

Extract from a speech by
THE GOVERNOR OF THE BANK OF ENGLAND
at the first annual dinner of the Confederation of British Industry
on 18th May 1966

The formation last year of the Confederation of British Industry marked an outstanding step forward in furthering still more the important progress that has been made year by year by your predecessor organisations in establishing the most efficient machinery to seek solutions to the problems of modern industry in this country . . . That this should be the first annual dinner of your newly constituted Confederation makes this an occasion of no little significance; that I should be invited to speak on this occasion and be given the opportunity to thank you, Mr. President, on behalf of all your many and distinguished guests this evening, I deem a great honour. I know I speak for all of them when I express to you, Mr. President, our very sincere thanks for your cordial hospitality. We will remember this evening for having had the honour to have attended this, your first annual dinner, and so joined with you in marking this milestone in the life of this important Confederation. The fundamental story that forms the theme of what I would like to speak about this evening is a success story.

You gentlemen here this evening represent a wide cross-section of British industry; I, for my part, have spent my life in the world of finance and commerce. Whilst your function as industrialists and my function as a banker are quite different, as far as the tasks that we are respectively called upon to perform, our activities are, of course, completely complementary to each other. For, just as industry is dependent on finance and commerce, so equally are the commercial and financial worlds dependent upon the products of

industry. Only by close collaboration and co-operation can we all, together, make our proper contribution to the prosperity of our country. There are those whom I personally regard as disruptive rather than constructive—the colloquial word is, I believe, abrasive—who seemingly find satisfaction in searching out differences, all too often for the purpose of accusing those who are doing a different job of not doing it as well as they might. In this imperfect world in which we live I see greater advantage in seeking the similarities that exist in pursuit of the common aim, whilst recognising that there may be different contributions to be made in achieving it. This evening, Mr. President, I certainly have no intention of dwelling on either the successes or the shortcomings of British industry on which I am not qualified to judge. I would rather venture to take some of your time to explain what I see as the City's role and the contribution it has made, is making and would like to continue to make, to assist industry and, in other ways, strengthen the national economy.

When I talk of the City I do not refer exclusively to the famous 'Square Mile', where it is true many of the financial and commercial enterprises are congregated. I would rather include in this generic term the various financial markets, be they located in London or elsewhere in the country, the banks, the merchant banks, the stock exchanges, insurance, shipping, commodity markets, investment and unit trusts and, indeed, the whole gamut of financial and commercial services which exist in this country. The common link lies basically, I believe, in the word 'services'. None the less,

the services that the City supplies to British industry are so manifold and diverse, and indeed so vital to British industry that I make no apology to this audience for very briefly pointing out the advantages that British industry enjoys from the existence of the City in the sense that I use that word—advantages which industry in many other countries would give much to see emulated.

Perhaps the logical starting point is the acquisition and continuity of supply of raw materials, as industry is hardly likely to come into being without assurance on this score. As virtually all our raw materials come from overseas the City has long been instrumental in assuring British industry of essential supplies. To start with, past British investment throughout the world has secured us vital sources of supply of all kinds, gold, oil, ores of ferrous and non-ferrous metals, rubber, cotton, wool—to mention but a few items—and of course foodstuffs of all descriptions. British creation and control of the source of supply of one kind and another have over the years, often at the most critical times in our history, played an important part in ensuring that British industry has not gone short of crucial raw materials—a problem that has been a serious limiting factor from time to time to the industry of other countries. But, in addition, the existence and operation of the various commodity markets in Britain, the metal exchange, the wool exchange, the Baltic Exchange and various other commodity markets, have all made available to British industry raw materials, regardless of origin, at the most competitive prices. To the British manufacturer these markets have been here at home, offering the most convenient of access and competitive pricing, mostly with the convenience of using our domestic currency—sterling. So efficiently do all these mechanics work that they tend to be taken for granted. But suffice it to say that if these facilities did not exist in the City as they do, and if British industry had to go abroad to some foreign market or bargain directly with every producer, I venture to suggest that life would be a lot harder.

Securing and acquiring the necessary raw materials might be regarded as the first stage in the manufacturing cycle. But it is the process of manufacture itself which most readily comes to mind as the essential function of industry.

The scale of industrial processes has long been such that more than the proprietor's capital alone is required to finance the construction of a plant, the purchase of machinery and the provision of working capital to finance work in progress. The financial services of the City, in bringing together the savings of the individual, and translating these resources into investment for the financing of industry, are perhaps the best known of all the City's activities.

It is sometimes alleged that the needs of industry are not fully known in the City. All I can say of a constructive character in this connection is that the City does not work behind closed doors and considerable efforts are made to find out the needs of industry. The doors of the commercial banks and the merchant banks are wide open and modesty or temerity should not put off the progressive industrialist, even though he be at present operating on a small scale, from entering the door of his choice and discussing his problems.

The final stage in the industrial process is that of the selling, shipping, insurance and the financing of the finished product. Here again the facilities of the City, at the disposal of British manufacturers, are—and I put it in terms of considerable modesty—as extensive as are to be found anywhere in the world. I recall lunching a few years ago with the President of the Export-Import Bank of the United States of America in Washington. In the course of conversation I remarked that from time to time British exporters regarded with envy the services provided by the Export-Import Bank to American exporters. My friend replied to me that some people did not know when they were lucky, for he was constantly being goaded by American exporters on the grounds that the Export-Import Bank did not give as good a service as the British exporters receive from the E.C.G.D. and the British banking system. My friend and I came to the conclusion that it is a common human frailty always to regard the grass in the next-door field as being greener.

Before going further into the contributions that the City makes to strengthening our national economy, I would deviate for a few minutes here on the subject of exports, not to chide and not even to exhort, but to take account of certain facts. I made a speech a few weeks ago in which I stated that in only two

years this century had our exports exceeded our imports. It seems that my homework was incomplete, although it was sufficient to make my point, for within a day or two of my speech an authoritative study on this subject was published which claimed that exports had only exceeded imports twice since 1822. That this should be the situation shows how immensely deep-rooted and fundamental are the problems to be faced in reversing this situation; I think it is fair to say that, with the exception of certain industries, which almost from their inception were designed to meet particular export markets, and certain industries which in the post-war years have risen patriotically, although not always particularly profitably, to the exhortations of Government with in some cases remarkable achievements to their credit, the generality of British industry has for long based its exports on selling abroad what it has not sold at home. Who has not heard the story of the merchant in India in the last century who tried to persuade English pottery makers that Indian eggs were not of the same diameter as English eggs and therefore eggcups for the Indian market needed to be smaller. He was quite unable to persuade the English manufacturer to meet his requirements and found it easier to persuade his customers that it was an old English ritual at the breakfast table to indulge in a pastime—which I can only describe as chasing a marble round a slop-bowl with a teaspoon. As our pottery industry today is a very major exporter—although they still do not meet the export demand for their products—I hope I can tell this story without giving offence. Stories of late delivery too are scarcely new. I recall reading of an occasion in the middle of the last century when a City merchant bank found it necessary to purchase a steelworks in the Midlands in order to ensure delivery in time of the rails that were required for the building of one of the major railroads in the United States which was being financed by the merchant banker, because the demand for rails in this country was at that time so high. I would like to think that all this has changed, but the fact remains that exports have not grown sufficiently and you gentlemen who manufacture exports are far better qualified than I to explain the reason. In saying this, I do not overlook the very creditable fact that

the last fifteen to twenty years have seen the fastest growth of British exports for generations. The trouble is that fast was not fast enough. I venture to suggest that one cause is that successive Governments have not faced up to creating an atmosphere conducive to exports. I venture to suggest that our high protective tariffs on imported manufactured goods have not helped and, although founder members of G.A.T.T., successive Governments of the United Kingdom have elected more to seek reductions by others than by ourselves.

But to return to my main theme this evening of the City and the contribution it makes to the economy, I have attempted to give a brief reminder of some of the services it puts at the disposal of British industry. These various services seemed to many abroad so attractive and efficient and the pound sterling relatively so stable that the various markets and facilities provided by the City were extensively used by foreign customers as well as British industry. The foreign customers buy their requirements through the British markets, pay for them out of balances kept with the British banks, often ship their wares in British ships and cover their insurance with Lloyd's and the British insurance companies. The large balances deposited or invested in London by governments, companies and individuals from the sterling area and many foreign countries have helped to provide us with working funds over and above our own savings, merely in return for paying the London market rate of interest. As a minor digression, as a banker and as a Briton, I am always astonished by those who come and live in our country and talk about the burden of our foreign balances. I can only suppose that unfamiliarity with our accountancy practices leads to regarding items on the liabilities' side of the balance sheet as a burden. Under our conventions naturally deposits with a bank appear on the liabilities' side of the balance sheet. I have yet to meet a banker who is not positively enthusiastic about seeing this sort of liability in his balance sheet increase. Only if he was incompetent to employ such funds to bring in a higher return than the interest he pays, or if he wishes to run his affairs in such a way that may incur lack of confidence on the part of his depositor, does he have cause for apprehension. Such has not been the British way.

Despite the two world wars and the natural growth of competition in other parts of the world, the volume of business carried out by the City for foreign account is enormous and the overseas earnings which found their way into the official statistics in 1965 from such activities and other overseas activities, deriving in the main from London's predominance as an international financial centre, were some £200 million. Although this figure is a large one, it probably understates the true total. These statistics cannot reflect in full the foreign exchange earnings by the professions—law and accountancy, for example, and those who serve them such as printers and the like. The international competition for the type of business carried on in the City is intense and we only keep this business as long as we continue to offer a better service and a more economical service than is provided elsewhere. If we drive this business away, it will not be easily recovered, as past experience has shown. I am sorry to say that business is again today being driven away as a result of our exchange control practices and some of our taxation practices.

Apart from the earnings by services of the City, the largest individual source of foreign exchange income for the nation derives from the overseas investments owned individually and collectively by residents of this country. As a result of skilful management through the years this source of income has consistently grown: over the past decade it has doubled to reach a net total of some £450 million in 1965. Whether these investments form part of the working capital of our markets, as some of them do, or whether they are longer-term investments benefiting from our national acumen in skill of investment management, it is essential—if these assets are to make their full contribution to our balance of payments—that full skill in management be applied to them. But the impost imposed last year on such activity is a serious deterrent to the exercise of skill in management and has impaired the working of this market. What would of course be more serious still would be if, in piping times of peace, British investors—individuals, companies or investment trusts—were induced by taxation or other measures to disinvest—actually to dispose of these foreign assets which bring into this country year after year essential foreign earnings and the possession of which

contributes greatly to British influence in the world. If this were to be the outcome of our policies, then mark my words gentlemen, the future greatness of Britain will be threatened—our influence in the world will steadily decline and we will progressively jeopardise our own standard of living—we would become a very small state in Europe.

Recapitulating, the two biggest items which make up what is called the 'invisible balance'—that is, the services performed by the City and the income from overseas investments—have in this decade brought in net amounts varying from a low of some £350 million in 1956 to a high of some £650 million in 1965. Even in the unhappy year of 1964 they brought in sufficient to cover the excess of imports over exports but unfortunately not all else. This is a record in which I think we may take some justifiable pride.

But we still have an important deficit on our overall balance of payments. To simplify the overall picture, we have to pay for a deficit on trade, and an ever-mounting requirement of Government, whose current payments and grants have increased from £172 million in 1956 to £454 million in 1965 and whose capital payments have over and above this been averaging about £100 million per annum in recent years. The only credit item is 'invisibles' which, contrary to their name, are as we have seen extremely tangible, but out of these 'invisibles' provision needs to be made to maintain a sufficient level of private investment overseas, both to expand our exports and to nourish the invisible earnings of the future. However, what we have so far done to balance the payments figures is, for the most part, action of a kind likely, as time goes by, progressively to reduce this main credit item. Whilst in the short term this produces the desired statistical effect, it still remains to be seen how well the other measures that have been taken work through to alter the fundamental situation.

The Chancellor of the Exchequer is striving to close the deficit. The eyes of the international financial world are closely focused on the progress we make this year towards establishing a balance in our dealings with the rest of the world as portrayed in the official statistics of the balance of payments. The importance of achieving this should not be underestimated. The Chancellor, in his budget speech, in

recognition of this made a voluntary appeal to industry to restrain from investment in Australia, South Africa, New Zealand and Eire to help to achieve this national objective. The achievement of this objective is of the greatest national importance and, for this reason, I add my voice in support of this appeal, for I am sufficiently well acquainted with the machinery of Government to realise that any Government finds it impossible, even though so disposed, to adjust their own programmes sufficiently quickly to this sort of situation. But each week that goes by our competitors abroad are joyfully taking advantage of situations which we can see ourselves but are deprived of the opportunity of exploiting. It is sometimes suggested to the City and industry that you cannot invest a deficit; how much less can one indulge in economic aid grants and loans which total considerably more than permitted investment. To deprive industry of the opportunity to expand abroad in order to maintain such a high level of overseas financial patronage is a policy which, in my opinion, can only prove self-defeating. Some of our friends in continental Europe have recently gone out of their way to express to me their regret at the absence of British investment, or participation in investment, in developments which are rapidly progressing in the continental countries. It is difficult to explain that this absence is due to a preference to dispose of our resources, borrowed or not, in a manner which offers us less opportunities of improving our financial position.

Mr. President, we are not alone in facing a balance of payments problem. Practically every country of Western Europe, and even the United States of America, has at one time or another faced similar problems. Practically every country has had the intractable problem of inflation to deal with—very often encouraged, certainly made easier, by allowing the money supply to increase faster than production, to the accompaniment of excessive wage increases and excessive increases in imports. This surely is one of our basic problems—for last year our money supply increased by some 7½% against an increase in the real national product of about 2%. We unfortunately have a system under which Exchequer financing can, and does, lead to the creation of money quasi-

automatically to the extent that the requirements of the Exchequer are not met by genuine savings or taxation. This is the outcome of a financing system perfected in two world wars, when the dangers inherent in the creation of money obviously took second place to other considerations. The utilisation of this system in peacetime clearly calls for the utmost restraint. As newly-created money finds its way into the economy as a whole, it makes it easy for potential demands to find expression and, indeed, it probably swells demands, so that means have to be devised to mop it up, usually in the form of some credit squeeze. As a credit squeeze undoubtedly causes wide disruption in industry, commerce and financial affairs, and as the demand which has to be held back would not have been there in such force had it not been for the circulation of the new money, it has always seemed to me that our difficulties would be greatly eased if restraint were to be placed on the creation of new money at its source. I believe that only by restraint in the creation of new money at its source will we get away from the spurious illusion of growth and regain less facile but more sustained prosperity which I suspect is what so many people would prefer.

Mr. President, what I set out to tell you this evening is a success story. At this time, when it is popular to go in for self-denigration, I am proud to be able to stand here this evening and proclaim success. The contribution that the City, in its generic sense, has been making and, despite considerable restriction on its activities, is continuing to make to the economic strength of the nation is something of which we can be proud. But I must solemnly warn that increasing restriction is leading to smaller overseas earnings from this time-proven source and, although I know that such restrictions are not lightly imposed, they do, each one of them, reflect failure in solving the fundamental causes of our deficit with the rest of the world. I would repeat the quotation that I quoted in a speech once before of one of my ancestors, who was not unsuccessful in the contribution he made to the financial strength of this country.

“A restriction or regulation may doubtless answer the particular purpose for which it is imposed. But as commerce is not a simple thing but a thing of a thousand relations what may be a profit in particular may be ruinous in general.”*

* Advice said to have been proffered by Sir Francis Baring to Lord North's Ministry.

I would suggest this thought be borne in mind, when new theories are put to the test.

Finally, Mr. President, I recall that in my Army days at the Staff College we were taught two things, which I think are apposite to the points I have been trying to make this evening. One was the dire effects, in an assault landing, of landing dental chairs before ammunition, and you must forgive me if this comes to mind when I see grants in aid taking precedence over investment. Second, we were taught to

exploit success—that this led to victory. This maxim we are not following at the present time—we are restricting those very activities which contribute so much to our economic strength. Given the necessary freedom I have no doubt at all that the City could further strengthen the international financial position of this country. I hope that in the formulation of policy for the future this is recognised. We, in this country, enjoy advantages which are unique and have integrity and experience second to none. Let us exploit our successes.