

THE BUDGET

All governments, as Sir Geoffrey Howe has recently reminded his colleagues, sometimes find it necessary to 'push out against the frontiers of their pledges', and the present Conservative administration seems intent on setting a new record. The 1981 budget both reflects and adds to the catastrophe which has overtaken the Government's strategy in the last six months. Much of the comment on the budget talks of monetarist insanity and the crazy folly of further deflating an economy which has already experienced the largest fall in manufacturing output this century and in which unemployment has reached 2.5 million and is rising. But what is most remarkable about the budget is that the Government should find it necessary at all to deflate at this stage in the implementation of its strategy. For the monetarists themselves the budget is the consequence of the failure to create the conditions for a genuine monetarist experiment. Every self-respecting monetarist is busy disassociating himself from this Government and its practice over the last two years. The original intention was that by this budget inflation and interest rates would be declining rapidly, productivity would have risen substantially, and the Government would be in a position to cut taxes and release the springs of enterprise and accumulation without risking a revival of inflation. The possibility disappeared because of a series of blunders, miscalculations, and political defeats.

The real ineptitude of the Conservatives has been their handling of the recession. Certainly from the outset they took credit for the recession and it is sometimes argued that they deliberately deepened it in order to break the bargaining power of organised labour. But this gives far too small a role to incompetence, muddle, and accident. It is more likely that the Cabinet was caught off balance by the consequences of some of their early decisions, particularly the decisions to cut the basic rate of income tax in the 1979 budget, to index army and police pay, and to honour Clegg settlements.

If taxes had been raised in the first budget, and a pay limit or a pay norm declared in the public sector, then the need to raise interest rates in the autumn to 17% would have been avoided, as well as part of the appreciation of the pound. As it was, a strong pound and high interest rates, when combined with an uncompetitive and unprotected industrial sector, made the recession much more severe than in other countries. Because the recession was deeper than intended it helped make it impossible for the Government to realise its financial targets. In 1980 both the PSBR



(public sector borrowing requirement) and sterling M3 overshot dramatically. By the end of last year Government policy was a shambles. The one thing the Government had originally declared was within its power to control was proving uncontrollable. As a result of a series of defeats in Cabinet the Government had failed to cut public spending on the scale required for its strategy and had also reversed its position on supporting unprofitable nationalised industries. By the 1981 budget the Government was faced either with accepting the logic of its recent decisions and returning to Keynesian and tripartite techniques for managing the economy, or with imposing very large increases in taxation (some £6 billion) in order to keep at least the medium term financial strategy which had been unveiled only a year previously on the rails.

What has happened in the last two years is that the wider social market strategy of which certain Conservatives dreamed in opposition has been steadily narrowed to a monetarist policy which is hard to distinguish from the traditional deflationary policy so long favoured by the Treasury. The problem is that by itself a deflationary policy undertaken to preserve certain levels of the PSBR and M3 is guaranteed no greater success in reviving prosperity than was that undertaken by most postwar chancellors in the equally sacred cause of correcting deficits on the balance of payments.

A monetarist financial strategy had to be accompanied by measures to improve the conditions for a social market economy if it was fully to succeed. Such measures would have included a radical reform of the tax

system, ending most forms of reliefs and allowances against tax, withdrawing all subsidies to state and private industry, and above all a readiness to confront and defeat trade union power.

Whilst there was widespread support for monetarist policies when they were combined with cuts in public spending, intervention, and taxes, there is only widespread derision for a government pledged to cut taxes but forced to raise them, and doing so by funking the need to raise the standard rate, resorting instead to the dishonest and regressive device of not indexing allowances and thresholds. The *Daily Express* called it a good budget for a monk with a mortgage — but for no-one else. The headlines speak for themselves: *Howe it Hurts (Sun)*; *That's Some Squeeze (Daily Express)*; *Howe The Hit Man (Daily Mail)*; *If You Smoke, Drink or Drive, UP YOURS from the Chancellor (Daily Mirror)*; *Howe Savages Consumers (Daily Telegraph)*.

The political problem for the Government is that not only does it have to start the monetarist strategy again from scratch but it has now united against it an important section of the Cabinet, large numbers of Conservative backbenchers, the opposition parties, the CBI, the TUC, and increasing sections of the media. Thatcher is increasingly isolated within her own Cabinet, something not helped by her strange reluctance to promote those hardliners like Nigel Lawson who do actually believe in the strategy. The consequence must be that the Government will come under enormous pressure to reflate in the autumn when unemployment will have reached almost three million, and when living standards of those in work will be sharply falling (for the first time in this Parliament), and the Conservatives will be facing electoral catastrophe. If the reflation cannot be sanctioned by Thatcher and Howe, it will very likely be sanctioned without them.

But how can a small group of Ministers in a divided Cabinet and a divided party and facing strong opposition from industry continue doggedly with a strategy of entirely ignoring demand, and concentrating single-mindedly on creating financial stability? The Keynesian consensus on economic management is still far from destroyed as the reaction to this budget showed. But it has been greatly undermined, as can be observed by reflecting on the practically unanimous support for reflation under the Heath Government when unemployment edged dangerously near one million. It is significant that today, despite the plight of the economy, the *Financial Times*, the *Times*, and the *Daily*

Telegraph, all continue to support the monetarist strategy, though with varying degrees of enthusiasm. It is remarkable by contrast what deep roots Keynesianism has sunk on the Left and how so many on the Left still believe that the problem of restoring conditions for capital accumulation can be relatively painless. The strength of monetarism and the social market strategy was always that it grasped that final demand was far less important than improving the basic conditions for creating profits. These lie in the labour process. But the strategy therefore always required far more than deflationary budgets if it was to stand any chance of success, and the series of reverses the Government has suffered since the autumn, culminating in the climbdown over the miners, has destroyed the political coherence and attractiveness of the strategy. This budget is the last chance for the strategy. The intention is that the next two budgets, aided by a strongly expanding economy and rapidly rising oil revenues, will allow big cuts in taxes and make the next election winnable. But the economic recovery will have to be miraculous if this Government and this leadership is now to win through.