Editorial—The Core of Inflation

"What we must aim at is not growth plus the highest possible degree of stability, but stability with the highest possible degree of growth."

Franz Heinrich Ulrich — Chief Executive, The Deutsche Bank, West Germany.

In the last few years the rate of inflation in many of the Western democracies has accelerated sharply. Rapid increases in wage costs and prices, and the failure of official policies to curb these increases, have given rise to a sense of despondency and even alarm.

Australia, which for some time was able to point with complacency to its relatively slow rate of inflation, now faces a similar situation. The Consumer Price Index for the December quarter, which does not include the 6 per cent national wage increase, revealed a rate of increase in prices of nearly 8 per cent a year. This, combined with the prospect of continued rapid inflation during 1971, has spread a feeling through the community almost akin to fear.

It should be noted that the 6 per cent wage increase followed hard on the heels of substantial increases in various State and Commonwealth awards. Two outstanding examples are engineers and executive officers of the PMG’s Department and the Melbourne and Metropolitan Board of Works who have received total increases of around 21 per cent. The Minister for Labour and National Service, Mr. Snedden, then predicted that average earnings in Australia would rise by 10 per cent in
1971. As national productivity can be expected to increase at the most by 3 per cent, this would suggest a price rise of 7 to 8 per cent in the current year.

There is widespread agreement that strong action to curb inflation is required, but no clear or confident consensus on what this action should comprise.

To have any chance of being effective, a policy to check inflation must start by recognising one central, inescapable fact common to all the free economies as the 1970 decade gets under way. This fact is the insistent urge of practically everyone to achieve rapid year-by-year improvements in their living standards — politicians, doctors, teachers, public servants, no less than the great mass of wage and salary earners. This has been well described as the revolution of rising expectations. Moreover, rightly or wrongly, probably wrongly, people equate their living standards with their disposable incomes (incomes after tax) that is, with what they have to spend on their personal needs. They do not include in this assessment the quality of the community facilities in schools, roads, hospitals and the rest available to them, although are quick to complain when these are seriously deficient.

In the last few years, demands for improved living standards (in this sense) have greatly intensified throughout the Western economies. In Britain and the United States, wage agreements in key industries are providing for increases ranging from 10 to 15 per cent. Precisely the same is happening in Western Germany and other European countries. These increases are, of course, many times in excess of the yearly gains in national productivity and are pushing up prices at a threatening rate.

Australia has now caught the contagion and the rate of increase in average earnings is accelerating sharply. What can be done about it?

In the Australian context, the revolution of rising expectations is colliding head-on with the national goals of rapid population increase and development. In this conflict is to be found the root cause of the Australian inflation. The massive scale of the migration programme means that an unusually high proportion of resources must be devoted to capital expenditures of a kind which make no immediate or early contributions to the improvement of living standards. Resources
used for capital purposes mean a reduction of resources available for consumption purposes and, in fact, the rate of increase in consumption expenditure in Australia has, for many years, been the lowest of any of the advanced Western economies. The Australian people are now exhibiting increasing impatience with the slow advance in their living standards.

The capital expenditures of governments, at all levels, are by far the most inflationary, not only because the benefits are usually long delayed, but because they are of a kind which the people do not associate with an improvement in their personal living standards. Practically all these expenditures are financed by heavier taxes and municipal rates, and by higher charges by public instrumentalities such as the PMG’s Department and those concerned with gas, electricity, water and transport. These taxes and charges are, in fact, the means by which resources are diverted away from the satisfaction of consumption demands.* But higher taxes merely serve to inflame the ever-present, smouldering demand for higher incomes. (This is especially true since the advent of Pay-As-You-Earn taxation.)

In this situation, the options of the economic managers are limited. Since the war, the use of the fiscal weapon to curb inflation has invariably been associated with an increase in taxes. The use of the other prong of the fiscal weapon, the reduction of government spending — because of the rate of population growth and the consequent need for the expansion of community facilities — has been regarded as impracticable.

Mr. Gorton’s T.V. address to the nation on January 29th seemed to amount to a remarkable change of approach and gave rise to hopes that Government was at last about to devise a strategy to deal with inflation which would strike at the underlying causes. The address suggested that higher taxes and interest rates, for the time being at any rate, were to be discarded from the armoury of counter-inflationary measures. The emphasis was to be on the reduction of capital spending, and particularly the capital spending of governments.

The Prime Minister’s speech also indicated that vigorous action against restrictive trade practices and a more discriminative use of tariffs were to be part of the policy. Neither of these measures should be taken too seriously as a counter to inflation.

*This argument is developed more fully in the Appendix.
Britain and the United States have had trade practices legislation for many years; they are also suffering from rapid inflation.

The policy thus stated held out the best prospect yet, not perhaps of stopping inflation altogether, and certainly not tomorrow morning, but of rendering it more manageable. At the same time it amounted to an extraordinary confession of error. For only a few months previously the Commonwealth Government had brought down a Budget providing for record increases in government spending, under pressures from State Governments endeavouring to cope with a huge intake of migrants. The Budget had also embraced largely futile, indeed harmful, increases in company and indirect taxation.

After the bold and admirable expression of intentions in his T.V. address of January 29th, Mr. Gorton’s statement to Parliament, only a little more than 2 weeks later, came as a shock to thoughtful and responsible people. The community was expecting at least the outline of a rounded, long-range plan to grapple with inflation; all they got was the brusque announcement of cuts in Commonwealth spending (running at over $8000 million a year) amounting to $75 million over the remainder of 1970/71. This would have been applauded had it been placed in the setting of a long-term programme to reduce spending by governments at all levels and to cut back the proportionate claims of the public sector on total national resources. Even with the cuts so far announced, the rate of Commonwealth spending in 1970/71 will expand by 11.4 per cent — slightly more than that predicted in the Budget estimates — and far above any possible increase in the Gross National Product. As it is, people have been left wondering if resolution has, for some reason, weakened since January 29th.

An ironical sequel of the Commonwealth’s decision to cut public spending has been the announced intention of the Victorian and South Australian Premiers to increase taxes, and also charges for public services such as transport, gas, electricity and water. If this course is persisted in, the central pillar of the Commonwealth’s counter-inflationary policy — the reduction in government expenditure — will be undermined. The cost of living will be further raised, inciting another burst of claims for higher incomes all round. Unless State expenditures are cut substantially, like the famous tower of Pisa the structural lean of the economy — toward inflation — will remain uncorrected.
No one would expect overnight results — in any event we will not get them as the prospect for the months ahead is for continued and possibly steep price increases — but at least the nation should have been left in no doubt about the strength of the Government’s resolve to rid the economy of inflation. This resolve will be tested in the Budget next August. Unless the Budget provides for a substantially reduced rate of government spending throughout the public sector, and especially at State levels, inflation is likely to continue. The central aim of government strategy must be to alter the disposition of resources between investment and consumption (or living standards) more in favour of the latter.

An inevitable corollary of this course is a reduction in the huge migrant intake to reasonable proportions. The reduction must be much more than nominal — perhaps to somewhere about half the present level. We should endeavour to maintain, however, the flow of skilled workers which in 1969/70 amounted to about one-third of the gross worker migrant intake.

Notwithstanding the huge outlays on capital works, the standard of public facilities in every field has continued to fall alarmingly below that deemed desirable in a modern community. The core of the whole problem resides in the fact that the rate of population growth cannot be supported, even at minimal community standards, without inflation.

Unless the Government’s fight against rising prices is carried to the point where excess pressure on resources is eliminated, particularly for labour, and also receives the full co-operation of the community, it will fail. The second proviso is no less important than the first. When living costs are soaring, government gets the blame. And it is true that the national government must bear the major responsibility. But national policies, it is often forgotten, reflect the pressures imposed on governments by the people.

Looked at in this way, practically every section bears some responsibility for inflation because in urging governments to spend more for their special benefit, or to follow policies of maximum growth (inseparable from additional expenditure) they act in a way which makes rising prices inevitable. Then everybody overlooks his own contribution to the end result and seeks to cast the blame elsewhere.
The Core of Inflation (continued)

The trade unions, for instance, are far from guiltless. Those unions which serve extravagant wage demands, or use any pretext to instigate work stoppages or go-slow measures, add their quota of fuel to the inflationary fires. Nor are employers entirely free from responsibility. There is a vein of truth in the view expressed in the National Wage Judgment that some employers are over-ready to reach an accommodation with the unions, especially when they are in a position to pass on increased costs in higher selling prices. State Governments, self-righteously obsessed with development at any price, should try to understand the economic consequences of what they are doing. Moreover, they have a special duty to set a good example. No one will deny the right of a member of parliament to a fair reward for his services, but for a State Parliament to grant itself a 22 per cent increase in salaries, at a time of great delicacy and looming inflation, surely amounts to a regrettable disregard of the public interest.

If as a community, we are earnest in our desire to overcome inflation — and it is certainly in the interests of us all to do so — then all sections must accept their share of the sacrifices required and must work together to conquer the common enemy. Unless there is change of heart right through the community, inflation will persist.

APPENDIX

Extract from “Curbing Inflation”
IPA Review April-June 1970

The cause of inflation is generally attributed to an excess of total demand over total supply. This is the explanation that usually emerges from official and academic quarters. It follows from this that to stop inflation, total demand (or, more precisely, the rate of increase in demand) must be reduced to bring it into balance with available supplies.

To ascribe inflation to excess demand, however, is merely to state a truism. What has to be determined are the causes of the excess. In this regard, there are two ratios within the total complex of demand which are significant: the ratio of expenditure on investment to expenditure on consumption and the ratio of private sector spending to spending in the public sector. In the Australian context, given the strong bias towards investment rather than consumption and toward public sector spending, particularly on capital projects, these relationships have a special importance.

If inflation could be cured simply by cutting back total demand — as the conventional wisdom suggests — then it is immaterial whether the measures affect mainly private demand or government demand, or investment spending or consumption spending. All that would matter is that the total be reduced. In actual fact, in Australia, it is private demand that gets the axe, while government
spending proceeds virtually unchecked. Also, the brunt of disinflationary measures always falls on consumption rather than investment.

The weakness in this approach is that if anti-inflationary policy impinges too heavily, as it invariably does, on private sector spending and on consumption spending, it gives rise to dangerous side-effects. Both the private sector as a whole, and the people in their capacity as consumers, strongly resist the attempt to cut down their shares of the available resources. This resistance results in a competition for resources between consumption and investment on the one hand, and between the private and government sectors on the other. Where the proportions of investment expenditure and of government expenditure (on goods and services) to total expenditure are already unusually high, as they are in Australia, the resistance, and the resulting competition for resources, is certain to be quite fierce.

The orthodox view assumes that this competition for resources must remain latent so long as consumers and the private sector are deprived of the means to express their demands. This, it is argued, can be achieved through raising taxes on individuals and businesses and by imposing restraints on their ability to borrow through the normal monetary channels. What this overlooks is that neither the consumer, nor the private sector, will submit to a severe curtailment of the resources available to them without taking compensatory action.

Faced with a sharp reduction in their current consumption standards (because of higher taxes, greater difficulty in borrowing, and higher charges for what they are able to borrow) consumers will react by demanding increased incomes, by cutting down savings and by seeking ways of borrowing outside the banking mechanism. Businessmen will resist the curtailment of the resources available to them (and their appropriation by the government sector) by raising prices and by competing strongly with governments for the supply of investment funds. The rise in the price of money (the rate of interest) that follows is evidence of this competition. Thus, attempts (which heavily penalise consumers and the private sector) to bring total demand into balance with supplies are certain to lead to retaliation by those affected and thus to new inflationary pressures which tend to undermine the purpose of the whole exercise.

To rid the economy of inflation (by curtailing demand) it is essential that the action be directed at the trouble spots. These are the imbalance between consumption and investment expenditure and between private and public sector spending. The main burden of the measures taken must fall on capital expenditure, and particularly the capital expenditures of governments.

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Responsibility for Inflation

EVERY so often the Commonwealth Conciliation and Arbitration Commission seems to be overcome by a strange aberration. When this mood comes over it, the Commission produces a decision which disturbs, and even shocks, many thoughtful people in the community. These people do not need to have a Ph.D in economics to know intuitively that the decision is an unfortunate one which may have far-ranging and adverse repercussions upon the economy. The award in the 1970 National Wage Case falls into this category. The Work Value Judgment of 1967 was another of the same species.

The task of the arbitration authority in national wage cases has become fairly clearly defined. On the one side, the Commission must have regard to the prevailing industrial climate and its responsibility for promoting industrial harmony. On the other side, the Commission must refrain from paying a price for industrial peace that might seriously disrupt and injure the economy. This is an extremely delicate, indeed unenviable, task, but it is one which the Commission might fairly claim to have performed in the National Wage Judgments of 1968 and 1969. The increases awarded in both these years, amounted, in effect, to an average 3 per cent addition to award wages. In the 1970 Case, the Commission, inexplicably, doubled the increase by awarding something over 6 per cent — around 8 per cent for a small minority on the minimum wage and 6 per cent for the rest.

What caused it to do this? The broad situation in the economy at the end of 1970 was certainly no stronger or sounder than in 1968 or 1969. Indeed, the threat of inflation is more pronounced at the moment than for over a decade. In addition, there is the complication imposed by the ailing rural sector, especially the nation’s major export industry, wool. On both these grounds the Commission might have been expected to tread more circumspectly even than usually.

Admittedly, this was not easy. There were two other factors which the Commission clearly felt unable to disregard in arriving at a judgment. One was the serious unrest throughout industry, evidenced by the fact that the record of days lost through work stoppages in 1970 was the greatest for 40 years. A second fact, which weighed heavily with the Commission, and which itself was a major cause of industrial disturbance, was the growing disparity between wages paid in different industries. This disparity was a consequence partly of the ability of strongly placed unions to extract higher wages from certain industries, and partly of competitive bidding by employers for types of labour — especially skilled categories — in short supply.

In light of the wage disparities that had developed in recent years, the Commission felt compelled to attempt to introduce a greater degree of equity into the wage structure by assisting the large body of less favourably placed workers.
The Judgment makes clear that this consideration had a major influence on the Commission’s decision. “If we are not realistic in our attitude to wage fixation then those who look to the Commission as their main source of wage increases, and there are many who do, will be treated inequitably, while more and more those who are strong enough to do so will seek increases in the field . . .”

It must be doubted, however, whether the Commission’s decision will, in fact, reduce present inequities in the wage structure. Those workers on higher awards will receive a bigger absolute increase than employees on lower awards, and the divergence between the two will thus be widened. Against this it might be argued that with workers on identical award rates, but differing over-award payments, those earning less will receive a larger percentage addition to their actual earnings than those earning more. Apart from the lowest paid workers close to the minimum wage, it must, however, be queried whether the Commission’s decision will realise the basic intention of its own Judgment.

The Commission has awarded a highly inflationary wage increase at a time when expansionary economic forces are already dangerously in the ascendant. There is no doubt that costs and prices throughout the economy must rise as a result of the new award. The Judgment itself concedes this: “In our opinion the increase we propose to award will cause some increase in prices.” The Commission, admittedly, cannot be held to carry the prime responsibility for correcting or avoiding inflation. Nevertheless, where inflation is threatening, the Commission, as a custodian of the public interest, should move cautiously in making its wage awards.

The Submission of the Commonwealth in the National Wage Case made it clear that the Government regards the Commission as having a major duty to avoid wage decisions which will add materially to costs and prices. A crucial consideration in a national wage case is the concept of economic capacity. How much can the economy afford to pay? The Commonwealth Submission supports the succinct definition of capacity to pay given by Professor Karmel, now Chairman of the Australian Universities Commission. “Capacity to pay must be taken to mean the capacity to pay the highest level of money wages without a rise in prices due to wage influences.” Unfortunately, this amounts to a doctrine of perfection seldom, if ever, observed by the Commission.

The Submission of the Commonwealth, while admirable for the picture given of the economy and for its simple clarity of expression, nevertheless is to be criticised for attempting to place the main burden for avoiding inflation on the Arbitration Commission. The Commonwealth argues that if increases in actual average earnings exceed gains in productivity, prices must rise and, other things being equal, will rise by roughly the difference between the two. This proposition is substantiated by some interesting figures for the 15 years from 1954/5 to 1969/70.

Average productivity increase — 2.5 per cent a year.

Average earnings increase — 5 per cent a year.

Increase in consumer prices — 2.4 per cent a year.

The Commonwealth purports to see in these facts the main cause of long-term inflation in the Australian economy.

This explanation of inflation has a lot in common with the conventional theory of excess demand. It is a definition rather
Responsibility for Inflation (continued)

than a diagnosis, a statement of a truism rather than an analysis. Of course prices will rise if demand exceeds supply or if incomes run faster than productivity gains. A first-term economics student could tell us that. A much more difficult and important question to answer is why demand is excessive or why incomes are rising too rapidly.

The Commonwealth Submission argues that the cure for inflation is to keep increases in wages, or more precisely in incomes of all kinds, in step with increases in productivity. What the Submission most curiously overlooks, however, is that the tendency for the rise in incomes to far exceed productivity improvements is due not only to the awards of the national wage-fixing body but also to policies for which the Government itself is responsible.

The Submission quotes some figures of the rate of increase in average earnings. Decade to 1963/64 — 4.5 per cent a year. 5 years to 1968/9 — 6.1 per cent a year. 1968/9 — 7.2 per cent. 1969/70 — 8.9 per cent.

Thus in recent years the rate of increase in average earnings has accelerated quite markedly. At the same time overtime payments have become progressively greater and the gap between actual earnings and award wages has widened. This is shown in the table below:

The Commission can hardly be held accountable for this situation. The earnings drift is, indeed, traceable in the main to the policies of the Commonwealth Government itself. The Commonwealth Submission maintains that the Government has played its part by keeping total demand in step with total supplies — and thus avoiding excess demand — through its fiscal and monetary policies. Surprisingly, it quotes, as an example of counter-inflationary action, the 1970 Budget which provided for record increases in government expenditure and which most independent observers regarded as strongly expansionary. The Commonwealth's position is, in this regard, quite untenable. If the official Government view is to weigh strongly with the wage-fixing body — it seems to have had little effect so far — then the Government must clearly put its own house in order first.

It is, of course, unfair to attempt to sheet home the main responsibility for inflation to the national arbitration authority. One must have some sympathy with the President, Sir Richard Kirby, in his defence of the Commission against its critics. Strong pressure appears to be building up to turn the Commonwealth Conciliation and Arbitration Commission into a kind of Incomes body which would limit wage rises to the average growth in national productivity — between 2 and 3 per cent a year. However, it appears that this may not be possible under the Constitution which restricts the Commonwealth's role in industrial matters to the prevention and settlement of interstate disputes. But constitutional limitations aside, any attempt to compel the Commission to act as such a body would weaken its capacity to contribute to industrial peace. To perform this function the Commission, in major wage decisions, can hardly avoid

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paying some regard to the industrial climate and to the feelings of the millions of people whose everyday lives are affected by its Judgments. In the recent National Wage Case the Commission was clearly influenced by the prevalence of widespread industrial unrest, and it was right in attributing this partly to the inequities which had developed because of large over-award payments in industries chronically short of labour. This can be said without applauding the actual decision. It was not a good one. Even the members of the Commission seem to have been somewhat uneasy about the magnitude of the increase granted for they sought justification in the untenable notion (which is nevertheless widely accepted among the community) that so long as prices and costs are rising no faster in Australia than in other countries little harm can result. This is dangerous thinking and its fallacies were convincingly exposed in the Submission of the Commonwealth. Yet, in the face of this, the Commonwealth's arguments are inexcusably and incomprehensibly ignored in the Judgment of the Commission. The Judgment states, "On the material before us we broadly accept the argument that Australia's overseas trading position is not adversely affected if our rate of inflation is no greater than the rate of inflation in countries which compete with us for markets . . .".

The real point at issue for Australia is, however, not whether our costs are rising no faster than costs in other countries, but whether they are rising faster than prices for our main exports. Over the past decade export prices have risen at a mere 0.3 per cent per annum compared with a 2.2 per cent rise in consumer prices in Australia. As an exporter mainly of raw materials, the continuance of inflation poses a more serious problem for the Australian economy than it does for countries which depend mainly on manufactured exports and which may be in a position to pass on increases in costs by raising prices.

But when all is said, the main burden for coping with inflation rests with the Commonwealth Government and nowhere else. The leadership in moderating inflation must clearly come from the Commonwealth. The prevention of inflation is simply not consistent with an ever-increasing tide of government spending and ever-increasing claims by governments on the resources of the community.

Members of the Government have questioned the wisdom of the Commission. They might do better to start by questioning the wisdom of their own economic policies.
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JAPAN: The Emerging Super-state

WITHIN a quarter of a century Japan could take over from the United States as the greatest economic power in the world. This is the staggering view of an American authority, Herman Kahn, Director of the Hudson Institute.* Kahn's book, "The Emerging Japanese Super-state", has been widely noted in American business circles and apparently also in Japan itself. Possibly no country in the world has a greater concern with the future of the Japanese nation than Australia, and Kahn's book would repay reading and study.

In the next decade or two Japan will almost inevitably achieve giant economic, technological and financial stature. Kahn says eventually Japan is likely to strive to become a military super-power as well.

Among a range of possibilities, Kahn predicts that Japanese per capita income could rise from $U.S.1,950 in 1970 to $5,000 by 1980 and to an incredible $20,000 by the year 2000. He suggests that by 1980 Australia's per capita income will be $4,500 (1970 $3,000) and by 2000, $10,000, half that of Japan's. Kahn says that Japan will probably pass the United States in per capita income in 1980 and in total GNP by 2000.

The reason why Japan is able to achieve growth rates almost twice as fast as any country in Europe, America or the Communist bloc has perplexed and intrigued politicians, businessmen and economists in the Western democracies. We are able to give here only a selection of Kahn's reasons for Japan's phenomenal rate of progress.

As one would expect, a major immediate reason for Japan's growth is an abnormally high rate of capital investment supported, of course, by an abnormally high rate of savings. The ratio of gross fixed capital investment to GNP is close to 35 per cent. This compares with 15 to 18 per cent in Britain and the United States, and around 26 per cent in Western Germany and Australia.

Why are Japanese savings so great as to be able to support a rate of capital investment of over 30 per cent without serious inflation? One of the main reasons appears to be the high ethical importance long attached to thrift in Japanese society. Another is the peculiar Japanese wage system; about one-third of an employee's annual salary is paid in the

The Hudson Institute is a privately financed research organization somewhat similar to, although smaller than, the Rand Corporation. From an earlier emphasis on the settlement of international crises through arms control and appropriate strategic and political policies, the Institute has since turned its attention more to economic matters, including the development of world resources and the future international environment of the business corporation.
The Japanese birth rate is currently around 20 per thousand, the same as Australia's. In 1947 the birth rate was 34 per thousand but was reduced to the present figure largely through the establishment of abortion clinics all over Japan by the Government.

In the years to come it is clear that Japan will have to invest a great deal more in infrastructure development and environmental controls and, according to Kahn, intends to do so. He indicates that one of the major Japanese aims is to make Japan a model for the world in environmental beautification and in achieving a solution to the great problems of industrial fall-out. While some observers appear to think that this will lead to a slowing down of Japan's growth rate, Kahn does not agree. The new Comprehensive National Plan adopted in May, 1969, is intended to make Japan into a kind of garden community so that it will be able to say to the rest of the world, "Not only can we equal you in economic development but we can do it without wrecking the country, the environment and the general amenities of living". The Plan seeks to maintain "harmony between man and nature". As the Japanese rate of growth is so extraordinarily rapid, Kahn believes that this objective could conceivably be achieved by diverting only a small proportion of its growth, or a mere 1 or 2 per cent of GNP, to purposes of environmental improvement.

What are some of the other main reasons behind Japan's phenomenal growth rate? Productivity studies in other countries have led to the conclusion that high productivity has its ultimate source in the attitude of mind of the people concerned. ("It is faith that moves mountains even when it employs bulldozers.") The people's attitude of mind have a unique importance in the Japanese context. The Japanese people are traditionally hard-working, dedicated, determined and enterprising. But, it may be argued, so are other peoples. A special characteristic of the Japanese, of the utmost importance in any attempt to nail the reasons behind their economic miracle, is the overwhelmingly powerful sense of group loyalty — in the first place to the family, then to the company, and finally to the nation. Kahn points out that in nearly all activities and issues the Japanese traditionally think of themselves as members of a group and their satisfactions are largely expected to come "through group fulfilment of group objectives". With this attitude it becomes almost a cardinal sin to let the group down, whether it is the family, the business by which one is employed, or the nation. Kahn notes that Japan is probably the only large country in the
world in which almost everybody concerned — management, labour, consumers, family, the general public — tends to "identify the success of a business firm with the success of the nation and with his own individual success". He says that the Japanese watch growth rates with the same interest that Americans follow football scores or the standings of baseball teams. "Japan is a society and culture probably more interested in national prestige than any other in the world today." There is thus an extraordinary willingness in Japanese society to make whatever adjustments and sacrifices are necessary for economic growth.

There is an exceptionally strong bond between employers and employees who often regard themselves as members of the same community rather than as antagonistic capital and labour. The company is the basic unit of labour organization rather than the trade union. (About 35 per cent of Japanese workers are unionised).

Recently, according to a German newspaper article, a British observer was quite astonished by the discipline and dedication of the workers at the Toyota motor car factory and the fact that there had been no strikes in the company for the last ten years; he understood why Toyota, with only one-fourth of the work-force, produced more cars than the British Motor Corporation.

The three main features of Japanese industrial relations, which contrast with Western practices — the provision of virtually life-time employment by big companies, promotion by seniority, and compulsory retirement at 55 — would seem to make for inefficiency. But so far they appear to have done the opposite. With their employees morally bound for life, firms are encouraged to invest heavily in worker education and training. This also greatly strengthens the loyalty and sense of participation on the part of the worker. Compulsory retirement at the age of 55 for all executives, except those with the ability to move on to the highest managerial and directorial levels, enables replacement of those with moderate abilities at a comparatively early age by younger, more energetic men. The lump sum paid to those retiring is usually not quite sufficient for their needs thus encouraging them to continue work in some other field at a reduced salary.

The nature of the relationship between government and industry is significantly different from that obtaining in most of the Western economies. In Japan, government uses free enterprise as the instrument of economic progress. There is no feeling of division or any clash between government and business in pursuit of the over-riding national objective of rapid economic growth. In some Western economies government and business seem to some extent to be in opposing camps, and the bureaucracy almost anti-business. But Japanese bureaucracy and business work closely together in pursuit of the major national objectives and are complementary to one another. Kahn contrasts this with the United States where he claims government has, in effect, become a "strain-creating, expense-creating organization rather than a facilitating and growth-creating organization". In this regard the Japanese system seems to bear some affinity with the French where there is close and detailed co-operation between government officials and business leaders.

Kahn attaches high importance to skilful economic management as a factor contributing to the Japanese economic miracle, and the willingness of the Government to act decisively and urgently when the occasion demands. He says that no one else would have been prepared to do what the Japanese have done three times since the war. They
have artificially created three very sharp, very severe and very short recessions to correct threatening balance-of-payments’ situations.

Kahn states that Japanese skill and responsibility in manipulating fiscal and monetary policies are largely unregarded in the West. However, the London Economist did note in its columns last year that Japan had the most sophisticated and most closely controlled economic system in today’s world.

Kahn says that another factor in Japan’s post-war productivity gains was the availability of American technology at bargain basement rates compared with what European countries had to pay. However, the Japanese are far from the copyists they were labelled in pre-war days. Expenditure on research and development by Japan is probably greater than in most European countries. Kahn confidently predicts that it will eventually be comparable with that of the United States and Russia. He is emphatic that at all levels, and in all kinds of areas, the Japanese are now technologically competent and sophisticated.

Another fact that has contributed to Japan’s rapid growth is the small proportion of its resources allocated to defence. Kahn points out that this has been possible because of the American nuclear umbrella. However, the position could change in the future.

The current defence budget of $1.35 billion is less than 1 per cent of the GNP. The Government is aiming to increase this figure in the early 1970’s to about 1.5 per cent. By 1975 it could reach an absolute level of $5 billion, which would be very high by international standards. Japan is obviously now thinking a great deal more about the matter of military power, although, as Kahn says, no Japanese politician is as yet prepared to publicly advocate nuclear armament. Increasing pressures for greater defence efforts are coming from the business community, because 90 per cent of Japan’s military hardware is made locally. Kahn seems to think that it is unrealistic to expect current “low military and political postures” to be maintained very far into the 80’s and perhaps not even through the 70’s.

Will Japan ever become a nuclear power? On this question Kahn is less than definite. He leaves no doubt that Japan will soon have the technological capabilities to be one. By the mid-1970’s her nuclear-based electric power industry could be modified without much difficulty to produce up to a thousand small nuclear bombs a year. Kahn says that a Japanese decision to acquire nuclear weapons would be one of the great turning points of the 20th century world, because it would almost certainly lead to the acquisition of such weapons by Germany, India, Italy and eventually many other nations. If this should come about, we would then be truly living on a nuclear razor’s edge, in a world of unpredictable political balances and enormous uncertainty. On the other hand, Kahn emphasises the great benefits to the Japanese should they decide to go through at least the 1970 decade without nuclear weapons — benefits both of an economic kind and in national prestige throughout the world. He speculates that this may well be the direction that Japanese policy will take, but points out that this would, of course, amount to a decision to live under the American nuclear umbrella.

The Japanese are apparently very concerned with the attitudes of other countries towards them, leading Kahn to comment: “If Americans appear to be always wanting to be loved and are anxious about their popularity rating, then this is all the more true of the Japanese; when they are abroad in fact, they show a constant pre-occupation with the problem.” But the Japanese are unlike the
Americans in that they are not concerned to export their ideas or institutions and techniques to other countries. All they are concerned with are to be admired and respected. Kahn says that, “As I have studied and visited Japan, I have found myself not only knowing more about the Japanese but admiring and respecting them, and even liking them more and more.”

Kahn’s view that Japan is in some ways the most racist nation in the world comes as a shock. He points out that by contrast with China and other countries, the children in Japan born of other parentage are barred from participating fully in the society. Children of mixed marriages apparently cannot hope to rise to positions of high importance.

The discovery of rich mineral resources in Australia is regarded by Kahn as one of the factors contributing to Japan’s “economic miracle”. He argues that the close connections now developing with Japan will eventually prove to be a very good thing for Australia, not only economically but socially and culturally. These connections he believes are likely to force Australians away from “their rather parochial and inbred life into the most stimulating and cosmopolitan existence”. Australia is one of the few countries which has consistently been able to maintain a favourable trade balance with Japan — exporting roughly double what it imports. Japan also purchases 60 per cent of all Australia’s mineral exports. But despite these facts Japanese investments so far in Australia have been insignificant. Kahn suggests this situation is unlikely to last for Japan is now becoming a major source of international investment capital. Since 1951 only 3 per cent of Japanese investment has gone to Australia and New Zealand, compared with 29 per cent to North America, 27 per cent to South America and 15 per cent to South East Asia.

Stemming from World War II, Kahn says that fear of Japan still exists in Australia and, as Japan’s strength increases, Australians are likely to become more anxious than ever to maintain an American involvement in Pacific-Asian affairs. He asserts that it is very important that Australians not feel that they have been left alone to face or work with Japan in the region.

If Japan continues to grow at rates comparable with those achieved in the last 20 years, by the end of the current decade it must surely become the third most important international power in the world, far surpassing its giant neighbour, Communist China, in influence and significance. The Japanese economy is already about twice the size of China and growing at two to three times as fast. Kahn says, “It is soon going to be increasingly clear, at least to foreigners, that Japan not China is the big power of Asia.” He believes that by the mid 1970’s Japan will probably pass Russia in per capita income and from there on every succeeding year is likely to see a growing gap between the two countries in standards of living.

Herman Kahn’s admirable book is clearly the product of a man not only skilled in the balanced interpretation of facts accumulated by intensive research, but with considerable personal experience of the Japanese people and their country. His findings are of special importance to Australians. Japan’s economic achievements since World War II are so unbelievable that it is strange they have not aroused more attention, particularly in Australia whose economic destiny is so closely linked with the emerging super-state.

The future implications of the Japanese economic miracle are so portentous that this lack of knowledge and interest cannot continue for much longer. Kahn’s book deserves to be read and studied by those Australians with a responsible concern for the future of their own country.
Britain Goes Right Ahead

An Assessment of Ted Heath’s Counter-Revolution

by

JOSSLEYN HENNESSY

Jossleyn Hennessy is well-known to readers of the I.P.A. Review in which he analysed Britain's postwar economic problems in June, 1966, discussed the pros and cons of U.K. entry into the Common Market in March, 1967, and the implications of the devaluation of the £ in March, 1968. Sometime Director General of the British Foundation on Automation and Employment, he has contributed prolifically to the Economist, Statist, Lloyds Bank Review, the Times, Spectator, Sunday Times and publications of the British Institute of Economic Affairs.

Is Ted Heath, as Harold Wilson (a not inconceivably biased observer) says, trying to put the clock back long past the depression years of the 1930s to the compassionless laissez-faire of the 1830s?

As a result of Butskellism — the pragmatic compromise of R. A. Butler with Socialism and of Hugh Gaitskell with Capitalism — there is no sector in the British economy in which (1) some form of bureaucratic supervision has not encouraged inertia and discouraged initiative in private enterprise, or in which (2) the state has not, with every passing year since 1945, got itself more deeply involved in forcing mergers, pumping money into research and development (with unbelievably small results), pouring millions (“to maintain employment”) into obsolescent firms or (“in the national interest”) into developing industries (for which over-taxed investors have no funds to spare), or in which (3) nationalised industries have not, by covert diversification, spread creeping stagflation ever wider.

The long-term Tory aim is to extricate the government from intervention in industry, finance, production, management and labour relations and to encourage a market economy by fiscal and monetary policies and by ensuring equality of employee and employer before the law.

The reaction of Ted Heath’s government to the bankruptcies of the Mersey...
Docks and Harbour board, and of Rolls-Royce, contrasts with that to have been expected had Labour been in office. Labour M.P.s make it clear that they would nationalise both enterprises. The Tories have told the bond holders of Mersey Docks that they must sort out their own affairs. On the other hand, they are allowing the Rolls-Royce receiver to sell the profitable car sector while nationalising the unprofitable aero-sector. For this, the government has been attacked for compromising its principles. The criticism is superficial, because the Rolls aero-sector has world wide contracts in America, Europe and Asia, and with the British Defence Ministry, and the government is merely acting as an emergency caretaker until these vast commitments can be sorted out, and the undertaking put up to auction for bids from entrepreneurs ready to risk capital after assessment of the new situation revealed by Rolls-Royce’s failure. Labour spokesmen say that this creates uncertainty for Rolls’ 50,000 employees. The Tories reply that every time the state steps in with taxpayers’ money to keep alive, by artificial respiration, a firm which cannot maintain itself, the state strikes a blow at the worker, because only production at selling prices for which there is a demand promotes job security and rising wages.

This is goodbye to Butskellism which, be it remembered, originated in the sense of guilt instilled into leaders like Butler, Macmillan and Gaitskell by the memories of the interwar depression when unemployment seemed insoluble. Of today’s thirty nine ministers, only one — Alec Douglas Home — was playing a major role in 1951 the last time that a Tory government launched new policies with such confidence. Then it was the generation whose minds were moulded in the 1930s who were in control.

Today’s policies are being launched as confidently by the generations that came of age after the war. Mr. Wilson alleges that they are out of tune with the electors. Are they? Let us look at some facts.

In the years after the 1966 election, Labour lost control of local governments all over the country, and in parliamentary by-elections the Tories won seats that had always been Labour Strongholds. Now, Harold Wilson is quick to sense opposition inside his party to any of his policies and, if it shows signs of developing seriously, he crosses over to lead the opposition to his policies. His diagnosis of the reasons for Labour’s set-backs since 1966 therefore merits study. He understood working-class resentment of high direct taxes and he tried to reduce public spending; he postponed raising the school age; he denounced compulsory wage-freezes as “monstrously unfair” and proclaimed his faith in a voluntary incomes and prices policy. Recognising the feeling among the public and workers alike that the union hierarchies were abusing their monopoly power, he introduced “In Place of Strife”, his industrial relations bill for trades union reform. By mid-1970, Mr. Wilson had led the opposition to every one of these policies. In 1966, he imposed a statutory wage freeze backed by the harshest squeeze in U.K. economic history, and he scrapped the National Plan with its near-four per cent growth rate. In 1969, when the T.U.C. mobilised its 130 M.P.s to oppose his trade union reform bill, Mr. Wilson said “...the passage of this bill is essential to the continuance of this government in office ...” But finding that, if he persisted, he would continue in office only with the aid of the Tories (who were not opposing the bill), he crossed over to head the T.U.C. opposition and withdrew the bill.

In other words, sensitive to the trend of opinion, Mr. Wilson the politician
reversed Mr. Wilson the Prime Minister and sought to steal Mr. Heath’s opposition clothes; the only exception was his industrial relations bill in which he began by adopting the Heath policy but crossed over to the T.U.C.’s opposition. So that when the election came, Mr. Wilson was, in fact, committed to what might be called “milk-and-water Toryism”, and one reason for his defeat was that the electors evidently sensed that if Tory policies were right, the best people to carry them out were Tories.

A second reason was that to prepare for an election either in June or in October, 1970, Mr. Wilson lifted the restraints on wage demands that had so angered his union supporters and, in effect, allowed the workers to seize the pie in the sky that they could normally have expected in a pre-election budget, so that on budget day, April 14, the Chancellor could, on the one hand, announce the success of his post-devaluation strategy in restoring the balance of payments, but, on the other, could offer no real tax relief, because several million electors had already had their election bonus via wage rises.

Mr. Wilson raised a roar of hollow laughter when he said that the opinion polls had nothing to do with his decision for a June election, which he had taken long before, but respecting his intelligence as I do, I credit him with foreseeing the wage-cost push inflation to come in the autumn, fearing that it would antagonise the voters and taking avoiding action by an early dash to the polls in June.

Before and throughout the election, Mr. Heath warned voters that they were in for heavy inflation from Labour’s policies, and the opinion polls have since suggested that the voters felt that, if there were economic storms ahead, Mr. Heath was better qualified than Mr. Wilson to cope with them.

Victory on June 18, 1970, put Ted Heath in a position of strength second only to that of Winston Churchill in British history. He personally created the Tory committees which since 1964 had been drafting policies, carefully researched down to administrative detail, for less government, more self-help, more selective Welfarism, reduced taxation, reduced expenditure, hiving off accumulated excrescences on the nationalised industries, switching agriculture from the system of subsidies to levies on imports—all of which add up to lower and fewer subsidies and hand-outs and increased prices to consumers of food and welfare. Heath over-rode criticisms that much of this was “electorally dangerous”. On the contrary, he began spelling out to the electors the whole “Tory New Deal” six years ago. No voter can complain that ambiguous promises of largesse deceived him. Ted landed himself at No. 10 when all around were doubting him. He entered owing no man a single political debt. Every Tory M.P. and minister owes his job to him. By contrast, although Harold Wilson towered high as the party wizard in 1966/67, he had to take notice of the views of George Brown, Jim Callaghan, Barbara Castle, Roy Jenkins and last, but far from least, the trade unions.

In opposition, Heath lacked confidence and authority and emerged groggily from sparring matches with Wilson, but as Prime Minister he acts and speaks with authority and as often as not sends the old master to the ropes.

II

The Tory balance sheet, like any other, has both credits and debits. Consider, first, the credits.

That the Labour government was driven to the Right, and that the Tories won on an unequivocal programme of “self-help” reform, implies that (1)
both political parties and (2) the electors agree that Butskellism is outmoded and that direct taxation must be lowered: the unsophisticated because as they rise into the taxpaying brackets they don’t like it, the sophisticated because they realise that Butskellism and high taxes have stifled initiative and enterprise.

The electors do not want the Welfare state to be dismantled, and Mr. Heath is not proposing to do so, but the evidence is ample that most voters consider that the methods of Welfarism no longer apply to present circumstances and that it is bursting with abuses which they want eradicated. It is significant that opinion polls show that those most indignant with Welfare “scroungers” are the workers. At present, for example, those who go on strike get, in effect a generous measure of tax free unemployment pay. The government proposes to stop up this hole. One would have thought that this would be enough to cause the barricades to spring up in every city, but talks with workers up and down the country support a recent opinion poll which showed approval for such measures.

The Institute of Economic Affairs’ new survey, Choice in Welfare, shows that the belief that there is overwhelming approval of the Welfare state is a myth; many would prefer a choice between public and private provision. The survey revealed that 46 per cent wanted the state to continue the Health Service but allow people to contract out and use the money to pay for their own services. In education, 35 per cent wanted to contract out and in pensions 40 per cent. Less than 33 per cent wanted the state to take more taxes to pay for better Health Services which everyone would have. In education, on the other hand, nearly 50 per cent favoured increased taxes for better services, whereas in pensions only 31 per cent. There was a 3 to 1 preference for charges rather than increased income tax to pay for state Welfare. In accordance with the trend, the proportion of people wishing to contract out of the three services had increased since the IEA’s last survey in 1963.  

In Welfare policy, Mr. Heath will streamline—not abolish—the Health, Education and Pensions services. In general, he will make scrounging more difficult; those who can afford services will have to contribute more to their cost. Help will be concentrated on those really in need. The Labour Party’s plans for creeping nationalisation of schools and pension schemes has already been scrapped. State schools and pensions will co-exist with private institutions, encouraging enterprise and choice in both sectors and, again, concentrating on the needy. In university education limits are likely to be set to the system whereby numbers expand at state expense by the automatic admission of everyone with the necessary number of A Levels (which lowers the standards to whatever this swollen number of candidates is able to reach).

III

Consider, now, the debits in the Tory balance sheet.

The Labour government kept up a stream of high drama, as Harold Wilson seized every chance to make historic—or at least histrionic—declarations by TV and Radio. Mr. Wilson too often appeared to think that a political speech, adorned with quotable nuggets, was identical with political action.

Ted Heath goes to the other extreme. In his first seven months as Prime Minister, he was interviewed on television once. He believes that he will be judged by the results of his deeds, not by the sound of his words. His colleagues follow his lead.
The trouble is that the government's goals are all long-term and that its get-on-with-the-job silence leaves the interim field clear to the Opposition.

This would be fine for the Opposition—if it had alternative policies to publicise, but its trouble is that if Harold Wilson criticises Tory policies on incomes, industrial relations, taxation, entry into the European Economic Community, or the economy as a whole, he attacks policies close enough to his own in the recent past to invite devastating quotations from the anthology of his 1964/70 pronouncements.

This means that the Labour leaders are torn between the demands of reality and the demands not of the trade union rank and file, substantial numbers of whom favour Heath's industrial relations reforms, but of the extremists in the trade union hierarchy, the biggest single element in block votes and in cash support of the Labour Party. At the time of writing, it is not yet clear whether Mr. Wilson will follow his intellect or his instincts. My analysis above suggests that the mass of the nation accepts (what it voted for) the Tory programme, but masses are acquiescent, while vocal rabble-rousing individuals will, if encouraged, always emerge to subvert and to destroy. If Mr. Wilson encourages the handful of disruptive militants among trade union officials and M.P.s, the debate could be transferred from the House of Commons to the factories, via political strikes, with incalculable social and economic damage. Mr. Wilson's intellect should warn him that in Labour's own interest, as the future alternative government, he should seek to keep the battle out of the workshops and streets and confine it to exchanges in Parliament and the hustings. David Wood, The Times political correspondent, summed the situation up when he wrote “In their own interests, of course, Mr. Wilson and Labour leaders will want to control the struggle within safe political channels, but it is not certain that they or union leaders have the will, or enough authority over the most militant workers, to impose restraints.”

During this first year of office, the government is (as David Wood also wrote) “being whipped along on a whirlwind, which the old government's policies—or abandoned policies—had raised.” It is also vulnerable from a phrase which Heath let slip in the election that the Tories would end inflation “at a stroke”. No political opponent could fail to exploit such a gift and, as prices rise and strikes boost wage-costs, Labour joyfully rubs it in. The Tories have a good reply but, so far, they have signalily failed to use the communications media to publicise it, i.e., their election manifesto said that the forces of inflation “could not be reversed overnight”, that Tory policies were not “short-term devices” but “a strategy for the next five years”.

In short, I am not urging that Ted Heath should dramatise day-to-day political tensions, or even inevitable periodical crises, by constant press conferences and TV interviews. But it is one thing to push them to the point, as Harold Wilson did, when they lose their purchasing power like an over-issued currency, another to ignore the necessity for a politician not only to be doing his job but to be thought to be doing it.

The Tory government faces two risks, the first within, the second outside, its control.

The first is that unless all ministers from Ted Heath downwards become much more public relations conscious, and much more available to political commentators and correspondents, they will leave the field to their opponents, who will enjoy the initiative. The Tories should remember that the electors eventually tired of the Wilson documentary film, which was all sound-track
and no film, and that they are likely to be bewildered by the Heath documentary, which, so far, is all film without an explanatory sound-track.

Outside the government's control is whether the Opposition decides to follow the lead of its Left Wing and preach class warfare in the factories. One reason for doing so that I have heard in Labour circles is that class warfare offers an emotional rallying point in which the mutually suspicious intellectuals and horny-handed sons of toil could, in the absence of a thought-out alternative policy of government, feel joyfully united. This, I submit, would be the way to divide the nation which, as the facts imply, is not divided today. Can the leaders of the Labour party realise that if they were successful in defeating the Tories by class warfare tactics, they would, in victory, find that they had created an ungovernable country, or at least a country ungovernable by democratic parliamentary methods?

IV

The basic challenge to Ted Heath's government is inflation—not a U.K. monopoly but a world scourge, which up to now has taken the place of inter-war unemployment as the "insoluble" problem.

The reason why inflation is "insoluble" is a gap not in economic but in political understanding. Inflation originates in the failure of governments to (1) enforce thorough-going competition, (2) limit the increase in the supply of money to the real increase in goods and services. Politicians shrink from (1) because pressure groups of employers and workers seek to maintain the status quo by tariffs and all subsidies which keep up, or more often increase prices. They shy away from (2) because they fear that their rivals will outbid them in tariffs, subsidies, and electoral largesse. Make no mistake: a government enforcing fiscal and monetary discipline from purely economic motives would, allowing for a reasonable growth rate, experience either stable prices or a gentle and tolerable rising trend. Inflation occurs in markets distorted by decisions taken for political reasons. Some people say that inflation doesn't matter, but all history shows that it creates social conflicts by re-distributing purchasing power in response not to real earnings arising from honest individual effort but from chance, to the benefit of profiteers, spivs and black marketeers. Lenin understood this: to destroy the capitalist system, he said, you must first debauch the currency. Although there is a handful of would-be-crypto but well-known Communists, who want to end capitalism, the overwhelming majority of electors voted Tory precisely because they are fed up with rising prices.

What is remarkable about Ted Heath's government, and should be proclaimed from the housetops of every country in the world suffering from inflation, is that he realises that inflation results from political decisions and his long-term aim is to introduce policies which leave the price level to fiscal and monetary control of the market.

The first step is to cut income tax. Over-taxation boosts inflation by making the worker reluctant to increase productivity. If he asks for another 40s a week, he knows that some 12s will go in taxes and another 8s in inflation, so he demands 80s as a precaution and, after (so-called) arbitration he gets an inflationary 60s. A stable currency would combine a rising standard of living with substantially reduced wage demands and keep those that came up within productivity limits.

Reduced taxes create extra demand for scarce goods and services, so the next step is to reduce demand by cutting government expenditure. One im-
important way is to apply "organization and methods" to cut down the numbers of those dependent for their livelihood on the central government, which have reached the fantastic total of over 1,000,000.

Big cuts will come by withdrawing subsidies to industry. The £600 million a year that Labour was pouring out in investment grants is being replaced by depreciation allowances. The January White Paper announced net savings of £300 million in 1971/72 and £1,000 million for 1973/74. This is a beginning. The next step in the disinflation strategy is to abolish the selective employment tax, which imposes 48s a week on all male and 24s on female employees in service industries (on the fallacious principle that only manufacturing increases growth); this will reduce all service prices and should rejoice the hearts of the 5,000,000 visitors from overseas who use British hotels and restaurants every year.

Looming over all, however, is money supply. The Chancellor could allow this to grow at (1) a "passive" rate financing the existing real growth and rate of inflation or (2) at a "neutral" rate financing only the sustainable long-term growth; (2) would be strongly deflationary on output in the early stages and disinflationary on prices thereafter. The Chancellor has opted for a middle way between (1) which is a "Go" policy, and would cause roaring inflation, and (2) which is a "Stop" policy that would cause rising unemployment and bankruptcies.

The trouble is that the Chancellor's policy is long-term and that in the short-term strikes and wage and price rises continue. There are, indeed, signs that public opinion recognises the futility of this and that hostility to irresponsible wage-strikes is rising, but (a) will the unions now moderate their demands and/or (b) can the private sector control them?

My guess is that the national disaster of the Rolls-Royce bankruptcy will have appreciable deflationary effects, because it reminds employers and employees that investment seems risk-taking, making profits and cutting losses, that higher wages can only come from profits, and that the taxpayer has no bottomless pocket out of which to finance losses. It is easy to criticise Rolls-Royce for under estimating costs and signing fixed-price contracts, but it should not be forgotten that the previous government was breathing down their necks, deflecting them from market assessments by offering substantial guarantees from motives of politics and national prestige. In the realistic economic climate which the Tories seek to create, the possibilities are that (1) competition may drive other featherbedded companies into liquidation, and (2) companies in general will now be more realistic in investing in new plant and in increasing their labour force. Jobs will become harder to find and trades unions brought up against the hard fact that they cannot, as Ted Heath told them, "go on indefinitely demanding higher wages without concern for the firm or the industry and without regard to the prices that customers will have to pay."

It is arguable that if Rolls-Royce had been kept alive "in the national interest", the Chancellor would have felt compelled to moderate excessive wage rises by steering away from his present midway course towards a "neutral" monetary policy. This would have been even more painful, although I believe that it would merely have hastened the redeployment of resources and labour that must come sooner or later as the government's policies clear the accumulated Socialist rubble from the market. The long-term result will be a Britain braced up, rejuvenated and competitive.