Extract from an address by the Governor of the Bank of England

Given to the Annual Conference of the Building Societies Association at Bournemouth on 22nd May 1969

. . . I do not think that there are many central bank governors who really like making speeches, and there are always plenty of people who think they should not do so. But, despite the confidential nature of much that goes on behind central banking doors, from time to time some public utterance is unavoidable. Carrying the responsibilities we do, the general public is entitled to know something of where we stand on the questions of the day which bear on our work. These questions can cover a wide canvas embracing all aspects of our economic and financial life or they can be restricted to the monetary affairs which are our immediate concern. The wider we range the better some people are pleased and the more others are annoyed. The former yearn to hear a voice they are pleased to regard as authoritative but not political, while the latter resent any outside orchestration of the current political theme. In short, as in so many fields of human endeavour, it is impossible to please all the people all of the time.

Whether many speeches do any good commensurate with the effort put into their preparation and delivery I rather doubt. Maybe some of the immediate audience may take away a few new and useful thoughts. The treatment by the gentlemen of the press varies quite markedly: some are prepared to provide extended space for what the speaker said; the majority, however, do no more than search for the odd sentence which might justify an arresting headline or provide the text for their own sermon. I think it is true to say that as a body they find any smell of conflict irresistible and consequently their nose for it is sometimes more sensitive than a dog's ear for a high-frequency whistle.

Imagined conflict between the Bank and the Treasury exercises a perennial fascination. When detected it tends to be paraded in the harshest terms, calculated to be as wounding as possible to one party or the other, according to taste. I assure you that these cosy little dramas hardly ever have any foundation in fact.

To return to the general subject of speeches and their usefulness, I doubt whether the abrasive speech often does a great deal of good. Politicians, of course, cannot help making such speeches – it is part of the game. The rest of us are moved to make them from time to time. It is the best way of getting a reaction, usually one of indignation, and of making the headlines, but does it alter anything? I wish I could think so. Exhortations to the trade unions or to management to improve themselves or to all of us to work harder fall, I fear, on stony ground. None of us likes being publicly lectured, which on the whole is not the way to win friends and influence people.

There is more point it seems to me in trying to explain, without heat, basic truths to which we must pay heed if we are to cure our troubles and restore our economic self respect.

The heart of the matter is made evident if we look at the ten years since Lord Cobbold spoke to you and the ten years before that. A good measure of our economic performance as a nation is our balance of payments on current account. In the 1950's we averaged an annual surplus of around £100 million, but in the 1960's we have been running an average deficit of around £150 million a year. Quite a small change, given the huge turnover of our international transactions, but crucial to our economic standing. To use what I fear is an overworked quotation from Mr. Micawber "Annual income twenty pounds, annual expenditure nineteen pounds nineteen shillings and sixpence, result happiness. Annual income twenty pounds, annual expenditure twenty pounds and sixpence, result misery."

There have been three main differences in our current account performance in the 60's compared with the 50's – two have been changes for the worse and one for the better. Taking the last first, our private invisible account has brought us in about £150 million a year more in the last ten years than in the previous ten. This improved result has come mainly from the growth of our investment income, despite current restrictions on new investment abroad. In contrast, our visible trade has been about £150 million a year more in deficit in the 1960's than in the 1950's. The second great change for the worse has been the huge increase in government expenditure abroad, mainly on aid to less developed countries and for defence, which has been £250 million a year higher, comparing the two ten year periods again. I am not concerned with the merits of this expenditure but with the effect of its increase on the overseas account as a whole. This has been extremely worrying and I am glad that at last the increase has been checked and is beginning to give place to a modest fall.

At home, the 60's have been in some respects better and in some worse than the 50's. On the brighter side, total output has risen by over 3% per annum, compared with about 2½% per annum in the earlier period. Also, fixed investment has risen more in the last decade, not only, as you will know, investment in housing, but also investment by private and public industry. These are welcome changes, but unfortunately they have gone hand in hand with more private and public spending on goods and services so that these two components of demand have taken a greater share of our total resources in the 60's than in the 50's. Hence the deterioration in our balance of payments. The hard facts are that while in the 50's our imports rose by £8 for every £9 of extra exports, in the 60's our imports rose by £11 for every £9 of extra exports. Many have tried to diagnose the reasons for this crucial change, blaming variously the age of our capital equipment, the deficiencies of our commercial and industrial management, our work practices, our taxation system, the scale of government expenditure and the difficulty we have had in finding our place in the modern world. Other reasons can be added to the list according to taste. In sum there is little doubt that we are suffering from a variety of ailments which no single drug – political, monetary or economic – can cure.

The basic fact for us all to remember is that our future depends on the volume, quality and price of our total output as a nation and how we apportion the claims made upon it. We need to be more united in our concern to produce the biggest and best possible output. Anyone who opts out of this concern is contributing to a less prosperous future for the whole country. United we stand, but divided we fall, sums up our situation all too accurately.

The apportionment of the claims on total output is just as important as achieving maximum sustainable output itself. This is where we have gone badly wrong in recent years. We have not sold enough of our output abroad to keep our external accounts in balance. So far short have we fallen of this necessary aim that we have had to borrow a great deal of other countries' foreign exchange resources to square our external books. The reason why we have fallen short is that we have been consistently consuming ourselves output which ought to have been exported. Home claims on total output consist broadly of private consumption, the largest element; public consumption; capital investment, mainly by industry private or public; and stockbuilding. It is in the first two elements where the trouble lies. They are large, representing at the present time about 65% and 20% of total output respectively; they both have an obstinate tendency to expand at all times and are most difficult to contract, whatever may be the underlying necessities of our economic situation. Given the overriding need to balance our external accounts this means that the other elements of internal demand, and especially industrial investment, on which the future growth of output depends, tend to be unduly squeezed. Our future therefore largely depends on cutting private or public consumption, or both; that is, for the time being accepting, if not a cut in our standard of living, at least a pause in its continuous rise.

Those who are reluctant to accept this somewhat unpalatable but, in my view, inescapable conclusion say that the answer is to expand our output so that all demands on it may be accommodated. This is a positive and creative approach to which one instinctively responds, particularly after the rigours, real or imagined, of prolonged squeezes and restrictions of all kinds. But it is as well to remember what must accompany that greater output. It must be competitive in quality and price. It must be capable of replacing imports and be available to boost our exports sufficiently. Those increased exports must not suffer from delays in delivery, and service must be efficient and quick. We have not so far shown that we are capable of meeting these essential conditions in a period of expansion. Until we do we have no option but to put up with enforced restrictions on internal demand.

Whether one diagnoses our troubles in recent years as arising from an insufficiency of output or from excessive domestic claims on it, the fact remains that we have accumulated large short-term debts in foreign exchange through our repeated failure to balance our external accounts. In the main we have been treated with patience and understanding by other countries and I am sure this will continue, but only if we make real progress in putting our house in order and in repaying our debts. This year should and I believe still can be the year of change. If so, it will not come a moment too soon.

The past twenty years have been a remarkable period, even if we in this country find ourselves at the end of them in some disarray and even though the international monetary system which has served us so well is now in need of repair. Full employment, expanding world trade and rising standards of living are the biggest prizes and we have enjoyed them, even if they have not always been fully earned. But they have not been without their price. In twenty years our money has lost nearly half its value. It is true that prices have risen rather less rapidly in the second ten years than in the first, but this is cold comfort when there is no real sign of the process coming to an end. I do not accept that inflation does not matter so long as the weaker members of society are compensated periodically. A stable currency is extremely important for us all and I hope we shall devote more effort in the future to achieving it. The example of Germany deserves closer attention. There, due to past bitter experience, the fight against inflation is a political asset not a political liability as here and elsewhere. The results speak all too clearly for themselves. The German economy is one of ever-increasing strength and prosperity with a rising real standard of living which we cannot match.

However we are all, even Germany to some extent, caught up in the rising tide of interest rates fostered by inflation in many countries, by structual imbalances between one country and another and by a world-wide shortage of capital. The net result of rising interest rates has been to cast grave doubt on the virtues of fixed interest investment so far as the lender is concerned. Who would have thought twenty years ago that we should ever see yields on British government securities exceeding 9% with potential buyers still wondering whether they might not do better to wait for still better yields. Not since 1694, when the Bank began its life, have higher yields been seen. A large part of the cause lies in the erosion of the value of money, a sinister influence which spreads its bad effects into many aspects of society. The U.S.A. is now belatedly trying to arrest inflation and is finding how difficult this is once the virus takes hold. They, like us, are resorting to a policy of severe monetary restriction. While this goes on there seems little prospect of our being able to do much to reduce our own rates.

This has a message, of course, for the building societies who have so recently been compelled to raise both their borrowing and lending rates to unexampled heights. The results so far have, I gather, not fully come up to expectations though a substantial improvement on recent past performance has been registered. I hope that in the autumn the societies will be able to inaugurate some appropriate means by which they can participate in the Government's new contractual savings scheme. This gives you, it seems to me, an invaluable opportunity to lessen your heavy dependence on what is, in form at least, very short-term money, which is not by any means the best basis for undertaking long-term investment.

More generally, I have read recently of proposals for changing the term and form of your borrowing; for changing the arrangements for the composite rate of tax; for paying interest gross to shareholders and depositors; for having two-tier mortgage loans (with one rate for new and another for existing borrowers); and for overhauling the option mortgage provisions. There are, I know, many other suggestions. While the movement can be as fertile in ideas as this there need be little anxiety about its future.

Although I would not presume to pose as an expert on building society affairs, I would like to offer you some suggestions of my own.

First, I think the societies would be well advised to confine their lending strictly to housing and housing improvement. If they were to enter the field of consumer durables, fitted carpets, etc. I would be bound to take a closer interest in their affairs, particularly, as now during periods of severe credit restraint. At present, virtually all their lending is within the priority categories and I have been able to spare them completely from the ceilings on their business which I have had to apply to the banks and finance houses. If the time should come when private housing needs are more fully satisfied so that the societies have a surplus of loanable funds I believe they would do better to widen the categories of borrower to whom they will lend and the type of property they will finance, rather than widen the service they provide to their existing borrowers.

In the same vein, I suggest that building societies should resist any temptation they might feel – and which Saturday closing of banks might sharpen – to try to launch out further into the banking field. Easy facilities for withdrawal and simple arrangements to transmit money to third parties are no doubt useful adjuncts to the attraction of personal savings; but to offer anything more closely approaching a full banking service, especially in the way of personal lending, would be a move of major significance of which – quite apart from the reactions of the banking community – the monetary authorities could not fail to take account.

If that seems dampening, let me make a more constructive suggestion. In spite of the concentration which has occurred in recent years, there seem to me still to be more building societies in the country than are really justified in terms of the best use of national resources. This will become more evident as we advance into the computer age which some societies have already embraced. I do not in the least mean to decry local effort and initiative or to advocate only three societies altogether, which I believe another student of your affairs has done. But I am in no doubt that the gods of the modern world of business are on the side of the big battalions, and I wonder whether some smaller building societies would not thrive better and more economically as part of larger groupings. They would not necessarily need to merge with large societies, but might perhaps form among themselves associations of a federal nature, sharing the costs – and the benefits – of technological change while retaining a certain degree of autonomy.

Lastly, I have seen some suggestions that recent developments, including notably the contractual savings scheme, may have the effect of drawing you increasingly into the ambit of the official machine. Some people might suppose that my own relationship to that machine would lead me to desire such a result. I should like to assure you that it is not so. Much as I welcome it when your Chairman and his immediate colleagues come to exchange views with me, or to consult me on some particular question, I have no ambition to do more than offer advice. Further, I believe that the long-term health of your Association will best be served by the use of your commercial judgement to run your businesses as you think fit. This is not to suggest that you should pay no regard to the national interest – for I am sure that you will – but merely a hope that you will continue to show a healthy independence of mind in all that you do . . .