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## Incomes policy after devaluation

Intereconomics

*Suggested Citation:* Abrahamson, George (1968) : Incomes policy after devaluation, Intereconomics, ISSN 0020-5346, Verlag Weltarchiv, Hamburg, Vol. 03, Iss. 3, pp. 70-72,  
<https://doi.org/10.1007/BF02930298>

This Version is available at:

<https://hdl.handle.net/10419/137897>

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# ARTICLES

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## GREAT BRITAIN

### Incomes Policy after Devaluation

by Dr George Abrahamson, London

Some months after the sterling devaluation the British Government, employers and trade unions were still wearily groping towards a new incomes policy or rather to a re-interpretation of the existing policy, for it is often forgotten that the Prices and Incomes Act, first passed in July 1966, is still in force and that wage increases may still be sanctioned only if they meet specified criteria. To recapitulate for the benefit of those who are bewildered by the confusing utterances of interested parties, the "standstill" imposed on all incomes from employment for six months, from July 1966 on, applied to all increases in pay and reductions in working hours except pay increases directly due to increased output, promotion or predetermined increments, or need for higher travel or subsistence allowances. In the following six months of "severe restraint", up to July 1967, higher pay was allowed for the lowest-paid workers or in return for productivity agreements, but not otherwise. In the current 12 months of "moderation", which extend to July 1968, changes in the cost of living and comparisons with incomes in other employment are still ruled out as justification for pay rises. Higher productivity and exceptionally low wages are the only admitted criteria for pay increases.

#### **Pragmatic Incomes Policy**

Unfortunately, in practice they are not. Reluctant to invoke the Prices and Incomes Acts, the Government has tried to win over workers and employers by a mixture of exhortation and cajolery, usually stopping short of coercion and thereby giving the impression that it was following the path of least resistance. The Trade Union Council was persuaded to act as arbiter between individual unions and to veto excessive demands by the stronger unions; employers' associations were backed in resisting wage demands; the Prices and Incomes Board was used increasingly to bring national considerations to bear on specific employment situations. The devaluation has not really made any fundamental difference to the Government's thinking. Its incomes policy remains pragmatic, its approach tactical; hence the confusion over official statements. It acts as if engaged in a rearguard action in which delay is as good as victory. What matters most to the Government at present is to give

the economy a breathing space during which the cost advantage stemming from devaluation can be translated into larger export sales.

The British policy of wage restraint pursues two major aims—the direct one of curbing producing costs, and the indirect one of holding down the pressure of home consumption. As a means of stimulating exports both are equally important and indeed complementary because, given the limitations of productive capacity, it is no less important to release resources for export (and investment) than to gain a cost advantage over foreign competitors. This was implied when the Chancellor of the Exchequer said that how harshly the next budget will have to bear on consumption "will depend in considerable part on the way incomes policy develops". He would prefer keeping tax increases to a minimum, for higher indirect taxes drive up prices and high direct taxes, under the British pay-as-you-earn system, encourage absenteeism. The whole success of any Government must indeed, as the Prime Minister said, depend on a satisfactory prices and incomes policy.

Whether he will get it depends largely on the support of the trade unions. The Trade Union Council at first would not accept another year's wage standstill and suggested a "centrally bargained" 3½-4 per cent annual rise on the assumption of 6 per cent annual economic growth. The figure of 3½ per cent has since been repeated without reference to expected economic growth and apparently accepted by the Government, which seems to be very reluctant to quantify the likely effect of devaluation, as the "basis" of an agreed policy, provided it is not a minimum but an average. Neither side has so far indicated how this rate of increase for the year to July 1969 would be affected by a marked rise in the cost of living resulting from devaluation or tax changes in the March budget. But even if price stability is the overriding objective for the Government and TUC, it is not necessarily for individual unions and their branch officials some of whom have been able to exploit the fluid prices and wages situation in the past. They resent Government intervention when they are in a strong bargaining position and, not without justice, point to many anomalies in the British wages system which need putting right. The employers who could

normally be expected to resist such pressure are under a system of supervised prices less interested in avoiding wage increases, which they are usually allowed to pass on in higher prices, than in industrial peace; for even though strikes in British industry are usually localised and less costly in terms of man-hours lost than in other countries they tend to have wide-spread adverse repercussions in such a highly integrated economy.

### **Criteria for Wage Settlements**

The problem is aggravated rather than eased by the deeply ingrained British belief in fair play and regard for the "underdog" who gets the worst of both worlds when prices and wages for the strong rise. His difficulties have been highlighted by the social welfare system which in extreme cases may give the unemployed father of a large family a higher income than if he were at work. Trade unions and Government have therefore been moving increasingly to the adoption of selectivity as a principle in assessing not only social need but wage priorities. Even the strong and correspondingly militant Amalgamated Union of Engineering and Foundry Workers is ready to abandon blanket pay rise demands for all, albeit on condition that its present wage claim is met first. So there exists a common platform on which Government, employers and trade unions can meet.

The criteria for special consideration under wage settlements are generally accepted. The wage lift for the lowest-paid workers may, as was done for London dockers, be combined with a guaranteed weekly minimum. The yardstick of productivity can be applied to wages in overmanned industries, making it easier to deal with redundancy. Similarly, the elimination of "anomalies", though it can be made to cover a multitude of sins, may in the present chastened mood do much good.

### **The Problem of Earnings Drift**

There remains however the problem of "earnings drift", the exploitation by pressure groups of any agreed norm whether for wage increases in general or for inducements under productivity and redundancy schemes, which has played havoc with previous wage "freezes" and "squeezes". There are perhaps grounds for hoping that this problem will be less intractable than it has been. A higher unemployment rate in the present winter, the postponement of the raising of the school-leaving age and the cuts in the armed forces and their effect on industries working for them should help to provide the manpower reserves which some economists deem essential for a successful incomes policy. An upturn in productive employment in spring will make it easier to cope with redundancy in the collieries, on the railways and in the docks. The trade unions are as keen as ever to retain the voluntary principle for wage settlements and as keenly aware of the loss of sympathy they have suffered among the public through unofficial strikes and indiscipline in essential services.

The past record unfortunately is not reassuring. In the three years from November 1964 on, when the Labour Government took over, to the devaluation in November 1967 weekly wage rates rose by over 15 per cent, compared with a cost of living increase of 11 per cent a minor part of which was caused by higher indirect taxes. Actual earnings, inflated by overtime, piece rates and fringe benefits, have risen more sharply. What is most disconcerting is that even the "standstill" of July 1966 made only a temporary dent in the steady upward curve. The period of "severe restraint" saw as steep rises as in previous years, and the beginning of "moderation" in July 1967 took the line of wage rates to where it would have been had there been no standstill at all. Even if present policy continues unchanged for the six months ahead, as the Prime Minister stated in the House of Commons, the Confederation of British Industry fears that earnings drift superimposed on permitted wage revisions will mean a lift in actual earnings by  $7\frac{1}{2}$ , 8 or even 9 per cent by July 1969. Together with the cancellation of both the export rebates and the Selective Employment Tax refund and premium, this would wipe out almost all benefit from the lower sterling rate to British export industries.

### **Wages and Export Prices**

Substantial exporters however take a less gloomy view. They take heart from the fact that in the three years before devaluation British export prices rose by  $7\frac{1}{2}$  per cent only, half the rate of industrial wages though twice the rate of average import prices. It is indeed doubtful whether the wages, and basic wage rates in particular, of one country determine export prices to any really significant extent. Rising wages were absorbed fairly easily by British exporters in the last few years when pay rates in other European countries also advanced. The exporting industries are, almost by definition, the most competitive British industries. They are also generally capital-intensive with a low labour cost: product price ratio. It is often argued that they need a flourishing domestic market which bears the overheads and carries exports as a kind of superstructure. In many British industries, however, a very different situation has prevailed in recent years: A protected home market offered an easy outlet for the bulk of output, making exports at world market prices less attractive. Wages as a cost factor are comparatively unimportant to the individual exporter if a captive home market provides adequate outlets. Spurred on by an insufficient domestic demand, he may be forced to forage farther a field for orders and pay more attention to competitive costs. Hence the Government experts' insistence on curbs on domestic consumption, public and private, and on stable prices and wages.

### **Important Time Factor**

As devaluation is bound to lead to higher prices (the Treasury estimates the extra cost of imports at 3 per cent) and as, in the light of experience, "moderation" cannot be expected to last very long, it is obviously

important to make the most of any time lag between price rises and wage advances. The Government seems to take a philosophical view of the reported spending spree of British consumers (and Continental visitors). Its immediate effect of softening the seasonal decline in business activity is indeed welcome, and insofar as future consumer demand is skimmed off, it may, especially if the predicted "hard" budget reduces private spending power, well result in a drying-up of home demand just when manufacturers have laid the foundations for an export expansion. Wages are in this context less important than middle class earnings, a fact which partly explains why the Government is willing to see low wages go up by as much as 14 shillings a week in the year ending in July 1969 but has set its face against similar percentage increases on the ground of differential for higher-paid workers.

With the time factor so important, the next few months will be crucial for the success or failure of the British incomes policy. If production can be made to rise before the cost of devaluation is felt at the retail price level, there will be the less need to insist on release of home market resources for export. If the import bill can be cut as the result of a contraction in British consumer spending, export gains will have a more pronounced effect on the balance of payments. The Government may therefore be expected to take a lenient view of wage increases yielding gains in production and to be reluctant to

intervene against wage increases if such action threatens to disrupt production. The very importance of exports may thus lead to higher wages in fields of production and transport linked to the export trade, and if exports increase at the same time, the Government is likely to leave well alone.

#### **Incomes Policy at the Price of Political Unpopularity**

Whether the British inflation has been of the cost-push or demand-pull type is a moot point. Successive Governments have tried to fight it on both fronts but laid more stress on containing demand, chiefly because the occasional and rather haphazard attacks on the wage spiral were politically injurious. British Ministers now speak of an export-led boom, partly in the hope, one suspects, that success in exports will help them to avoid having to tackle themselves immoderate and harmful wage demands by those in a strong bargaining position. Not only the Trade Union Council but the Prices and Incomes Board have been brought in to pronounce on what should be Government decisions. The Government, and especially the Minister of Labour, have still to prove that they are determined to enforce their own incomes policy at the price of political unpopularity. They have under existing law the power to delay wage increases for six months even if agreed to by the employers but still hesitate to use, and even more to augment, this legal power.

### **CAPITAL AID**

## **The Indebtedness of Developing Countries**

by Dr Ulrich Jeromin, Hamburg

**I**n the discussion about development aid increasing attention is being paid to the problem of the growing indebtedness of the developing countries and to the question of whether and if so, in what circumstances, these countries will be able to fulfil the obligations they have undertaken regarding repayment. In this regard it is possible to hold widely differing views and to be either optimistic or pessimistic about the possibility of solving the problem. Apart from these two alternatives there exists yet another variant—a point of view which makes light of the problem or even denies its very existence.<sup>1</sup>

Those who incline to this third view, far from casting doubts on the correctness of the available statistics, make them the very basis of the argument. As long as capital aid takes for the most part the form of credits no one need be, or in fact is, surprised that

developing countries accumulate debts. It is undoubtedly not the accumulation of debts in itself that causes disquiet in both creditor and debtor countries, but the debt service that results from it. These payments constitute an additional burden on the already precarious foreign exchange situation and in turn increase still further the credit requirements of the capital-importing countries.

#### **A Development without Risk?**

Such a development, it is pointed out by those adhering to the above-mentioned third view, involves no risk as long as the industrial countries are prepared to grant net capital aid sufficient to ensure a satisfactory growth. This assumes that it will be possible for the creditor countries to go on exporting capital on a steadily rising scale so as to cover not only the debtor countries' fresh requirements but also the service on previously incurred debts.

<sup>1</sup> Compare: Hans-Jürgen Petersen: Verschuldung der Entwicklungsländer (Indebtedness of the Developing Countries). In: Konjunkturpolitik, 12th year (1966), No. 4, pages 223 and following.