We have already returned to the private sector 20% of the state-owned industry we inherited in 1979 by the end of next year I expect that to have risen to some 40%.

One critical measure of the program is the success of the companies in the private sector. And by that test privatization has already more than proved itself.

Which is hardly surprising, no one can doubt that management and workforce have clearer goals when they are left along by politicians. Moreover we have given particular encouragement to both employees and the public at large to buy shares in the 12 major companies which have so far rejoined the private sector. The largest of these was of course British Telecom, and they also include British Aerospace, Britoil, Cable and Wireless and Jaguar.

Latest figures show that the number of direct individual shareholders in the UK has already doubled since we took office, from 7% of the adult population in 1979 to 14% today.

The impetus to increase direct personal involvement in share-owning will continue. In my budget last month I announced the introduction of Personal Equity Plans which will give tax incentives to the small regular investor who buys shares directly.

Privatization is now being emulated throughout the world, from Japan to France, where privatization was a main plank of the new government's election program, so much so that my new French opposite number is officially styled the Minister for Finance, the Economy and Privatization. I understand that even the US now has privatization firmly on the agenda.

I believe that privatization, couples as it has been with wider share ownership, will prove to be one of the most important innovations we have undertaken, with far reaching economic, social and political consequences.

If anyone doubts this, let them come to Britain and look at the changes which have already come about as we have allowed people to buy the homes they have previously rented form local government. Council Housing, as it is known in Britain, used to be notorious for its unattractiveness. Now whole tracts are being brightened up. You can see the change which persona ownership makes before your very eyes.

On a different level, out venture capital industry has come from almost nowhere to be at least as large as yours in relation to our respective national incomes. The UK today accounts for 2/3 of the total of venture capital investments in the whole of the European community. In short, capitalism in Britain is alive, well and popular.

Freeing markets - of course, even the private sector can only flourish properly if it is itself set free. We have scrapped whole batches of controls - on prices, dividends, foreign exchange transactions. We have got rid of some unnecessary taxes, and reformed and reduced others. We have cut the top rate of income tax from an absurd 83% on earned income and 98% on investment income to 60%. And at 35% we now have the lowest rate of corporation tax in the industrialized world.

The City of London turns over $50,000,000,000 in foreign exchange a day, raised $150,000,000,000 in Eurobonds in 1985, and leads the world in insurance business. It contributed $9,000,000,000 to our foreign exchange earning last year. Financial and business services altogether account for some 13% of GDP. To maintain and enhance this important international rose we paved the way for the revolution that is now occurring in the market which will, as you know, culminate in the so-called Big Bang in October - similar to but perhaps more fundamental than your May Day. This will bring our domestic securities market (the third largest after the US and Japan) on to a more competitive international basis and I am particularly pleased that so may international investment banks have based their plans on the assumption that London will be a major centre of the Global securities market.

Labor Relations - but, for too long in the UK, we have had the special problem that the Labor Unions have been too powerful. This too is changing.

Throughout the 1970s, the large number of strikes and days lost through industrial action were a major feature of the British industrial relations landscape.

Since 1979 the Government has legislated to control the closed shop and picketing; to encourage strike ballots and to restrict excessive union immunities. As a result there has bee a general improvement in industrial relations. The number of dismissals for non-union membership has fallen dramatically. A number of major employers have terminated closed shop arrangements; and we have seen a dramatic reduction the number of strikes. In 1985 the number of recorded disputes was the lowest for nearly 50 years.

It takes time for these changes to have anything like their full effect. Employers in the UK have been conditioned by years of bitter experience to expect union bloody mindedness, and to believe that people are trouble to employ; to prefer machines to men at almost any price.

Hence the continuing high levels of unemployment still the major black spot in our national record. But I am confident that the passage of time will improve the prospects here too.

Conclusion - I have kept this survey short, but I hope I have said enough to show that things in Britain aren't what the used to be. We have been in office 7 years, which in the life of any economy and a society is not a long time. Suppose, 7 years ago, that I had come to the Economic Club and told you this:

That Britain would be enjoying steady, uninterrupted growth of around 3% a year, for the longest period since the war;
That we would move from the bottom t around the top of the European growth league;
That, within that growth rate, investment and exports would have risen faster than consumption;
That we would see a dramatic and sustained increase in both productivity and profitability;
That our current balance of payments would be in steady surplus, year in year out;
That this would be achieved not only with no resurgence of inflation but with a sustained fall;
That we would have returned a 5th of the nationalized industries to the private sector;

And that we would have survived unscathed, both a 12 month coal strike and a halving of the oil price.

I wonder how may of you would have believed me then, yet that is the record I report to you now - not as an aspiration but as a solid achievement.