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THE GOVERNANCE OF LONDON – A PERSONAL VIEW

A talk given by Mr Steven Norris, Director General of the Road Haulage Association, to members of the Economic Research Council on Tuesday 28th April 1998.

I was in the House in 1986 when Margaret determined that Ken Livingstone really had overstepped the mark. With those idiotic banners hoisted over County Hall, policy on Nicaragua and Northern Ireland a plenty, but none on housing in Hackney, it was simply too much: the GLC had become a democratic affront; it had become extraordinarily bloated (something like 17,000 officials employed at the end) and notoriously inefficient and so she put an end to it. We killed off this beast that had, in any event, come to the end of its useful life. It was also Margaret's view that what we did not need to do was simply abolish one layer of bureaucracy in order to insert another in its place.

As a result, we subsequently saw a strengthening of the Borough structure, particularly after the abolition of the ILEA which followed not long after, through greater borough powers and a framework of quangos and joint boards. These were established in order to deal with the simple proposition, that in any great city there are some strategic issues that are clearly not amenable to resolution by an individual borough. The most obvious of those is transport, but there are many others, and I'll say a bit about that in a moment

Nonetheless that was what we were left with in 1986. GLC gone, ILEA gone, empowered boroughs, power retained in the hands of Government Ministers, and, in so far as it was delegated, in the hands of quangos and joint boards.

I suppose from 1986 until about 91/92 that situation persisted without public debate largely because London was actually doing rather well at the time. During that time there was little argument between the parties as to the defects or merits of the system that we had inherited in London, largely because the argument itself was as sterile as the one that had actually accompanied the original abolition. You were either with Thatcher or you were with Livingstone. It was a polarised debate, characterised by a great deal of heat and precious little light. What was however patently obvious was that London did not collapse; that in the wake of the GLC's demise, despite the extraordinary prophecies of doom that we were regularly exposed to during the run up to abolition, London went on to become the cultural-gastronomic-artistic 'capital of the world'. And as it happens also, the City, which contains more international banks than any other city in the world, a City which trades more French stock than all the stock exchanges in France put together, and more German stock than all the stock exchanges in Germany put together was proving more successful than ever.

So London was ostensibly thriving, and if you took that point of view then you clearly saw no merit in changing the status quo. On the other hand you could point to a number of underlying concerns about the way London was being managed and they all concentrated essentially on the lack of strategic direction. To the insider it was clear that all was not well.

The great change in the nature of the debate about London came about at the point at which the Labour Party committed itself to determining not to resurrect the GLC, but to put in place a new proposition: an elected Mayor and Assembly. The second influencing factor was William Hague's election as Leader of the Conservative Party. You might find that rather a surprising assertion but, prior to his arrival, the Tories were locked in opposition to any form of new local government in London. I argued the contrary position (for reasons which I shall come onto in a moment) to no avail within the last Government. It was heartening for me to see that one of the first positive policy statements William Hague actually made was that it was perfectly obvious not only that Londoners wanted this sort of initiative, but that there was ostensible merit in it, and that we as a Party should not be impeding it simply because it might be interpreted as a repudiation of what we had done in 1986. On the contrary, the deficiencies of the GLC were there to be seen. Abolishing the GLC was undoubtedly the right course of action at the time. What we had perhaps not done was to go on to think through the full ramifications of leaving London without anything in its place.

So we arrived at a position in 1997 where Labour had been elected on the basis that they were prepared to entertain this new model for the strategic management of London, and a Conservative opposition that was also prepared to see merit in it. Why did I personally see merit? Well I offer you one distinctive career feature, which is that I think I was the first Minister ever in the British Government to actually have London gazetted into his official title, when John Major made me Minister for Transport in London in 1992. I stayed in the Department so long that I was regarded as a sort of honorary Civil Servant, and stepped down just before the last election. So I had a pretty long stretch in the department During that time I got to know London intimately. I know the Borough leaders; I know the structures; I saw the way the city worked. Obviously my particular concern was the way transport worked in the city. But transport was clearly a template for many other issues. I became convinced that the plethora of joint boards and consultative committees, and indeed the creation of this Minister for Transport in London, working out of the Department of Transport, and having a rather loosely defined relationship with a Minister in the Department of the Environment, (the Secretary of State, who was also informally designated Minister for London,) was not only a complex process which requires a PhD to define, but was not actually operating in the best interests of London. There were three areas where it was quite clear that the structure we had given London had failed.

Three Tasks for the Future

The first is the most obvious: the absence of a 'Voice for London'. I heard people only tonight in the Guildhall asking 'Why do you need to have this new body, even if it is only going to cost £20 million (which in terms of there being eight million Londoners is pretty cheap)? Wouldn't that twenty million be better spent on an inexhaustible list of worthy but currently unfunded projects?' Well, the Voice for London has two sides, both of which impinge directly on London's vitality as the leading World City in Europe.

On the one hand, there's the external voice. There's the extent to which London lacks the ability to put forward something as simple as (and I use that term advisedly) an Olympic bid; a bid to host the World Cup or similar sporting event; a great international cultural event. London currently has less capacity to co-ordinate that sort of bid than many lesser cities in the UK. Much more relevant, it has less capacity to harness the bidding advocacy process within Europe, in terms of grant aid for the Capital that is now an absolutely essential part of the process of funding major civic projects.

London has less organising capacity than Richard Knowles had when he was running Birmingham, or Graham Stringer had until very recently when he was running Manchester, because those two gentlemen had the ability to harness all of the resources within their city. They could effectively co-ordinate all the effort that needed to go into the process. They could call on different departments to put together a comprehensive, first class, understandable bid. We suffered the ignominy in London of having seriously to compete with Manchester to host the Olympic Games. I spent last weekend in Manchester and it's improved enormously, but I've got to tell you that as a venue for the Olympic Games and in comparison to London, there really is no serious debate.

Much more to the point, however, is the internal debate (which is now really at fever pitch in Scotland over the allocation of national resources within the United Kingdom). As you know, there is a very strong body of evidence that London is a substantial net contributor to the National economy. Ken Livingstone would say to you that if London were to receive the level of Government expenditure per capita that Scotland receives then London would receive an additional four billion pounds per annum. So the second use of 'the

Voice' is to talk up London's case to the rest of the United Kingdom. This process of internal bargaining between regions for resources creates real tensions. I was in Scotland the other day and saw an extraordinary performance by Donald Dewar, a man for whom I have an enormous affection and no little respect, in which he castigated one of the potential London candidates for having the temerity to suggest that perhaps it was time for London to stop subsidising Scotland. I saw an equally ferocious attack on the gentle Trevor Phillips – rumoured to be a potential Mayoral candidate – who too had had the temerity to suggest that perhaps this imbalance of resources might need to be addressed. Well, let me tell you, 'the Voice' needs to be there to ensure that despite all of this there is a very clear commitment in Whitehall to giving London the resource which it deserves. London is not simply 'a part of' the United Kingdom. If you look at inward investment decisions made in the North East, or in Wales, in Scotland, or in the North West, they are always (there are no exceptions to this) investment decisions made by teams coming from across the globe who pass through and first encounter Britain in London. London will still be the part of the UK they most look forward to visiting.

The second area is the power to co-ordinate. This is at a level which is so pedestrian (and that's rather an awful pun) that I hesitate to mention it. But let me explain, as an example, how when I was rolling out the London Cycle Way Programme, all the boroughs agreed with me that this was a good idea and all signed up to it. I gave them all some money through the Local Transport Settlement and off they went and delivered a programme entirely at their own pace. What you see now, six years after I began that programme, is that it is still half finished, bits of it finish here, new bits start there, nobody linking it all together. Ironically the money is there, more or less. It's about the co-ordination of that money and making sure that we optimise the value that we can get out of it. That is what we singularly have failed to be able to do in the past.

The third power is the power to initiate. Within the thirty-three boroughs; the Government Office for London; the various quangos; the Parking Committee for London; the London Traffic Director and so on, you see plenty of capacity to react, but no capacity to initiate. Cities are dynamic by definition. They are not locked in a time warp. They present a complex and constantly changing series of problems.

An Elected City Manager

So what we are now offered is an interesting model; one that is largely imported from the United States. It is not the only model that is available, but it is what is known as the 'strong Mayor' model under which you have an elected Mayor, who is directly elected separately from an elected supervisory body – the Assembly – which will consist, in London's case, of 25 members. I think the Government was rather brave to go for the strong Mayor model. It is a model that makes clear from the outset that this person can make mistakes. (If you doubt the capacity of Mayors to make mistakes, think not of Guiliani in New York and his great successes. Think instead of David Dinkins and Ed Koch and New York near bankruptcy and anarchy. The automatic assumption that elected Mayors are good is, I fear, long since disproved.) The reality is that there is, however, the potential within this new, dynamic model, to change the nature of the democratic process in the city.

At the moment, in the kind of pluralist model we are all used to, you elect perhaps sixty/seventy individuals of varying political complexions to represent a rainbow coalition of views. As each issue arises it is then a subject of debate between these various individuals. The view that emerges is allegedly a consensus, and life moves forward. The practical reality we know is a million miles away from that. The practical reality is that the process of local government is grindingly inefficient and slow, and here again we come to a central feature of city management. The current vacancy is not for a Mayor in the sense in which anyone in Britain conventionally understands the word Mayor. We are creating an elected City Manager. The punters don't want a political 'hack'. They want an efficient city manager, and that is precisely where the conventional pluralist model of local government starts to break town. In the United States they have had no qualms about saying 'Let's elect a single individual. We'll invest that individual with considerable power. We'll give that person a mandate. And, frankly, if they don't deliver we are not interested in excuses. We'll simply elect somebody else.' It's tough, if you like, there is no second chance. It's very, very much a live or die model for the individual concerned. But, of course, the tremendous advantage is that after the successful individual has articulated a manifesto that individual takes the manifesto out and delivers it to the best of his ability and is judged on the results. I suspect the judgement may on occasion be brutal, that's democracy. Who said it was ever fair!

What can be Achieved

In London our Mayor will deal with transport and traffic; crime and the police; economic regeneration, and other general powers in relation to the arts and culture; the management of the Fire and Civil Defence Service; and other areas such as co-ordinating strategic planning. If the Mayor actually has the power to co-ordinate; if the Mayor actually can energise; if the Mayor can use the Evening Standard outrageously (which he or she will clearly wish to do); if the Mayor can say to any Cabinet Minister 'Look I have the votes of ostensibly eight million Londoners behind me, probably literally two or three million personal votes – more personal votes than any other politician in Europe bar the President of France – and more than any other city in the world except Tokyo' then they are going to be listened to.

It's clear that there will be no new money. The impression has been created that somehow the Mayor will 'have a budget of £3.3 billion'. Well notionally, yes. But in practice every penny of that £3.3bn is already committed and spent. There are very significant gaps in the infrastructure in London, particularly in relation to the Underground. Something of the order of £7 to £8 billion, which somehow the Mayor will have to find. The Government has, in fact, proposed two new spending powers. It has accepted that the Mayor may wish to introduce private non-residential parking charges and/or access cordon charges in a bid to reduce congestion and generate resources which can then be hypothecated back into the local community. Incidentally, I think you will find that that power will emerge in the White Paper on Transport as generally being available to local authorities, so even that won't be unique to London. With it and with the ability to negotiate within Government for a larger slice of National resources, there is the prospect that the Mayor will be able to deliver a step-change in relation to transport.

Personally, I think the danger is that John Prescott is selling the pass, that he's pre-empting the power of the Mayor to make a real step-change in London Underground by this extraordinary hybrid model that he's introduced in relation to private sector involvement. This is like that old story about a failing world in which the British are the cooks the Swiss are the lovers and the Italians are in charge of the organisation! It is a world in which you put the private sector into managing infrastructure and you leave the trains in the hands of the public sector. It is the daftest model you could possibly imagine for getting the private sector in. I just don't think Mr Prescott realises the private sector not only provides money, but entrepreneurship and initiative as well.

Look at the history of the privatised railway, considering what an appalling mess the private operators inherited. At the time, the Department saw growth in passenger traffic of 2.5% to 3.5% p.a. Coopers & Lybrand produced a study, which said that every train operating company would go bust, because they couldn't conceivably achieve levels of growth of more than 5% p.a. The reality is that on even the best routes prior to privatisation, like the East Coast Main Line, GNER has increased ridership by 8% in the first year. Other operators have increased by 12% and 15%. Despite all the plethora of nonsense that I've heard talked about rail privatisation, the reality is that it has enormously improved the number of passengers that use the service. Of course it takes a decade to get the necessary investment in place, as Mr Branson will no doubt be the first to tell you. But you have to make the first step, and in forswearing the advantage of that, the Government has rather seriously damaged the Mayor's ability to deliver the goods in London.

One last point – the role of the Police is often rather under-valued in the debate on London. The discussion revolves around transport, and very little is said about this rather odd hybrid that we have policing our city. Because, of course, we live with the odd notion that the Home Secretary, generally not even representing a London constituency, is the sole Authority for the Metropolitan Police, and we have within the Metropolitan Police a body that doesn't just administer Police services in London, it also offers a series of National Services, not least in anti-terrorism, diplomatic and civil protection, fingerprinting, and so on. There is far too little attention paid within that model to the real policing needs of Londoners.

I was the PPS to the Home Secretary for nearly two years, and I can tell you that during that time we had two meetings with the London MPs. Each was a run around the table for about an hour, in which they told us what they wanted for policing in London. That, I may tell you, and this is absolutely no exaggeration, passes for democratic accountability for the Metropolitan police as far as back-bench MPs are concerned. Believe me, when a committee of Londoners who are committed to getting the best value out of the Metropolitan Police Service actually have a say in what the priorities for the Metropolitan Commissioner ought to be, you'll see a substantial change in the policing priorities within the capital.

The Issue Today

A huge amount of attention is paid to who the candidates may be. Unfortunately, that is one of the products of the 'strong Mayor model'. I don't think that's the issue right now. The issue is about getting the structure right, then making sure that we draw in the calibre of candidates who are actually capable of making a significant difference. I believe this all represents a tremendous opportunity for London. I hope that Londoners will grasp it on May 7th, and then go forward to make the most of it.

EDUCATION: A PRIVATE OR PUBLIC GOOD?

Some points raised in discussion following a talk by The Rt Hon Dr Sir Rhodes Boyson, to members of the Economic Research Council on Tuesday 17th March 1998.

A full text of the talk and discussion is, unfortunately, not available but amongst the many aspects raised, the following points, given in summary, were made:

On management by the Ministry of Education

There is a widening gap between the schemes laid out by the Ministry and the practice both at school and university level. Schemes for curriculum content, ethical practices and general objectives can be wonderful but are out of touch with the realities of teaching, the needs of students and with later opportunities in the world of work.

On higher education

With the conversion of further education colleges to new universities and a wish to reduce unemployment by retaining young people unwillingly in the education system we have hastened the demise of the apprenticeship system, reduced the standards obtained in universities and in general merely created 'longer' rather than 'higher' education.

On basic education

Early education is failing to provide students who can do basic reading writing and numbers by the age of seven. Many are told that this hardly matters and find themselves falling behind and imagining themselves to be failures from this crucial age onwards. Tests at this stage should be seen not as a burden on children but as a standard below which the teaching system should not fall.

On the school leaving age

Many children are being forced to stay on at school when they have no wish or interest in doing so. The result is indiscipline and frustration. The way forward is to allow children at the age of 14 – a significant moment in psychological maturity – to leave school on two important conditions. These are that they pass a school leaving test, again in reading writing and arithmetic, and that they show written proof that they have a job or apprenticeship offer to go to.

The test should be administered in March of this leaving year. If they fail the test they should have a second opportunity in June. If they fail the second time then both they AND their teachers should remain in school throughout the summer to prepare for a third attempt in September.

Those that remain in school after 14 will therefore be doing so because they wish to. Those that leave should be given five years worth of education vouchers which will be valid for use at ANY time during their lives.

On the National curriculum

In developing this scheme we have not even matched the content of a book entitled "Guide to Teachers" given to every new teacher in the late 1940s which contained chapters on course content, discipline and organisation. Dr Boyson held up his own, now aging copy, some 2" thick which, he supposed, was one of the few remaining in existence.

On the plight of teachers

Something, he pointed out, must be wrong in the teaching profession. Fifty years ago one in five qualified teachers were retired. Today four out of six are retired. Very few stay after the age of 45. Heads of schools are retiring in very large numbers. It is hard to find male teachers in primary schools. Frustration, indiscipline, teacher status and intrusive bureaucracy must be held to account for these problems.

On apprenticeship opportunities

Young people often learn best from a 'master' whom they respect – in a task which involves skill and a prospect of future income. Such used to be widely available here in apprenticeship schemes and is still a common route for young people in such countries as Germany and Japan. There are problems but they must be overcome.

EUROPE'S ECONOMIC DILEMMA

by John Mills

Macmillan 1998. £10 plus postage in paperback form direct from Macmillan Press Ltd, Houndmills, Basingstoke, Hampshire RG21 6XS. Also available in America from St. Martins Press, Inc, Scholarly and Reference Division, 175 Fifth Avenue, New York, N.Y. 10010.

John Mills has quickly followed up his book *Tackling Britain's False Economy*, which contained an analysis of Britain's economic problems, with an equally penetrating study of the state of the European Union's other economies. A third volume is in draft, which deals with the United States' economic problems. The whole trilogy promises to be essential reading for all economists.

The second book of the trilogy is called *Europe's Economic Dilemma* and is published by Macmillan. Like its predecessor it is highly recommended, and as John Mills is now both a member of the Economic Research Council, and is playing an active part in the Council's work, members have no excuse at all for neglecting his books.

I saw the book in draft when it still lacked some statistical tables which it now contains. Although what I originally saw impressed me greatly, the addition of the tables dramatically strengthens the arguments, for John Mills has found ample significant empirical evidence with which to support his challenge to the policies of the economists of the Treasury establishment and their counterparts in other EU countries. By the time one has studied his evidence one is left with the unhappy conclusion that mainstream economists are disciples of Plato not Aristotle, that is they fall in love with theories conceived in the enclosed groves of Academe, and care nothing for the facts of the real world outside those groves. John Mills is an economist by training, but he has the enormous advantage of also being a successful businessman with worldwide experience; he has the practical expertise which enables him to interpret the data accurately, and his mind is focused sharply on the facts which really matter.

The essential theme of the first book was the pivotal role of the exchange rate for the British economy. That theme had been my own concern for forty years, and I totally supported him. In the second book he shows how the same theme has developed in importance for many of the countries of the European Union, even for those whose great post-war success was founded on having the benefit of an undervalued currency. In table 5.1 in the book he sets out the scale of devaluation which is needed relative to the Deutschemark to achieve a three per cent unemployment rate throughout the EU. Only the Luxembourg currency needs no adjustment downwards. He argues that the EU's problems have been exacerbated by the return of the fashion for monetarism. Monetarism has been the dominant concern of governments for most of the twentieth century (and before), and it can be blamed for being at least a major indirect cause of the Second World War.

It is of course well-known that it was the extreme monetarist policies adopted in Germany after the hyper-inflation of 1923 which laid the foundations for the rise of the Nazi Party. Heinrich Brüning, the Chancellor of the Weimar Republic, reacted to the 1929 crash with a policy of severe cuts in expenditure and subsidies. The effects on the farming community in particular were sufficient to cause them to add their support to the Nazis in the election of January 1933 and it may have been their votes which were crucial to the Nazi success. John Mill's statistics show that at the time of the election unemployment in Germany was 33 per cent, a total of 6,000,000. After the election Adolf Hitler was determined to keep his promises to create jobs. According to his biographer, at interviews with candidates for the post of finance minister he asked the question, *'How much can the banks lend me to build autobahns, and to rearm?'* When it was the turn of Hjalmar Schacht to answer he said, *'How much do you want?'* By luck Hitler had found the one man in the world who fully understood the credit creation process. He also knew how to circumvent the stringent laws which were supposed to 'protect' the German currency from debasement. He did not bother to change the law, no doubt because that would have delayed things too much; he just bypassed it.

John Mills details the unemployment record of the major countries during the 1930s. Germany stands out as the great exception, for by 1938 the rate of unemployment was down to two per cent. The expansion in employment was not only in arms and public works, though the arms industry had risen to 9.6 per cent of GDP in 1937, and to 18.1 per cent by 1939. Inflation between 1933 and 1939 totalled only 7 per cent. GNP had risen 65 per cent and consumer expenditure 25 per cent. This compares with a fall in GDP of 25 per cent during the monetarist era of 1929–1932. Britain too abandoned monetarist attitudes in 1932 and in the following five year period the economy grew faster than in any other five year period in its history.

Readers will find the book would have been worth their attention for its description of the historical background alone.

On page 158 John Mills writes:

> *We need to look back no further than the 1930s to see how much damage was done then by mass unemployment in the heart of Europe. Unemployment in Germany peaked at 6m in 1932. It is 4.7m now. In percentage terms it is higher in France and much higher still in Spain. The darker side of humanity is not so far below the*

surface that Europe can afford lightly to take the risk with the possible outcomes of another decade or two during which unemployment rises to completely unacceptable levels.

Those, like me, who remember the horrors of the Second World War are fearful that the economic policies of the EU governments, largely motivated by the need to fulfil the arbitrary convergence requirements of a single currency, are creating the fertile breeding ground for another populist leader from the mould of Adolf Hitler. But let no-one assume that Hitler's economic success is an argument for dictatorship, for John Mills also shows that the other notable dictator, Benito Mussolini, severely damaged the Italian economic growth rate by his insistence on a strong Lira.

John Mills is a Eurosceptic, but not a Europhobe. He knows several European languages and is familiar with many European countries. He shares none of the typical Europhobe's prejudices. His complaint is that the EU has followed economic policies which have hindered growth and that we should not associate with them. Presumably his attitude would change if the EU adopted his constructive ideas, which are set out towards the end of his book, and which include the true way to defeat inflation, that is the encouragement of real investment. His fear that this will not be so is expressed on page 167 by these words:

Perhaps the single worst legacy of a quarter of a century of slow growth in the EU has been the accumulation of power among those least likely to respond positively to the prospect of the kinds of shifts in policy which are most needed.

It was very pleasing to see that he disputes the idea that raising interest rates is a cure for inflation. On page 135 he makes a calculation of the probable effect of a four per cent cut in interest rates. Far from causing inflation, his deduction is that the cut would result in a fall of 1.7 per cent in the Retail Prices Index.

Of course he attacks the ineptitudes of the Common Agricultural Policy, but I know that he is aware that the CAP is a very different animal since the introduction of the McSharry reforms in 1993 even though the implementation of the reformed subsidy arrangements was initially botched with typical incompetence. Europe's agriculture is moving as fast as is wise towards the British model. Any faster reform could precipitate those dark forces of populism again, as in 1932. Nor should one object to the attempt to stabilise agricultural policies which is the fundamental purpose of the CAP, as the effects of a free market are known to be catastrophic. An agricultural free market is stopped from functioning as Adam Smith would have wished by having an influential joker in the pack known as the weather. The CAP originally tried to solve that problem by the system of sales into intervention. But the CAP was not the first known legislation to authorise sales into intervention. That controversial honour belongs to Law 51 of Hammurapi the Great of Assyria, 1760 BC. Agriculture's peculiar economic problem, due to the waywardness of nature, has been around since agriculture itself was invented. A totally free market in agriculture has to be predicated upon a willingness to allow the occasional deaths from famine.

This qualification is the only point I would come near to criticising in John Mills new book. Like its predecessor it is book of major importance, and a totally constructive contribution to the economic debate. Let me not merely recommend but beg or even command everyone to read it as soon as possible.

Geoffrey Gardiner

CARTELS OF THE MIND (AND INDUSTRY)

Cartels of the Mind (Japan's Intellectual Closed Shop) by Ivan P. Hall.
Published by Norton Books, March 1998, price £18,95

Blindside (Why Japan is still on track to overtake the U.S. by the year 2000) by Eamonn Fingleton. Published by Houghton Mifflin, 1995, price £20.00

These two books are worth looking at together for whilst Fingleton concentrates on industrial policy (but passes comment on the Press) Hall concentrates on intellectual activities (and necessarily also includes the Press).

The common theme is the attitudes in Japan towards open competition versus cartelisation. Japanese society, government and business seem to have an almost instinctive proclivity for managed activity, establishing exclusive privilege for those involved at the expense of those who happen to be outside or new – and especially at the expense of the long suffering ordinary Japanese consumer, reader, student, litigant – in fact any and every individual pitting his position against organisations and power of every sort.

Methods vary. Ministry guidance forces firms to comply with cartel requirements through indirect controls over credit provision, the threat of investigations of 'irregularities', the provision of government favours and contracts etc. In schools, universities and the legal profession the requirements for involvement, the control of funding and the strict limits placed on the numbers who can qualify (which can create exam standards in the legal profession which few Japanese, let alone outsiders, can reach) ensure that, in the end, only those Japanese who are both able and lucky can realistically join in. Japanese-only press clubs have exclusive access to news briefings by Ministries and organisations (including commercial firms) to ensure that even information becomes a rationed good.

The acceptance of this situation (compared by Hall to the running of Franco's Spain) is clearly based on Japan's combination of a dominant ruling elite (Samurai turned Bureaucrat) and an intelligent and able, but subservient, mass (Peasants turned Salarimen). Somewhere within this lies a democratic and liberal-minded minority (craftsmen and merchants turned skilled workers, internationalists and artists) whose views seldom win the day.

Thus, the two authors taken together give us a clear and invaluable insight into the question of how Japan is run. Both would argue that Japan's exclusivist, clique-based orderliness is not really based on racism, adherence to an ideology or even the need today to overcome economic problems.

Rather, it has grown historically from the determination of Japan's rulers to avoid colonialisation, to catch up with the 'West', to avoid being looked down upon, to protect a different and unusual culture and ultimately to prove the superiority of that culture.

And for this task the helm must be manned not by politicians (regarded as an embellishment, a concession to foreign ideas, or simply as the public relations arm of the state) but by the best and the most able, the products of the top universities, the graduates mainly of Tokyo university's law school, the key bureaucrats in the ministries. And supreme amongst all of these, the core team of the Ministry of Finance.

The above two paragraphs are Fingleton rather than Hall but Hall lends support for the thesis that this top ministry, through its control of taxation and disbursement, through its ability to have outwitted both the occupation reforms and subsequent internationalisation demands and through its powers of indirect control through looking with approval or displeasure at the actions of Japan's cartels, ultimately 'calls the shots'.

But whilst analysis and perception by these two impressive and respected authors coincide, the conclusions each reach are markedly different. Fingleton argues that, in terms of economic effectiveness (investment, availability of capital, stability, growth, the takeover of profitable worldwide markets etc) Japan has created the idea of the 'good cartel' enabling the country to undertake 'big logic economic supergrowth'. In contrast Hall points to the crushing abuse inherent in intellectual cartels.

Fingleton points to strengths we don't notice (and would see even today's crisis in Japan as but a stage in the strategy) whilst Hall points to weaknesses that we haven't seen before. For Fingleton, Japan is a ship sailing to neo-mercantilist victory under our noses whilst for Hall Japan has a pathos likely to lead to a 'new seclusion' – a new withdrawal from the modern world. They could both be right.

J.B.

VAT THE UNACCEPTABLE FACE OF TAXATION

As a follow-up to ERC Research Study No. 14. 'VAT The unacceptable Face of Taxation' by John Davison, Bill Jamieson, writing in the Sunday Telegraph *commented:*

Concern over tax avoidance was fuelled in 1995–96 by a startling shortfall in VAT receipts of £6bn. John Davison, senior VAT manager at accountants Pannell Kerr Foster, has sent me a disturbing analysis of the subsequent panic by Customs & Excise for yet more complex legislation, even though, in the Excise's words, 'innocents would be hurt'.

A Treasury report into the shortfall found there was no quantitive evidence of avoidance, either among the top 20 VAT payers (accounting for 15 per cent of all VAT paid) or by packaging products to benefit from zero rating.

It found only anecdotal evidence of increasing tax avoidance, though this would include activity by firms faced with ever increasing penalties seeking to improve their tax planning and minimising VAT liability.

What, then, was the cause of the shortfall? The main source of error was found to be inaccurate forecasting, a conclusion dismissed fairly rapidly by the Treasury team but one which, Davison tells me, should come as no surprise to anyone used to VAT revenue forecasts. The last time that the out-turn of VAT exceeded the forecast was in 1988–89. Since then the forecast has always been in excess of the out-turn and the margin of error has ranged from 3 per cent in 1994–95 to 117 per cent in 1995–96.

As much as £2bn of the over-estimate in that year stemmed from changes to the Bad Debt Relief system and the increase in the VAT registration threshold. Further shortfalls of £400m arose from legal challenges to the Excise – that is, the cost to the Treasury of the Excise interpreting the legislation incorrectly.

The best guess the Treasury could offer as to the shortfall due to VAT avoidance was £1bn – a guess based on anecdotal evidence

Even assuming this to be accurate, it is substantially less than the £1.6bn of VAT the Excise estimates could have been lost to it had companies taken advantage of legal avoidance schemes open to them. Such revenue, formerly not due to it, but now collected following tax law changes, the Excise disingenuously describes as ‘protected VAT’.

Obsession with avoidance has caused it to introduce ever more complex legislation and harsher fines. It accepts there will be innocent victims – for example, a recent amendment could lead to VAT being imposed on white sticks and Braille products for blind people and Zimmer frames for the infirm, while property transactions have caught new doctors’ surgeries in a net meant to haul in quite different fish.

More worrying is the drive by the Excise to blame avoidance on an interpretation of tax law contrary to that which, in the Excise’s opinion, was intended by Parliament. The disturbing consequence of this would be ‘purposive’ legislation under which the Excise would effectively be able to have the legislation interpreted in the way it thinks it should. It would be tantamount to a new 11-word Tax Act: ‘VAT is due when Customs & Excise says it is due.’

Davison concludes ‘Before Brown accedes to any such requests he should assure himself that the measures are workable, they will not create unfair burdens, and, most importantly, that they are justified.’

Meanwhile, the chancellor should assure himself that Customs & Excise is more careful in its own budget plans, currently in disarray due to a failure to allow for the cost of a vessel hired last year from the Royal Navy to counter smuggling.

The overlooked cost, estimated at close to £1m, triggered a flurry of telexes to Excise offices throughout the country last December urging cost cuts. Travel, subsistence and training budgets have borne the brunt.

LETTERS

Responses to 'Devolution and Regionalisation: the Outlook for England' by Professor Peter Davison from Dr Bernard Juby and from Mr Fred Hummel (with a reply from the author)

Dear Sir,

I am reliably informed by my Gibraltarian colleagues that, as a formal part of the UK, Gibraltar became a part of the EEC (& subsequently the 'EU') when the UK joined (Prof. Davison, B&O, Spring 1998).

Incidentally, despite being a Member for far longer than the Spanish those from the 'rock' are treated as pariahs by the former when crossing Spanish borders and travelling within the EU. Their passports are not recognised and they are liable to be sent back to their destination or, worse, detained.

Bernard Juby
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Royal Leamington Spa
Warwicks, CV31 lEZ

Dear Editor

I was saddened to find that Euro-mythology has crept into the Spring 1998 issue of Britain and Overseas. In the article by Professor Peter Davison *Devolution and Regionalisation: the outlook for England,* the map on page 20 is said to refer to 'British Isles as Divided into Regions of the European Union by Brussels'. The division of the UK into Regions was, of course, not decided by Brussels but by the British Government whose relevant White Paper *Building Partnerships for Prosperity* was published in December 1997 by the Department of Transport, Environment and the Regions. Why did Professor Davison ignore that White Paper?

Fred Hummel
8 The Ridgeway
Guildford
Surrey, GUI 2DG.

Dear Editor,

Mr Hummel is quite right that the division of England into regions was done by a Conservative Government. The reason I did not mention this was because I did not know at the time I spoke. As you know I learned of this only when I read a letter from Mr Tim McNamara, Head of Regional Relations, European Commission, London, printed in *The Sunday Telegraph* on 26 April. And, as you also know, I contacted you then to ask if I could send this correction for publication in a future issue of *Britain & Overseas.* McNamara also stated that there are nine regions, not eight.

I would have been helped had the European Commission answered my requests for details of regionalisation in greater detail. They sent me a map, pamphlets about *eight* regions, a list of *unelected* representatives, and a brochure, *Funding from the European Union,* which failed to provide the details I gave on pp. 21–2. All that I displayed. The map shows *eight* regions (named in brown caps) and for each I was sent a brochure. I assume that the ninth region is London. When I wrote in January, no details seemed to be available - at least, none were sent me. London is marked on the map in much smaller black letters, with nothing to indicate it is a region, simply that it is, according to the Key, a national capital. As I said at the meeting, the South-East brochure for Regions of the European Union, states that 'As a Europe of strong regions steadily develops, so too will the links between London and much of the South East' (almost suggesting a paucity of existing links – which may not surprise some rail travellers) and that 'A separate brochure on London is in the course of production'; that was in a brochure dated 1996, but when I wrote and telephoned in 1998 no information about a London region seemed to be available. That a British Government so divided up England gives me no joy and I am more surprised that so little publicity has been given to this division than by my (and others') ignorance.

I am very sorry if I misled those who heard me and have read what I have written, but it proved very difficult to get information and it is plain from the need for Mr McNamara to respond to Mr Booker in *The Sunday Telegraph* that even much better-informed observers of the European scene have been – are? – in the dark. I have spoken to many people, in the main intelligent and generally well-informed, and hardly one has heard of either the British or European Governments' regionalisation. My abiding anxiety is, as I hoped I made plain, that such ignorance, coupled with Devolution as planned, stores up trouble for the future that we can all well do without.

Peter Davison
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A response to 'A Miscellany on Money' (Autumn 1997) from Mr T. B. Haran

Sir

In his letter in the Autumn 1997 edition, Mr Lee Cheney repeats and supports some of the false concepts making up unilateral monetary theory and, in particular, the one that banks create money by lending.

The Americans are at a fatal disadvantage in discussing these contentions, because overdrafts are not permitted in the USA and loans are paid into creditor accounts in borrowers' names. Every loan then creates a deposit, which is incorrectly deemed to be money.

Neither a bank in Britain nor one in the USA can alter the basic money supply by such a procedure. The net positions of the banks and the customers are unchanged. The action starts when the borrowers spend the funds and get into debt in terms of both cash and services.

In Britain, payments from borrowers to savers clearly reflect the creation of basic money and those in the opposite direction its *destruction*. Moreover, payments from one overdrawn account to another do not create a deposit.

As a result of the American practice, the relevant deposits are of two types – savers' deposits and borrowers' deposits. A borrower's account is 'overdrawn' when the balance is below the amount of the loan to the extent of the difference. Now, it can be understood that payments from borrowers to savers reflect the creation of basic money and those in the opposite direction its *destruction*. The process is identical in both countries. It is visible in Britain, but not in the USA.

There can no longer be any doubt. Banks do NOT create money by lending; basic money is subject to creation and destruction. What goes round does NOT, (as the Americans say in respect of basic money), come round. Basic money can only be used once; moreover, every transaction alters the constituent parts of the basic money supply. Thus, that supply is automatically self-regulating and there neither is, nor ever can be, a monetary phenomenon.

Apart from petty cash payments, central banks do not use their banknotes as a means of settlement; they simply sell them as purchasing vouchers for general purposes. The true position is that they create service debts on spending and destroy them with earnings. Thus, their experiences are exactly the same as those of any other service debtor and only relate to the service debts side of the basic money supply. They are not, as Mr Cheney contends, able to print their own money in the sense that they can create it unilaterally.

People trade solely in services and as a result become either service creditors or service debtors. This activity takes place outside the banking system and that is where the service credits and service debts are created and destroyed, regardless of whether payment in confirmation is made immediately or subsequently. The banks operate the settlement system, which lags behind the events. As an analogy, trade is the game and bank records are the scoring system.

The service credits can be deposited and lent, but neither of these actions creates or destroys basic money. Banks simply keep records of who owns the credits and to whom they have lent them.

In my letter in the Autumn 1997 edition, I set out an accounting formula showing how, if it were possible, the basic money supply could be calculated. I have since realised that I should have made allowance on the Service Debts side for sums owing to service debtors, but not yet paid. The amended version is as follows:

Service Credits	**£billion**	**Service Debts**			**£billion**
Cash	60	Gross Indebtedness			2,290
Deposits	990	*less*	Cash	40	
Investments	1.020		Deposits	80	
	2,070		Investments	100	220
less Debts	70				2,070
	2.000	*less*	Credits		70
				2,000	

In that letter, I made a mistake in saying, 'As can be checked from the formula, dealings in stocks and shares have no effect on the totals'. This is true of direct investment. In the case of subsequent dealing, no change takes place when the parties are of the same status; where, however, the statuses differ, the investment has to change sides in the formula at its original cost in the opposite direction to the payment. This results in a net increase or a net reduction in the basic money supply.

The economics profession have made a colossal blunder in teaching unilateral monetary theory and have thereby indoctrinated the monetary authorities, the media and their students with false concepts. As a matter of urgency, that teaching should be replaced by the bilateral version and monetarism must be abandoned.

It is disappointing, therefore, to find that Tim Congdon (Winter 1997) still believes that inflation 'is the result of the quantity of money increasing at a faster rate than the trend rate of increase in the quantity of goods and services'.

The quantity of money is the result and reflection of the trading activity in services and cannot be the catalyst of inflation. That catalyst is the continuing practice of raising pay and prices.

Consequently, the rate of inflation is governed by the strength of the workforces in pursuing their 'legitimate aspirations' and the ability of various groups to exploit the public. The trade unions discovered that chasing after a high wage economy resulted in job losses and have moderated their claims and behaviour, but the exploitation has gone unchallenged.

There is no natural rate of unemployment. It is caused by the insistence of the workforces on maintaining too high a pay and price structure. This prices some workers out of their jobs, makes labour too expensive and prevents job-seekers from achieving their objectives. It would, therefore, be a horrendous error to allow the Bundesbank to influence the monetary policies and practices of the European Union.

An article in the Financial Times, 'Deflation; the real enemy' by Professor Robert Reich (January 15) particularly warrants rejection.

He wants policymakers to forget inflation and focus on the danger of falling prices and demand, as he believes they may spiral downwards. This sequence of events he describes as deflation, but it is actually due to another process.

A period of deflation in Britain would, for example, allow pay and prices to fall, savings to gain in value, the purchasing power of the pound to increase and the poor to become better off. The build-up of the purchasing power of savings would encourage spending , full employment would result and, if the process were continued far enough, foreign workers would have to be brought in to deal with the growth of the economy.

Inflation debases the currency; deflation refines it. The former is harmful; the latter is beneficial.

The condition Professor Reich describes is a loss of basic money supply. If funds are borrowed for business activities, which prove unprofitable, or for speculation, which goes wrong, service debts of the borrowers become irredeemable and corresponding service credits are lost. Bankruptcies and liquidations result, which in turn cause a domino effect.

An economy suffering in these ways has to contract until it becomes viable again at a lower level of trading activity and with a poorer standard of living. The fall in pay and prices is actually the remedy and not the fault or the catalyst.

Our recent recession, the Wall Street Crash and the present crises in the Far East are examples of the process in action.

Perhaps now, those newspapers, which fail to provide space for a right of reply to such articles will realise the damage they are doing.

In my aforementioned letter, I condemned the practice of raising interest rates. Now, the Monetary Policy Committee has got itself into the ridiculous situation where growth of the economy is deemed to warrant an interest rate increase, while manufacturing industry needs a cut.

Blanket remedies are, therefore, completely unsuitable and the faults of the economy should be dealt with individually.

A Trading Policy Committee should be set up to replace the Monetary Policy one. Here are some suggestions as to what it could be empowered to do:

Eliminate inflation by banning bank lending for wage increases and speculative purposes; compel groups making profits and raising pay to cut prices; ensure that too much money is not being lent to specific markets; reduce the salary multiples for house loans; take action against the excessive salaries being paid for financial services in support of gambling activities euphemistically described as investment; curb the exploitation of the public by sport, entertainment etc gaining benefits from television; reduce the disparities between shopfloor and boardroom rewards; ban stock options and curb other perquisites; and cancel Peps, Tessas and Isas.

By normally trading at a loss, we have allowed a large part of our means of production to pass into foreign ownership. This has been given the euphemism of inward investment, when economic colonisation would be more appropriate. We need a period in which we enjoy a favourable balance of payments position and may have to cut pay and prices to achieve it.

At present, the benefits of scientific and technological advances are being acquired solely by the workforces and shareholders. The duties of the new committee must, therefore, include ensuring that part of these benefits is passed on to the poor. The ultimate aim must be the introduction of negative income tax, so that everyone has at least an adequate income.

Above all, there must be no turning back to monetarism. It is very easy to fall for the cliche that inflation is caused by too much money chasing too few goods. There is, however, no shortage of goods in our economy and retailers do not operate on the principle that they will push prices up and down in step with the number of customers present. The truth is that using the monetary aggregates for calculating the real (basic) money supply produces nonsensical figures.

In all the centuries of monetary history, this appears to be the first opportunity to get the true situation firmly on record and to have the principles of bilateral monetary theory brought into practice. I, however, am not a young man, so if this opportunity is not taken while it is on offer, it may be further centuries, if ever, before the issues are again correctly brought to light.

Yours faithfully
T B Haran
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