

Briefing Note

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INDUSTRIAL RECOVERY

Economic Prospects. In recent months, developments in the world economy have been encouraging. Oil prices have been falling and the prospects for worldwide reduction in inflation are much improved. High interest rates, resulting largely from the very high level of the US budget deficit, are, however, proving a problem for many countries.

Surveying prospects for the UK economy in a speech in Birmingham on 27th April 1982, Sir Geoffrey Howe said: "It is not my purpose to paint some improbably optimistic picture of surging economic growth and rapidly falling unemployment. But I do believe, and most outside forecasters believe too, that prospects are now definitely more encouraging".

- * Overall economic growth is expected to be 1½ per cent this year and 2 per cent in the first half of 1983.
- * Firm control over government borrowing, both last year and this year, is contributing to confidence in the markets and exerting downward pressure on interest rates.
- * Most importantly, inflation is falling rapidly, and the outlook for single figure inflation (not achieved this time as it was under Labour in 1979 by temporary wage controls and nationalised industry subsidies) is very encouraging.

The Chief Secretary to the Treasury, Mr. Leon Brittan, recently observed that, "this Conservative Government is set to be the first in thirty years to pass on to its successor a lower average rate of inflation than it inherited" (Knutsford, 23rd April 1982). Falling inflation means more confidence in industry in making investment decisions, more downward pressure on interest rates, and greater international competitiveness.

Prospects in Industry. In his Birmingham speech, Sir Geoffrey pointed out that, "it is firms and individuals, not Government or forecasters, which ultimately determine what happens in the real economy". Indicators of our industrial performance have recently been very encouraging:

- * Average earnings in the economy as a whole are rising at an underlying level of 10¾ per cent per year. This is the lowest rate of increase for four years.
- * According to the CBI, pay settlements in manufacturing this year have averaged about 7 per cent, and more than eight out of ten settlements have been in the 5-10 per cent range.
- * Output per head in manufacturing rose by 10 per cent between 1980 and 1981 to a record level. This large increase is quite contrary to the normal behaviour of productivity in periods of recession.
- * Pay moderation and higher productivity have meant that unit labour costs in manufacturing rose by under 3 per cent in the year to February 1982. This is below the rate of increase in almost all of our principal competitor countries.
- * Exports have held up much better than expected, and in particular engineering export orders are at a record level.
- * Latest surveys suggest some recovery in private sector industrial investment.

* A recent survey of managers and trade union leaders indicated greatly improved confidence in the economic climate and, more significantly, a "strong suggestion" of important long-term changes in management and union attitudes (Times, 26th April, 1982).

* Industrial companies increased their profits by a quarter in the second half of 1981. This is good news for investment and ultimately for jobs.

The 1979-80 Recession. This performance has to be seen in the context of the recent recession, which was probably the most serious for fifty years. Between the end of 1978 and the beginning of 1981, the price of internationally traded oil virtually trebled. The Organisation for Economic Co-operation and Development (OECD) has estimated that the total loss of income suffered by the industrial nations because of the crisis was very considerable; around 5 per cent of GNP in 1980 and nearly 8 per cent in 1981.

Britain has escaped the balance of payments difficulties which other countries have faced, because of oil self-sufficiency. However, as a major trading nation, we have inevitably suffered from the decline in world trade. Indeed, our historically poor competitiveness and low profitability in industry made many firms particularly vulnerable.

Our difficulties were compounded in the early part of the crisis by the failure of wage negotiators to respond quickly enough to the changed economic climate. For example, wages in manufacturing in the third quarter of 1980 were 21 per cent up on the previous year, compared with 9 per cent in the USA, 8 per cent in Japan and 7 per cent in Germany. This led to lost orders, lost output and lost jobs.

Unemployment increased by 15,000 in April, including 11,000 Easter school leavers. The underlying rate of increase, however, continues to decline. In the winter of 1980, unemployment was increasing by 100,000 per month. By the last quarter of 1981, the increase was down to 33,000 per month, and in the first four months of 1982 to 23,000 per month. By contrast, unemployment in many other OECD countries is rising very rapidly.

Wage moderation, increasing company profitability and increasing competitiveness all bode well for our long term employment prospects. The Government's fight against inflation and excessive borrowing is also crucial. As Mr. Brittan has cautioned: "It took years to generate conditions for British stagflation and it will take years to remove them" (ibid.). But an impressive start has been made.

LMR/JLS

Correction

Briefing Note No. 15, 21.4.82 on the Local Elections. The 1982-83 Borough rate figures for Lambeth and Wandsworth were incorrect. For 61.25p, read 69.3p; and for 7.75p read 15.8p. The Lambeth rate is therefore over four times that of Wandsworth.
