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LETTER TO THE PRIME MINISTER

The Rt. Hon. Mrs Thatcher,
The Prime Minister,
10 Downing Street,
London S.W.1.

8th August 1985

Dear Prime Minister,

Since 1943 when the ERC was founded, its members have examined the economic policies of successive governments and we have applauded and criticised where it was felt appropriate. When your Government took office, we had every confidence that your Ministers had grasped the basic economic principle; that money in circulation (in the broadest sense) must approximate goods and services available and that if the Government ran a deficit it must be funded by borrowing that did not interfere with this balance. Until the last election we felt your Government was pursuing this principle within the bounds of political practicality.

Since the last election, however, we have viewed the apparent myopic approach by the Chancellor to the entrails of money supply, M3, M0, etc., with growing concern. He appears to have lost sight of the whole and is more concerned with symptoms rather than causes. To change the method of measuring Money Supply because as a statistic it is going in the direction that he does not approve of, seems to be like re-calibrating the thermometer if you don't like the temperature of the patient. The question of why the Money Supply is growing faster than he would like remains unaddressed.

When we read that the Government views the growth in Money Supply with concern, we fail to understand why the cause of this growth is not examined – instead the figures are massaged by, so called "over funding". This method of adjusting the figures in the long run we believe increases the nation's liquidity so the logic of the exercise is in doubt. More importantly the overall effect is to keep interest rates high, to the detriment of industry. It also encourages what used to be called "hot money" to flow, destabilising the exchange rates which causes great difficulty for exporting industry in the international markets.

Over the last five years the industrial base of the country has had to contend with relatively high and unstable exchange rates and high interest rates compared with our competitors. To this burden has been added the recent changes in taxation which will sharply reduce industry's liquidity and make capital investment more difficult and expensive.

If the Government on the one hand wishes industry to take up the slack in the employment market, which is indeed a desirable objective, it cannot on the other hand deprive industry and commerce of finance at an internationally competitive price and a stable currency that facilitates export and trade.

Yours sincerely,

D.P. de Laszlo
Chairman
Economic Research Council

MONETARY POLICY
Questions in the House of Lords

An interesting exchange of views took place in the House of Lords on Tuesday 23rd July 1985. On the question of Money Supply, Lord Beswick posed the following Question - "To ask Her Majesty's Government whether, in view of the fact that the money supply has increased by 101.9 per cent in the 5-year period to mid-April and that only 5 per cent is accounted for by the increase of state minted coins and the printing of currency notes, they will now state by whom the remaining 96.9 per cent of money was created and under whose authority."

In reply, the Earl of Gowrie said-
"the additional 96.9 per cent represents new bank deposits, created in the normal course of banking business. No Government Authority is necessary for this."

Lord Beswick replied -
"I thank the noble Earl for that reply, the implication of which are of course very far reaching. Would the noble Earl not agree that at one time it was clearly understood and firmly enforced that the only authority in the country which was empowered to create money, either by printing notes or minting coins, was the Government of the day, the state? Now that credit transactions have largely superseded minted money and paper currency, is there not some reason for asking for an authoratative and objective commission to consider this matter and to see who is getting the benefit of this enormous amount of extra money that is being created each year?"

The Earl of Gowrie replied -
"The noble Lord makes an interesting suggestion, though, as he has said, for Question Time it is perhaps a little far-reaching in its implications. It seems to me that on the whole the economies of the Western World are benefiting from these new monetary habits.

Lord Tranmire followed with a supplementary question –
"are not the figures for the increase in bank credit and money supply disturbing when compared with the annual increase in output of 3 per cent? Will my noble friend have a look at this as suggested by the noble Lord, Lord Beswick, and have an enquiry made into how money and credit come into circulation and the consequent burden of the increase in our national debt as a result."

To which the Earl of Gowrie replied -
"the Government keep a very close watch on monetary aggregates, as the House would expect. I agree with my noble friend that there have been some rather eccentric movements in M3 recently, but I am glad to tell my noble friend and the Opposition that MO has been behaving impeccably."

Lord Barnett asked -
"Can the noble Earl tell us what has been happening to M1, M2, M3, PSL1, PSL2, and PSL3, and which of them the Government think is right?"

The Earl of Gowrie replied -
"the Government think that the monetary aggregate indications of the present rates of inflation are broadly right and are a great deal better than the behaviour of any of the monetary aggregates when the noble Lord was Chief Secretary to the Treasury."

Lord Bottomley asked -
"is the noble Lord aware that during the last war Government policy was fully to employ labour and materials to win the war? This was done with a modest increase in inflation. Can the Minister say why the present Government do not follow a similar policy to win the peace?

Finally, Lord Beswick returned to his original Question -
"would the noble Earl be good enough to draw a distinction between the Question which I asked and the one asked by my noble friend on the front bench? I am not querying the amount of money that has been created under these different guises. What I am asking is: who is getting the benefit of it? As things are, it would appear that it is the private banking institutions, and not the Government. In view of the fact that the Government have this enormous problem in public sector borrowing, would it not be right to have this matter more carefully assessed?"

The Earl of Gowrie replied -
"of course I am glad to acquit the noble Lord, Lord Beswick, of low political behaviour. The fact of the matter is that he is sceptical of whether the banking institutions should be the proper sources of supply in this area, and we are less sceptical. As I say, it is a somewhat knotty issue to take up in a question and answer session."

Following this interchange the House of Lords went on to debate the Finance Bill. The following brief extracts are of interest.

The Earl of Gowrie:
"The American headache is deficit financing – running an overdraft. Most American commentators do not believe that the deficit can be sustained, and yet the American boom depends on it, and before long the American boom may start to wobble. The headache of the developing countries is debt. The scale of their debt may imperil the growth rates of our developed world, growth rates on which they, in turn, depend."

Lord Barnett:
"It is right that the consolidators should have their way on capital assets as regards the infrastructure, for two reasons. One reason is that if they do not do so there will be a disastrous decline in the infrastructure in this country. Your Lordships do not have to take my word for it. A pamphlet has recently been issued; it is entitled The British Economic Base 1985 and is by W.A.P. Manser of the Federation of Civil Engineering Contractors....
In his booklet he says:

> "Britain's infrastructure, including railways, roads and sewers, which was deemed ill-cared for five years ago, is now sufficiently unkempt and at risk to give rise to public alarm."

....One is bound to ask why, in the face of this evidence, another intelligent man such as the noble Earl, still insists on such high interest rates? They are startingly high in any context, certainly in international comparison. They are some 6 per cent above those in Germany and Japan, and even the United States, with a huge budget deficit, is some 3 per cent lower. They are higher than when the Government came into office in 1979, and despite all the economic recovery we heard of from the noble Earl, and six years of huge benefit from North Sea Oil, we still have this massively high interest rate.

Why do we have it? The answer, I regret to say, is the cursed money supply. Because of that we have these penal rates to reduce demands for money and credit. But even that does not do the job because penal interest rates, as we have seen, have not choked off demand for money and credit. Instead it has had the perverse effect. High interest rates have attracted huge sums to banks, thus increasing sterling M3, and building societies, thus increasing PSL2 (which is the wider definition), and it just adds to the nonsense because companies then have to borrow more money to pay the higher interest charges.

This situation which has been created by this Government, with all the "great benefits" that we heard about from the noble Earl. But it is even worse than that. The Government could have cut public expenditure substantially more, so helping all of us, but the Government – indeed all of us – have to pay substantially more in net interest charges, and find that that is precisely the biggest and fastest growing area of public expenditure. Net interest charges have grown from 1979-80 figure of £3.4 billion to £9 billion which is the Government's own estimate for 1985-86. That is the crazy situation to which this Government has brought us."

Lord Ezra:.... "my suggestion is that the time has now come for a major review of the thrust of economic policy. We are a country which in the past has achieved greatness on the basis of being the first to industrialise. We have subsequently over the years tended to diminish that great asset, and certainly in the most recent years – and it does not start in 1979; it goes back earlier than than – the size of our manufacturing capacity has progressively diminished.

This is a phenomenon which is true of many other countries. But what is different between Britain and our major competitors is that, whereas the share of manufacturing industry in GNP in most major countries has diminished, in our case the actual manufacturing activity has reduced in absolute terms, and in those other countries it has not. In other words we are seeing a rapid diminution in absolute terms of our manufacturing base. I believe that the time has come when we must address ourselves seriously to that problem.

....we need to be considering very seriously what steps we can take, without leading to inflation, to restimulate our industrial base and to study carefully what other nations are doing in this connection. We need also to take seriously the warnings which are coming from all sides about the state of the infrastructure. The noble Lord , Lord Barnett, referred to one recently published document from the civil engineering contractors which is a very serious document, and I suggest to the noble Earl that this be read seriously by the Government".

THE STATE OF THE NATION

With both Houses of Parliament now in recess until mid-October, it is timely to take a look at the situation which now confronts the country in the economic sphere. Although the outlook seemed to improve in the first part of the year, recent reports suggest that economic recovery is petering out. Present indications, therefore, do not seem to bear out the optimistic view taken by the Chancellor of the Exchequer in a letter sent recently to Conservative M.P.'s.

In the first place, it is clear that there has been excessive growth in bank credit and money supply. This has grown by about 12 per cent, while at the same time output has been growing at about 3 percent. Hardly a recipe for stability in the purchasing power of money! Predictions that the rate of inflation will fall by the end of the year are not universally accepted. The Executive Editor of "The Times" commented on 29th June that "the rate of inflation will not fall to 5 per cent by the end of the year. Indeed it is likely to be closer to the present 7 per cent".

The present levels of unemployment show little signs of improvement, it remains over the 3 million mark. Total output in the second half of 1984 was estimated to have risen by only one per cent. Interest rates, which have such a close bearing on industrial growth are still at unacceptable levels. Total taxation remains too high. At the same time there are resources which are under-used, while there are many urgent jobs to be done in the sphere of housing, roads, hospitals, sewers etc. A recent report, referred to by several Peers in a recent debate says that total spending has fallen below the level at which it stood when the Government took office. This report has been compiled by W.A.P. Manser (a member of the Executive Committee of the Economic Research Council). It states that the Government's efforts "have failed in their management of public finance, and they have failed as stewards of the nation's basic structure."*

* *The British Economic Base 1985 available from the Federation of Civil Engineering Contractors, Cowdray House, 6 Portugal Street, London WC2A 2HH*

Need for Sound Money

There is fairly general acceptance that the present Government is right to put the control of inflation at the top of its priorities. All contracts, agreements, incomes, prices etc. are calculated in terms of money, a fact which underlines the need for sound money. But the question is – how successful have the monetary authorities been in their efforts to stabilise the purchasing power of our monetary unit? Even more important, what price has the community had to pay in the attempts to achieve this objective? Certainly, the level of inflation has been significantly reduced, yet there is something obviously wrong, not with the Government's stated objective of conquering inflation, but with the mechanism by which it seeks to operate.

Committed to a policy of reducing inflation and relying on the free market economy, the question arises - can a free market economy function properly under the present monetary system?

Pledged to fight inflation the government had two choices; they could either reform the monetary system and eliminate the increasingly obvious weaknesses which are at the root of the trouble, or, they could seek to maintain the present system with all its imperfections and hope that by exercise of constant vigilance and ingenuity they would be successful in restraining the banks and keeping the issue of credit-money within reasonable limits. Unfortunately, they choose the second course with the results we can see only too plainly.

Lord Cromer put his finger on the main weakness of the system as long ago as May, 1966. Speaking at a C.B.I. dinner he said "last year our money supply increased by 7½ per cent against an increase in real output of about 2 percent. Unfortunately, we 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."*

Increase in Money Stock

It is here that the present monetary mechanism is most vulnerable. The reply to a recent Question in the House of Lords (10 June) revealed that over the past five years the money stock had increased by 101.9 per cent. Where did this additional money come from? Who created it and under what conditions? There are questions which need an urgent answer if we are to reach a solution to the problem.

Efforts to obtain a satisfactory answer to this question in the House of Lords on 23 July met with the usual stone-walling tactics by the Government spokesman (see report on page 4)

Historically, the issue of all forms of money was the prerogative of the State. Today, while money in the form of notes and coins is created by the Bank of England, the amount being fixed in agreement with the Treasury, this is only a small proportion of total money supply. Interest earned on the securities held by the Bank of England Issue Department against the issue of notes is refunded to the Treasury since the Bank of England is a government agent and profits on its operation are payable to the Treasury.

However, the greater proportion of money in circulation is in the form of credit, created by the banking system as a debt bearing interest. As Lord Cromer showed, when the government require additional funds above its income from taxation and genuine savings, it borrows from the banking system. Under present rules, there is a multiplier effect and the banks can then create additional credit up to three times their holdings of government paper, i.e. Treasury Bills. This is bound to have an inflationary effect. It was dealt with in the last war by replacing Treasury Bills with Treasury Deposit Receipts, which did not enter into the liquidity of the banking system. Inflation was thus kept within bounds. As the system works now when additional money is required to be put into circulation to meet growth in the economy, this will have the effect of stimulating inflation. Moreover, it adds to the National Debt on which interest has to be paid.

For these reasons it is becoming increasingly urgent that the mechanism by which money is created should be thoroughly over-hauled. The growth of the National Debt, under the present sytem is reaching alarming proportions, in the forseeable future interest payments will have grown so large that they will consume the entire GNP. Is this sensible?

If the economy is not only to survive but also to grow in strength we must be prepared to examine whether the present monetary mechanism fulfils our needs and can lead to an expanding and prosperous community.

It is only possible to outline some of the ideas which are current regarding the reforms required. First there must be the recognition that it is goods and services which give money its value in the modern world. The need therefore is to base the issue of money on commodities. By establishing a "commodity currency" we would be basing our money on reality rather than fiction. Professor Hayek has given his blessing to this idea.° Secondly, when the goverment requires additional funds to enable it to promote growth in the economy, it should apply the same rules to the creation of credit as already applies to the issue of notes and coins. Thirdly, as neither governments, banks or private institutions should be trusted with the supremely important responsibility of controlling money supply, this should be placed in the hands of a Currency Commission. As Professor Hayek put it – "Our only hope for stable money is to protect it from politics"°.The proposal for the establishment of a Currency Commission was first put forward by Ricardo in 1824. He envisaged the institution of a Board, independent of Government but responsible to Parliament. Over the years this idea has had the support of many leading economists°°, including Peter Jay. When he was Economics Editor of 'The Times', he advocated "the creation by law of a "Currency Commission". "The Times" said of his proposal "were such a policy to be introduced and followed serious inflation would be literally impossible°°. As a nation, stable money would make us richer than inflation can ever do."

The nation has everything to gain by operating within an economic framework which ensured that the medium of exchange, that is money, should be reasonably stable.

° *Article in the Daily Telegraph (30.8.75.)*
°° *The Case for a Currency Commission, published by Aims 1976*

EEC REFORM — removing the inhibitions
by John Coleman

There is a great deal of talk of reform in Europe at the moment. The Conservative Party has produced a Conservative European Reform Group with over sixty MPs belonging to it and the Foreign Secretary has said that precisely because Britain's membership of the EEC is 'irreversible' the Community must be reformed.

Everyone recognised that the institutions of the EEC are full of anomalies and nonsenses, but that is not the real core of the problem. The formation of an artificial superpower would be fraught with problems.

When Britain joined the EEC she was hit by three powerful blows; (i) an influx of European manufactures which has led to the massive deficit in trade in manufactures with the other EEC countries currently running at between 9 and 10bn annually, (ii) an enormous increase in food prices and - this is a point that has not yet been properly appreciated - (iii) a massive inhibition in Britain's trade in manufactures with the food producing countries outside the EEC.

Britain could have absorbed blows (i) and (ii) provided that the way had been clear for trade with those countries outside the EEC and there had been a loosening of governmental, bureaucratic restrictions by the other EEC countries in such areas as insurance and high technology. Sir Winston Churchill understood the fundamental problem about Britain's relationship with the rest of Europe when he said that if Britain ever had to choose between Europe and the High Seas, she would have to choose the High Seas. He knew that Britain's industrial base could not sustain being geared to Europe only and that is fundamentally what is wrong with Britain's present membership of the EEC.

Abide by the Rules

The other EEC countries, France in particular, have insisted that since Britain joined knowing the rules, she must abide by them. They have a fair point. They have gained a twofold short term advantage up to now; they have been able to sell a good deal of their food surplus to Britain and they have been able to capture a large share of British markets in manufactures; but it must be clear to them that this is a situation that cannot go on for long unless Britain's wealth-creating sector, its industry, can expand in some other direction.

It is now late in the day to deal with a problem that should have been dealt with when Britain joined. Had Britain been allowed to continue its trade with the food producing areas of the Commonwealth and Third World countries, and expand it, its great traditional industries would have remained intact, its people would have remained in work and they would have created sufficient wealth to sustain the trade which the rest of the EEC, including that of the giant British companies who moved their plant and capital onto the Continent, now enjoys. The fact that it is now enjoying that trade is solely because North Sea oil has provided the wealth to go on buying Continental goods. As oil revenues run down this will cease to be the case unless the rest of the EEC is prepared to take steps to enable Britain's wrecked industrial base to be repaired. If this is not done the EEC will be cutting its own throat as well as Britain's, not exactly a good recipe for a healthy community! The steps that have to be taken will certainly mean exempting Britain from many of the provisions of the Common Agricultural Policy.

It always was rather absurd for British Industry to try to capture the Continental markets. They were already well provided by their own manufacturers, and even if Britain had been spectacularly successful in this it actually would have been harmful to Europe and created higher unemployment levels there. Traditional British industries should have turned to the real middle range technology markets of the food producing countries of the world. They had a real need for Britains manufactured products and Britain had a real need for their food and that's what good business is really about.

An Outward Looking Europe

What is now needed in Britain is surely a grand effort – in the spirit of Winston Churchill – by both pro - and anti-Market factions to bring about this great change, this great reform in European Affairs. It would ensure a better, more outward-looking, more outward flowing Europe. It would ensure the continuance of the EEC but in a form that would enable an economically strong Britain to hold her head high in independence within partnership in Europe. Time will sweep away the bureaucratic nonsenses, the headless stamp and the faceless passports, of the small-minded Euro-busibodies who hope to superimpose conformity on the characters of the great nations of Europe. The way will be open for Britain and the rest of Europe the make a significant contribution to removing some of the perils of the North – South rift which many now see as an even greater danger to the future of the world than the present superpower conflict. The food producing countries of the Commonwealth and the Third World are crying out for trade rather than aid so that they can stand on their own feet. With a flow of real trade supplying real needs in real markets, not fancy goods in over-saturated markets, Britain can both contribute to Europe's internal prosperity and enable her to beome once again truly outward looking.

All will be the winners.

FURTHER THOUGHTS ON UNEMPLOYMENT

By J.F. Standish

It is incontestible that prolonged massive unemployment presents the greatest single threat to the national well-being, short of war. Most people enjoy working, i.e. being employed, since in addition to an assured income, work provides a necessary ingredient of self-respect, whereas those denied the opportunity of working are in the main frustrated, feeling that they are not wanted. Those who are in this sense unemployed, not idlers, usually do not know what to do with their enforced leisure and would prefer the constraints of a job which, even itself dull, offers security and often prospects of advancement. To argue otherwise is contaray to both observation and experience. In regions where unemployment is on a seemingly endless large scale, such as the North East, people are certainly not

reconciled to their adverse circumstances. It might be added that prolonged unemployment creates social discontent leading to disorder, on the principle that the devil finds work for idle hands to do. Where continued idleness flourishes "nothing teems", as Shakespeare says, "but hateful docks, rough thistles, kecksies, burs.".

Displacement of men by machines is a subject of great importance in this consideration, but is such that it calls for separate study and appraisal. It is suggested here, however, that some practical and effective steps could be taken to remove barriers to employment and thus providing more genuine job opportunities so that the level of unemployment might be lowered. These might be as follows.

1. Wages. These are too high and continue to increase, having the same cumulative effect as compound interest. Wage controls should be lifted, or else minimum wage agreements progressively reduced, and the Wages Councils abolished.
2. Unemployment benefits. These are such that, in many cases, there is little inducement to work. They should be further reviewed and reduced to make wage-earning worthwhile.
3. Penalties on employers. Present legislation disproportionatley favours employees at the expense of employers – unfair dismissal and redundancy claims heading the list – and this discourages smaller firms from taking on labour which might prove to be an expensive risk. There are infinitely more small firms than large ones. This legislation urgently requires overhaul to establish equilibrium between employer and employee.
4. Overtime. This might be reduced, thereby increasing the opportunity for work by others, if National Insurance Contributions were increased on overtime. By such means, it would be possible to offset part of the cost of maintaining the extra number of employees required, whether working full time or part time.

Youth incentive schemes and similar activities are simply expensive palliatives; what is needed is genuine employment of a constructive and productive nature so that real market forces can operate and not, as largely at present, be frustrated. An economic hothouse generating unreality is bad for the health of a nation; a good draft of fresh air blowing away needless restrictions would show a marked improvement.

THE BANK GUARANTEE INDEMNITY SCHEME

Contributed by Michael Imeson

Raising on-demand bonds for export contracts is such a problem for small to medium-sized companies that it is damaging Britain's export effort, Christopher von Meister, director of Bond Support Advisers Ltd, says he has come across countless cases of exporters forced to give up trying for contracts because they cannot raise the necessary bonds. So, in connection with insurance companies and brokers, he has come up with a solution – the Bank Guarantee Indemnity scheme.

"Mrs Thatcher is telling us that the low pound and rising manufacturing productivity are helping exports," argues von Meister. "But this is all irrelevant if you cannot get bonds."

The main problem with on-demand bonds is that the banks issuing them on behalf of the exporter want to reduce the exporter's credit lines pound for pound by the same amount as the bond. Small companies generally have only small credit facilities which quickly run out.

"If a tender bond is 2 per cent of the contract value," says von Meister, "and the success rate when bidding is one-in-eight, then for every succesful contract an exporter's facility is being debited by 16 per cent of his overall annual tender volume, which is considerable."

Net result: credit lines are soon exhausted, the bank stops issuing bonds, the exporter can no longer bid and sales opportunities are lost. Even if bid bonds are raised and the contract is won, the exporter may then have to raise performance and advance payments bonds and face the same problem all over again.

A way round this is to try to get ECGD (Export Credits Guarantee Department) support. This indemnifies the bank should the bond be "Called", enabling the bank to issue a bond for the exporter without reducing his credit lines. However, this Government help has its limitations which seem to fall hardest on the smaller exporter.

"The Bank Guarantee Indemnity scheme provides a private sector solution to the bonding problem," says von Meister.

Created in March 1983 the scheme is an initiative of major City insurance companies and brokers, with Bond Support Advisers Ltd providing financial and company analysis the underwriters. 'Since we started we have supported more than 600 bonds, and indirectly contracts in excess of £350 million. It has allowed the smaller exporter to bid for contract he might otherwise have been unable to go for," says von Meister.

The scheme works by providing a 100 per cent indemnity to the bank issuing the guarantee (i.e. bond) without affecting the exporter's existing bank facilities. Should the bond be called — for whatever reason — the bank is indemnified by the BGI scheme's underwriters.

The exporter, instead of providing a counter indemnity to the bank, enters into a *recourse agreement* with the underwriters. Within this recourse agreement insurance cover of 90 per cent can be provided against fair and unfair calling of the bond.

But for the smaller exporter the scheme really comes into its own by not setting the same limitations that ECGD does. There is no lower limit to the contract value, the exporter's customer do not have to be in the public sector, ECGD basic cover is not essential, contracts do not have to be on cash or near-cash terms and the scheme can process applications much more quickly.

Von Meister claims that: "Without this new bond support scheme, several hundreds of millions of pounds-worth of UK exports might not have been won."

"ECGD's bond support scheme has been very valuable to exporters since it was started in 1975 and has often been instrumental in gaining both construction and supply contracts for the UK. However, it is still only provided under Section 2 of the Industry ACT (National Interest Cases) and applications are often subject

to delays and fairly stringent recourse assessment.

"Were it not, however, for ECGD the private market would probably not have got off the ground. But now the Bank Guarantee Indemnity scheme has clearly shown it is capable of filling some of the gaps and is proving to be a major help to smaller exporters."

The head of ECGD's bonding section Arthur Elston says: "we welcome the intitative from the Bank Guarantee Indemnity scheme in attempting to plug the gaps in the support side of the market."

For free brochure and more information, contact Christopher von Meister, Bond support Advisers Ltd, Sarasin House, 5-6 St Andrew's Hill, EC4V 5BY, or telephone 01-236 9935.

KEEP NAGGING

Contributed by Commander Christopher Havergal

This article has been inspired by the fact that the extract from the late Sir Arthur Bryant's writings – which appeared on page 12 of the Spring edition of 'Britain and Overseas' – came at a time when the present wave of British unemployment was at or near its peak. Readers will recall that in this extract Sir Arthur added his eminent historian's voice to the voices of the many others, who, over the last hundred years or so, have advocated the setting up of a non-partypolitical Currency Commisssion, charged with the creation and maintenance of interest-free money, to finance the commerce of the State. My article attempts to show that an effective Currency Commission could also provide a cure for present unemployment.

Among Currency-Commission advocates has been our Editor – Edward Holloway – especially in his paper entitled "The Case for a Currency Commission (published by the Council for Aims for Freedom and Enterprise), in which Mr. Peter Jay, as Economics Editor of the Times newspaper is also quoted as a backer of the Currency Commission idea, saying, inter alia, that such a Commission should be responsible for latching the money supply to "the Country's productive potential"; and by so saying even Mr. Jay slipped into the all too familiar semantic thickets which trip and bedevil so much economic thought and discussion. What for example is a "country's productive potential"? How would one measure it? And why should it be "potential" suggesting suspense and latentcy, when, concerned with currency, we need to mean movement and immediacy?

I believe it may be a decade or more since Miss Cairncross as our dinner guest of honour suggested that, when the 'magic' principle for real sound national recovery came to light, it would probably be found to be as simple as 'only what goes up can come down', or words to that effect. I think she was right as I will show.

Stable Purchasing Power

On the basis that this or any other nation's secure prosperity predicates the maintenance of stable purchasing power in its currency, it would appear a quite unavoidable conclusion that the currency must be firmly indexed to some absolute-value commodity, somewhat like gold used to be before the size and speed of modern commerce found it wanting. So what commodity can be expected to do the job?

To answer that question we have to take a quantum leap of thought to perceive that the only constant-value commodity in human affairs is our being, namely or man and woman hours of life; and their 'value' is generated as we bargain some of them in exchange for all those goods and services that we ourselves and our neighbours need and want. Individually of course the market prices for manhours differ. But when a whole national productive spectrum of manhours is considered they can be expected to come to a reasonably constant average.

Since, collectively, we almost all work for our communities, either directly or via employers, we thereby sell our productive man and woman hours per unit of the passage of time (i.e. per hour, per day, or per any other chosen measure), instead of using them for ourselves. If we did not, or were not alive, to do so as a nation, there could be no wealth at all; for wealth and life are dynamic, not static. Static 'wealth' as, for example, in the planet Mars has no value because there is no-one to dig it up and bring it to our doors after marketing and fashioning it into demandable goods.

Here therefore surely is that absolute commodity we are seeking; namely it is the sum of all those manhours of services which are supplied to an Economy per unit of time for the purpose of bringing to our doors the whole host of demandable goods and services, which attract each and every one of us to bargain away quite large fractions of our lives to get. Money must represent and quantify this exchange. And the more freely the exchange flows the richer will be the Economy; and the more demandable a man's or woman's work the richer that individual will be.

So, as was said earlier in this article, I maintain that Miss Cairncross was quite right. The magic rule is the simple one that 'Only that productive energy which is put into an Economy, day by day, can be taken out of that Economy, day by day'. Hence no matter how large the collective M's of money supply may be, day by day, they cannot enlarge the productivity supply, day by day, and the money leaves the 'threshold of exchange' inflated, or only part-filled with manhours.

Perhaps I may be forgiven if for the sake of clarity I repeat* hereunder my mathematical expression of this principle:–

If the letter 'S' is used to symbolise the volume of productive manhours supplied to any Economy per unit of time, and if 'D' symbolises the volume of the productive manhours demanded from that Economy per the same unit of time, and if 'Q' symbolises the proportionality between the two of them, then, by hypothesis:

$$S = QD$$

Since to serve our purpose the rate and volume of the flow of 'D' must be expressed in units of currency, it would be necessary to give the relevant currency unit a MANHOUR STANDARD OF VALUE – by the simple expedient of dividing the sum of the existing nationally employed manhours per day (say) by the existing money supply from all sources, per day. Were we to have access to actual statistics the figure might well prove to be about 0.5 man hours per £ at the present time. If so, it would then be frozen at this figure, and used in the above equation for determining the permissible money supply at any chosen time, which is necessary to maintain the value of 'Q' at one; since when the latter is one the purchasing power of the currency is stable, when less than one the currency is inflating, and when more than one it is deflating.

As might have been expected this theory leads to some corollaries, of which the following two are probably the most significant at the present time:–

Firstly, any unemployment of employable (i.e. demandable) manhours constitutes an entirely unwarrantable national impoverishment.

Secondly, were the existing money supply to be increased as necessary to mop-up the present rate of unemployment, the process would be both wealth-enhancing, and completely non-inflationary (i.e. it would neither add to nor subtract from the present inflation rate – which, of course, arises not so much from mechanistic gremlins as from a mixture of insufficiently controlled commercial and industrial cost-push).

A Pilot Currency Commission

Is there not therefore a very strong case indeed to be made for advocating the setting up of a 'pilot' Currency Commission which would be empowered to create and control a small interest-free fiduciary supplement to the existing money supply, of a size equal to the employable manhour content of the employable unemployed (i.e. after it has been divided by the existing Manhour Standard of the £)?

Were the government to answer yes they could then use the new money for public works like making and mending our economic infrastructure.

See ERC Occasional Papers 28 and 29 of 1974

NEW PRESIDENT OF THE ECONOMIC RESEARCH COUNCIL

Lord Ezra has accepted an invitation to become President of the Economic Research Council in succession to Lord Beeching. He will be giving his inaugural address to members at a dinner to be held in London on 10th October, 1985.

Formerly Sir Derek Ezra, Lord Ezra was made a Life Peer in December 1983. He joined the Marketing Department of the National Coal Board in 1947 and became Chairman, in succession to Lord Robens in 1971. Since retiring from the Coal Board in 1982, he has taken on an impressive list of appointments including Industrial Adviser to Morgan Grenfell & Co., President of the Coal Industry Society, Chairman of the British Iron & Steel Consumers' Council and President of the British Standards Institution.

Members of the Economic Research Council have greatly welcomed Lord Ezra's acceptance of the Presidency of the Council. In a recent speech in the House of Lords he called for "a major review of the thrust of economic policy". He pointed out that "we are seeing a rapid diminution in absolute terms of our manufacturing base." (see page 5)

U.S. National Debt.

A leading monetary scientist testified before National Conference of State Legislatures Sub-committee investigating the Fed. on 8 May 85.

Margaret Thoren, a leading monetary scientist and author of the new booklet Figuring out the Fed, testified today before the National Conference of State Legislature Goverment Operations sub-committe which was set up last year to investigate to Federal Reserve banking system.

Speaking to the sub-committee, which is comprised of ten State legislators, Miss Thoren pointed out that "...it took over 200 years for our national debt to reach $1 trillion -- and it will take only five years for this $1 trillion debt to double to $2 trillion. The Office Management and Budget is projecting a national debt of $2.07 trillion by 1986. The interest paid on the National debt last year came to $133.8 billion -- enough money to pay all of our 535 Congressmen a salary of $61,000 every year for the next 4,121 years.

"The solution to these problems, which are a direct result of the Federal Reserve's debt-money system is the return of the money-creating function to the Treasury under the direction of Congress, as mandated by the Constitution, and with mathematical monitoring. A money system based on debt-free money spent into circulation by the Treasury will lower interest rates, eliminate the deficit, reduce the national debt, lower taxes and increase business activity,"