

MEMORANDUM

THE CRUNCH

Possible Political Repercussions and choices when the Economy can no longer carry on as it is.

General

The politico-economic crunch is not a long way off; it cannot be avoided indefinitely.

The initiative is still in the Prime Minister's hands. There is still time to cut state expenditures selectively (see appendix) in order that the private sector may be allowed some relief without any abandonment of money supply targets, indeed while tightening up implementation of these targets. As the crisis deepens, all cuts are resisted more strongly: by workers, because unemployment and reduced activity make it harder for them to envisage alternative employment; by employers, because private recession increases their dependence on state contracts and purchases. The deeper the crisis becomes, the less initiative and freedom for manoeuvre will remain in the Prime Minister's hands.

(For example, a top trade-unionist with his heart in the right place, asked a friend of mine whom he knew had Conservative contacts, to pass on to the Minister for Industry the advice that the sooner he got all his steel closures over the better for him, because workers now willing to take their "handshake" and go, will resist - under prompting from union militants and militant unions - when unemployment figures become more frightening. This, he agreed was partly psychological, but psychology counts in politics.)

To put it another way, the Prime Minister's capacity to "stand firm" cannot remain unaffected insofar as the ground crumbles under her feet, "the ground" in question being "her constituency", the business sector. If they continue to undergo a squeeze, whose severity is likely to grow in the coming months, and this is not compensated for by substantial cuts in public spending to give hope of an end to interest rates and other concomitants of "crowding out", the private sector will become increasingly restive politically. November's CBI conference will reflect that.

The underlying danger -forshadowed in Sir Keith Joseph's "Monetarism is not Enough" - is that the private sector's desire for short-term survival, which is after all a sine qua non for long-term survival, will lead them into a common front with the TUC and assorted inflationeers, Heathites and ill-wishers, in the demand for immediate relief, without corresponding cuts in government spending, on which some indeed depend.

This will create political strains and stresses which will be exploited by the opposition, not only in Parliament but by extra-parliamentary action. (There is a good piece in NOW of 24 October on SWP's "right to work" strategy.)

There are limits to the possibility of retaining the private sector's political loyalty simply by brandishing the Benn Bogey and then telling them that under Labour it will be even worse. For one thing, some will answer that they have become worse off, not better since May 1979. Some will react that in the long run we shall all be dead. In any case, given the quality press's capacity for self-deception, it will soon have persuaded itself and many of its readers in business and politics that Callaghan's successor is quite a reasonable chap and has the Left in hand, just as they did of Callaghan. Conversely, insofar as the private sector's discontents can be channelled into demands for cuts in state spending, this will strengthen the Prime Minister's hand.

Forms of the Crunch

A As I argued above, a likely development - if it is not pre-empted by remedial initiatives - would be parallel pressures by the CBI and other business spokesmen and by the TUC, backed by Labour, for "relaxation". There is the danger that this would de-stabilise sections of the Conservative Party. Labour could attempt to exploit this to precipitate political crisis by pressing on sensitive and "compassion" issues which would enable some Conservative back-benchers to stage revolts, discreetly encouraged by "smoke signals"- as John Biffen rightly stigmatised them - from front-benchers and their familiars, and seek support from the minority parties.

You will remember that in 1962 - with unemployment a small fraction of what it is today - the TUC-organised Unemployment-March on Parliament, mainly manned by employed workers conscripted for a day's outing, visibly panicked the Macmillan government into expansionary measures - Maudling's "dash for growth", which tripped up. The results played their part, together with Macmillan's handling of the succession, in losing the 1964 election.

There is nothing to stop Labour putting down 'no confidence' motions on potentially divisive issues of this kind. I am not an expert on parliament. But the Liberals - who support Incomes Policy - could find their way into the opposition Lobbies, together with the Welsh and the Scottish Nationalists - who will always gamble on improving their present position in an election - and some of the Ulstermen, out of general pique with the government. This will create strong temptations for the "internal opposition" to hawk their consciences round in one way or another.

B A variant would be a fall in Sterling - followed by a surge in the RPI - precipitated by a combination of any one of the following:

- i decline in political confidence,
- ii a strengthening of the dollar, particularly in the case of a Reagan victory,
- iii a further falling off in non-oil exports,
- iv a continued fall in world demand for oil leading to a fall in oil prices, just at a time when we become net exporters. (We should already be net exporters if energy intensive economically wasteful activities like Steel, Shipbuilding, Council Housing and other state building, and British Rail were not encouraged.)
- v a particularly damaging strike.

C Conversely the Prime Minister could fight the battle on ground of her choosing by instituting a public- public-sector freeze, explaining the reasons to the public, creating a sense of emergency, as in 1931, when the patriotic national response among all classes was so overwhelmingly positive. (Old-age pensioners sending in their pension-books to the Chancellor, etc. The public response is well documented. The Commons' Library could dig it up.) The fact to be remembered is that the National Government was returned in 1935 with one of the biggest swings in British electoral history, though it promised less than any government from the 1870's to our own day.

There may yet be other forms and combinations in which the crunch might come, though they are beyond my range of vision for the time being. But it seems to me that the main division is on two planes. On the one plane, the alternatives seem to lie between the Prime Minister's initiative, and force majeure from outside -events or people or both. On the other plane, the choice is between a momentous cut into parasitic state expenditure, on the one hand, and some form of "relaxation" without cutting state expenditure, ie hyper-inflation, which would entail a crushing political defeat for the Prime Minister and her ideas, and eventually for the party too, on the other. (I deal with the question of the form and nature of cuts - related to the matter of initiative - in a short appendix.)

APPENDIX

The Form of Cuts

As Keith Joseph warned in "Monetarism is not Enough", old errors will creep back in new form. Without substantial cuts in state expenditure, the rate of inflation will continue to rise. But cuts are matters of quality as well as quantity. Cuts, if left in the hands of civil servants and nationalised industry bureaucracies, will be designed to do maximum harm to people and economy while protecting the parasitic structure. One of Sir Harold Wilson's advisors designates this as "off-loading cuts" by civil servants. In nationalised industries, the same process takes place. Sir Peter Parker sells off railway land, which is public property, in order to pay wages for wholly superfluous railwaymen. He neglects maintenance and capital work, so as to present a panic-bill before the elections, meanwhile over-spending on wages and current account.

Cuts can be divided into several categories:

- a Those which reduce socially valuable services, ie less policeman or battleships versus those which simply cut waste, eg council housing, British Steel, Shipbuilding, Rail, etc, surplus central and local government penpushers.

- b Those which mainly cut labour which entails limited complementary resources, eg auxiliary health staff, policemen on the beat, etc, versus those which cut jobs entailing heavy complementary resources, often imported resources into the bargain, including management, credits and investment. This category includes steel, shipbuilding, rail, subsidised manufacturers, and new lame-duck enterprises funded by the NEB and the Industry Act.
- c Those which leave resources unused, versus those which release resources for productive use. For example, where concentrations of nationalised industries or subsidised work-simulation centres exist eg shipbuilding and steel, paying higher wages for little work - since the real purpose is not production but "employment" anyway and there is no incentive to cut costs - private employers, existing ones and more so potential ones, are priced out of the market. So unemployment persists and is then used as a reason for maintaining make-work, a vicious circle. If nationalised, some ~~subsidy~~-consuming firms, could actually earn money.

All in all, "crowding-out" is not only financial but resource-wise, ie operations of the nationalised industries raise the cost of all resources - labour, raw materials, management, financial resources, to productive industry. It is this combination of high internal costs with a high Pound which is so irksome to industry.

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These considerations become important in view of the imminent political decisiveness of the "crunch" for good or evil.

END

30 October 1980