

Speech by the Governor of the Bank of England

Given at the dinner of the British Export Houses Association at the Mansion House on 5th June 1967

It is less than a year since the Government announced a number of related measures to strengthen the economy. Although we have by no means solved all our problems, there has since last July been a marked improvement in our situation. A welcome feature of this improvement has been the transformation in our balance of payments, to which the growth in exports has already contributed greatly. But we need this improvement to continue and to grow. For the time being, the success of our efforts to date is being obscured by a variety of troubles overseas but, if we persist in virtue, the results must shine through even this darkening scene. We all hope that, at least, the more ominous political clouds will disperse. If they do, and if the expected upturn in the American and German economies takes place, I see no reason why the rise in world trade, and the better opportunities which this brings for us, should be interrupted.

The export houses are playing a valuable part in our recovery and I welcome this opportunity to acknowledge their contribution. But let me first say something about one aspect of the national policies concerning the balance of payments, an aspect on which much comment is focused; that is the alleged difficulty of getting a surplus in the balance of payments without giving up growth. This is a field in which judgments, cautiously formed after painstaking examination of the evidence, will always need to be kept continuously under review and re-examined in the light of fresh experience and growing insight into the workings of the economy. What is important is to ensure that, before policies are decided, the critical propositions are set out as clearly and realistically as possible, so that attention is directed as near as we can humanly get to the real areas of choice that lie before the policy-makers.

It is not at all difficult to present the issue as being a choice between more surplus in the balance of payments, or more growth. I do not believe, however, that it is a bit clear that we are really faced, except in some very ephemeral way, with this simple choice. To talk as if we inescapably are does more to confuse the very difficult issues that really face us than to clarify them.

I am concerned tonight with long-term policies and effects, not with the short-term consequences of emergency action, the so-called 'stop-go' which I would rather describe as 'go-stop'. This, I know, does serious damage to business confidence, arrests cost-cutting improvements in efficiency and organisation, and discourages both management and labour from discarding restrictive practices that do certainly inhibit faster growth.

The question I wish to pose is this: could we, *in the long run*, achieve a higher rate of growth but for the need to achieve a surplus in the balance of payments? Views are passionately held about the right answer to this question – perhaps just because no-one is able to give an unqualified, definitive answer. But there seem to me to be a few guidelines that should help, and it is about one or two of these that I want to talk.

You will accept, I think, that there must be some broad upper limit to the level of output – the amount and the quality of it – that the economy, including all the resources of management, labour and capital, is currently capable of producing. It is not

to be described with some precise figure, for what we can produce must depend very much indeed on the efficiency of the effort we make with the resources we have, as well as on what it is we are trying to produce. Yet admitting the limit is a range rather than a single point, it must be true that as the availability of natural resources and the amount of productive capital equipment increases and its quality improves, and as the size and skill of the labour force and of management grow, that upper limit of output must itself rise. The rate at which this absolute maximum of output is rising obviously sets a maximum to the growth in actual output.

How near in practice can we get to this theoretical maximum of present output and future growth? A plausible case can be made for expecting that a higher pressure of demand will not only ensure that existing resources are fully used in the short term, but also a faster rate of growth in those resources in the long run. If that were true, then it could also be said that we were holding back demand only to secure a balance of payments surplus, and without that constraint we could have a higher rate of growth. But is it true?

Experience so far seems to be teaching us that in the longer run that policy is self-defeating if pursued too far. By no means all the factors of production can be expanded quickly to meet the higher pressure of demand; the size and skill of the labour force cannot be expected to grow suddenly, nor the availability of raw materials. On the contrary, bottlenecks and shortages occur, particularly in natural resources of materials and in highly specialised skills and equipment. The quality of investment deteriorates in the less competitive climate because an inefficient firm can make profits and survive without becoming efficient. Some firms tend to postpone needed improvements and re-equipment because of their fear of losing business while production is interrupted. Mobility of resources – redeployment from the less efficient to more efficient and more productive activities – gets obstructed if demand is too high. Labour hoarding, with its inevitable consequence of declining productivity of labour for the country as a whole, brings the level of output below what it could be if expanding and efficient firms were to get hold of the resources they need. In short, the output apparently forgone by maintaining a small margin of spare capacity to sharpen the competitive drive for efficiency, is not really forgone; the possibility of securing that extra output, and sustaining the higher level of capacity utilisation in the longer run, is illusory. This, it seems to me, is one of the hard permanent facts of life, not simply a temporary phenomenon. It is not a conclusion which can sensibly be shrugged off as being reached merely by the exercise of so-called conventional wisdom, whatever that is supposed to mean.

No-one of my generation overlooks the severity of the human and social problems raised if men are without work for any length of time. My hope is that we can see such unemployment as we must have made up more and more of people in the process of changing their jobs. For then, the output apparently forgone by maintaining a small margin of spare capacity is doubly no real loss. On the contrary, the existence of a little elbow room contributes to the growth of productive capacity.

I do not question that we have to walk a tightrope. If we get too close to a recession, enterprise and effort get discouraged and we fail to build up our powers. On the other hand if we press things to the limit in the short run, we create conditions that obstruct

growth as well as bringing ourselves into trouble with our overseas payments. To avoid any misunderstanding, may I say that I see no reason to differ from the Chancellor's view of what our present situation requires in this respect.

My message is that I do not believe it is right to blame the need for a modest amount of spare capacity upon the balance of payments. However, I would be doing my argument a dis-service if I were to leave you with the impression that just to ensure that we do not strain our resources is sufficient to put the economy on the right path. There is plainly much else that needs to be done. The measures which the Government took last July are only the beginning of a long-term strategy. It is one thing to ensure that the resources needed for desirable investment and other important national needs are not pre-empted; it is another to make sure that they are used to meet those needs.

Even if we get the right domestic policies on growth, and manage to achieve something approaching the highest *sustainable* rate of growth we are physically and humanly capable of, we shall still need a strong balance of payments, the more so because we have ahead of us a heavy burden of debt repayment. Exports must continue to rise. Much is heard about the steady fall in our share of world trade since the early 1950's, in spite of the fact that part of this was probably inevitable. We started with a very large share and were therefore vulnerable to the recovery of other industrial countries from the effects of the war; many Commonwealth countries have achieved independence in this period and have naturally wished to diversify their trade; and we have gained little – so far at least – of the particularly rapid increase in trade between member countries since the formation of the European Common Market. Talk about losing our share of world trade tends to make us overlook the marked improvement in our export performance in the context of our own balance of payments and of our economy. Whereas before the war our exports covered no more than two thirds of the cost of imports, last year they covered as much as 97%. This considerable achievement has only been realised because we have managed to raise the proportion of resources we devote to supplying overseas markets. As the President of the Board of Trade has recently pointed out, this country already allocates a larger share of its output to exports than most other industrial countries.

Nevertheless, these developments will have to be carried still further if we are to repay our debts without further strain. World markets will be expanding fast over the next decade, as tariff barriers are lowered, and the developing countries push ahead with their development plans. Competition, however, will be stiff. More and more countries are entering world markets for manufactured goods, and there will be a significant reduction in protection of our home market as a result of the Kennedy Round agreements. I have no illusions about exporting being easy or fun; suffice it that, as we all know, it is vitally necessary. It needs hard work and a continuous effort to improve our organisation for selling abroad. Some export sales no doubt are less profitable than domestic sales; but, though I do not of course accuse you of this oversight, it is sometimes overlooked that the increased volume of sales helps in the long run to offset lower profitability per unit. Moreover, firms with a wide spread of export markets are much less vulnerable to the fluctuations of 'stop-go' – a point that some manufacturers, but not all, have already learned to appreciate.

I am also well aware that exporting can raise all manner of difficulties, particularly for the smaller firms who are unable to maintain permanent overseas representation. Often products which are well received in home markets do not get sold abroad because manufacturers are not aware of relatively minor changes in specification or marketing technique which would make the product attractive in foreign markets. Setting up outlets overseas is an expensive and risky process which small manufacturers are understandably reluctant to undertake on their own. This is undoubtedly the reason why a very large number of firms still do not do any exporting at all. It is also the point at which your members make a real contribution to our prosperity.

I was pleased to learn from your Chairman of the steps taken by your Association recently to reorganise and revitalise itself. I know that this is seen as a sort of 'coming-out' for the Association, as a preliminary to a vigorous new effort to sell your organisation to others in the same important business. I wish your Association a rapid success in establishing itself as a comprehensive body, speaking with the authentic voice of the export houses, fostering their efforts, disseminating information and guidance, and generally playing a truly indispensable part in the promotion of British exports. If you do succeed, we shall all have the greatest cause to be grateful to you.

I have much pleasure in proposing the toast of the British Export Houses; and I am glad to be able to couple with it the name of the President of your Association.