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Briefing Note

BEATING INFLATION

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Evidence is growing that the Government's economic policies are now paying off.

* Inflation fell to 7.3 per cent in September, the lowest figure for 10 years. It is expected to be down to 6½ per cent by the end of the year, and lower still by Spring 1983. Last month prices actually fell for the first time in 12 years, and, for the first time in 15 years, they have not risen at all for three successive months. The Government is set to be the first for 25 years to achieve a lower average rate of inflation than its predecessor.

* Raw material prices for manufacturers are falling too. They rose just 3 per cent in the year to August and the CBI's July survey showed the lowest pressure on costs for 15 years.

* The recent half point reduction in bank base rates - which govern all other interest rates - took them into single figures for the first time in 4 years. Interest rates have now fallen 6½ points in the last year, and each point helps company cash flow by £250 - 300 million over a full year. This has been made possible by the Government's success - in the face of worldwide difficulties - in controlling its own borrowing. The PSBR is well within this year's target of £9½ billion. Real interest rates are now on a par with France and Germany, and lower than those in the USA and Japan.

* Productivity is up. Manufacturing output per head has increased 12 per cent since the end of 1980.

* Industry is becoming more competitive. Competitiveness in overseas markets fell by 50 per cent between 1975 and the beginning of 1981, but in the following year it improved 10-15 per cent, largely through higher productivity and pay moderation. There is still a long way to go; Britain's inflation is still higher than in Germany, Japan and the USA, and competitiveness is one third below its 1975 level.

* Profits are recovering. The gross trading profits of industrial and commercial companies rose by about 5 per cent in the second quarter of 1982, and apart from a modest fall earlier this year have now risen throughout 1981 and 1982. Profits in the first half of 1982 for companies not involved in the North Sea were 22 per cent above their level in the same period in 1981.

* Investors are showing their confidence in the Government's policies.. The Stock Market is booming, and the FT Index reached a new record high of 626.1 on October 19th.

* Pay settlements are falling. In the 1981-2 round they averaged around 7 per cent, 2 per cent lower than in the previous year.

Why is inflation so damaging?

Inflation hinders growth and destroys jobs by (a) increasing the cost of living, which leaves people less to spend and so damages industry; (b) forcing up interest rates as investors seek a real return on their money; (c) poisoning industrial relations, as unions struggle to keep up with prices and employers try to contain their costs; (d) pushing up production costs, making our exports less competitive and imports more attractive; (e) heightening social tension by hitting those on fixed incomes, like pensioners and the unemployed.

Isn't inflation preferable to unemployment?

Inflation and unemployment are not alternatives; inflation destroys jobs. Even Mr Foot recognised this when he was in office: "Inflation helps to cause unemployment" (Hansard, 28th October 1975, Col. 1269). Experience bears this out; inflation and unemployment have risen together. Inflation nearly doubled from 2.3 per cent to 4.5 per cent during the 1960s; in the 1970s it averaged 14 per cent a year, and in 1975 under Labour reached an all-time high of 26 per cent. Unemployment did not fall. It rose from a third of a million under the Conservatives between 1951 and 1964, to half a million under Labour in the 1960s; to three quarters of a million between 1970 and 1974; and it doubled under the last Labour Government.

Why not reflate the economy?

Reflation (i.e. pumping into the economy money that we have not got) means inflation. For every £ of extra money demand injected into the economy during the 1970s about 95p went into increased imports and higher prices, andonly 5p into extra output and jobs.

Isn't British industry short of orders?

Britain's problem is not a lack of domestic demand in general; it is a shortage of demand for British goods and services. In the year to mid-1982, for example, total money demand rose by 11 per cent and real demand by 3 per cent - but output rose only 1 per cent. The difference was supplied by imports. Until British industry can supply goods and services competitively, simply pumping extra money into the economy will not help jobs.

What is the Government doing to help business?

Falling inflation and interest rates, achieved by responsible fiscal and monetary policies, are the safest way to expand the economy. The fall in interest rates over the last year is worth about £1.5 billion to British business, and the cut in National Insurance Surcharge made in the last Budget is worth £640 million this year. Cuts in capital taxes, special help for small businesses, trade union reform, privatisation and deregulation will all help British business too.

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