Planning the Free Market

By RONALD BANKS

"To retain or 'review' tariffs for 'planning purposes' is to give away the argument for both free trade and the free economy."

THE Conservative and Labour Governments since the war have shown little difference in their fundamental approach to economic policy. Both parties seem convinced that it is only the academic expert who is able to tackle economic affairs with any success, with the result that it has now become fashionable to accept this. On this basis, all initiative is left to the Government of the time, and the skill, ingenuity and resourcefulness of the people are left to stagnate while the Government and its experts work out their formulae.

While one can criticise the Labour and Conservative parties on the strength of the policies pursued while in office, the Liberal Party has to be judged by its own criticism of the policies of the government of the day, and by policy statements made by Liberal spokesmen.

Since the fortunes of the Liberals have revived, they have shown an inclination to embrace fashionable ideas at the expense of principle, and "planning" has become an important word in their vocabulary.

The first welcome signs of a return to basic principles, however slight, appear in a new statement on economic policy by Christopher Layton and Richard Lamb.* It must first be said that the document contains inconsistencies; largely attributable, it would appear, to an over-reliance on the "expert" and on the role a government is expected to play in a "new economy." However, there are sections — on protection, the market economy and the price mechanism — that are extremely well argued, and it is during the discussion of such subjects that the authors are at their happiest.

Tariffs, hidden subsidies, quotas and other protective devices are attacked on a number of counts, not least as the bastion of monopolies. High tariffs are criticised as preventing investment in new machinery and capital equipment because businesses can make profits in an easy home market with out-of-date factories and plant. Distortion of investment is also laid at the door of protection in that declining but protected industries survive longer than they otherwise would, and thus lock up precious capital and labour resources.

The authors propose a reduction of tariffs, together with stricter legislation against monopolies and restrictive practices, but the term used is "reduction of tariffs" and not "free trade" and the reason for this is soon apparent. It is stated that "all tariffs should be reviewed and used as a positive instrument of Government economic planning." Free trade, of course, cannot be used as a planning instrument. Free trade is in itself the antithesis of planning. With tariffs, decisions are in the hands of the "experts"; with free trade decisions rest with the whole population. To retain or "review" tariffs for "planning purposes" is to give away the argument for both free trade and the free economy.

A similar kind of reasoning is to be found later in the booklet, when the nationalised industries come under discussion. To quote from the document:

"It is high time the price mechanism, which is the best instrument we have for gauging the relative efficiency of different sectors of the economy, and the best means of telling us where to invest our resources, was properly used, here as well as in the private sector. This does not mean abandoning planning or ruling out all social considerations in public services. But it does mean making use of the price mechanism to tell us *where* the nation's money is most economically invested, and planning accordingly. It also means giving a clear directive to the nationalised industries that they must compete and survive on a profitable, commercial basis, with the state providing a conscious, direct subsidy for any particular social objectives which it considers to be necessary."

Except for the reference to planning, which seems irrelevant except to social objectives, the paragraph quoted could appear with merit in any textbook on free enterprise economics. From this point on, however, economic planning is the by-word, although it is apparent that the term "planning" is given many different meanings.

Stress is laid on the importance of overall objectives for economic growth set by the Government, together with Government help to industry to plan for the future. This proposal is hardly consistent with the authors' previous proposal to allow market forces to determine where and how resources should be used; the authors seem to be unaware of the effects that their free market proposals would have on industry and the economy generally should they be implemented. For instance, a reduction of tariffs, legislation against monopolies and a really free market economy would all combine to produce naturally the right conditions for economic growth. There would be no cushioning from a protected home market, and this would stir businessmen to greater efficiency and more selective investment. The skill and ingenuity that exists in this country would be mobilised and utilised without Government planning.

The authors also propose new planning instruments to stimulate exports and investment in the "right place,"

* *The Morning After* by Christopher Layton and Richard Lamb. New Directions No. 10. (Liberal Publication Department, 5s.)

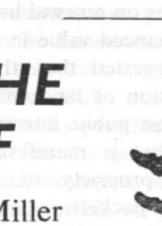
although their other free market economy proposals would serve far better than government intervention. Their apparent lack of faith in the workings of real Liberal principles looks like lip service without conviction.

On the subject of housing they recognise that previous intervention by the state has caused imbalance and distortion, and that the Government should help to redress the imbalance. Yet, instead of proposing the removal of obstacles to increased home ownership (of which land monopoly is one) they propose a plan that will cause even greater distortion of the housing market — that of the Government providing substantial tax reliefs for entrepreneurs who build houses below a certain rent and above a certain standard!

The reference to land reform above will probably prompt a question about the Liberal policy of land-value taxation. Unfortunately, there is no mention of it. It is even more disheartening when one remembers that one of the authors recently wrote a booklet on site-value rating and extolled its virtues.* It appears that, in common with most modern economists, our authors believe that land has nothing to do with economics!

* *Make Rates Fair* by Richard Lamb and Colin Clark. New Directions No. 9. (Liberal Publications Department, 5s.)

OFF THE CUFF



By Robert Miller

BANK RATE up to 7 per cent ; building society interest rate up to $6\frac{3}{4}$ per cent ; local authorities offer $8\frac{1}{2}$ per cent on loans.

What is the connection between these statements, and why is it that they claim so much attention from people with, or perhaps more frequently, without, money? Why, in fact, do so many people get so concerned whenever there is a change in the Bank Rate? (There have been eighteen changes in the last seven years, on average every four or five months or so, with fluctuations between four and seven per cent.)

When the Bank Rate is raised, one object is to discourage spending and to encourage saving. Among those immediately affected are local authorities, who borrow from the Treasury for housing schemes ; faced with the need to raise money in excess of the quota allowed them by the Public Loans Works Board, they turn to the general public, competing with others in offering more tempting terms to lenders. This tends to draw funds away from building societies. The minimum sums accepted by local authorities as loans are usually large enough to exclude the majority of building society investors, but nevertheless, this "drain off" is considerable enough to cause anxiety to the building societies.

Effect on Mortgages

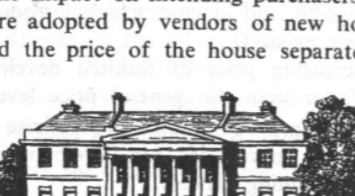
The obvious thing to do when the red light shows is to charge more to borrowers, and as funds get low, to restrict mortgages to those who can afford higher deposits. At the same time, rates offered to lenders have to be raised in order to attract more cash. But these can never be raised high enough to win back the money being transferred to local authorities and elsewhere, because if this were done the rate charged to borrowers would be so high that few people could contemplate a mortgage, and business would come to a standstill.

In the last few years building societies have loaned hundreds of millions of pounds, and the simple answer to the question of why it is now so difficult to obtain a mortgage is that funds are drying up. It goes without saying that if houses had been cheaper during this period the money would have gone further. The reason why houses have been so expensive is due in no small part to an artificially-created scarcity of land — which is not really a scarcity at all. According to the Co-operative Permanent Building Society, the average price of all new dwellings mortgaged to the Society rose by 10 per cent from the end of 1963 to the end of 1964.

Effect on Building

Another inevitable and serious consequence of a high Bank Rate is that because fewer people are able to obtain or afford mortgages, house builders are beginning to cut back their future building projects, and the shadow of unemployment in the industry looms ahead. Of course, it can be argued that as demand for houses diminishes in this way, prices will fall and tend to balance things off, but building prices cannot fall much below that required to cover current costs plus a competitive profit. I doubt if any such fall would be anything like large enough to save a very serious situation that threatens to involve not only the building industry, but — unemployment being such a contagious disease — many others as well.

Finally, I would like to observe that in order to justify what must appear to be too high a price for a commodity a tradesman frequently quotes two prices, his own economic price and the purchase tax. It is intriguing to speculate on the impact on intending purchasers if a similar method were adopted by vendors of new houses so that they quoted the price of the house separately from the



price of the land. One certain result would be that people would have a much clearer idea of where a large slice of their money is going. It might also cause them to reflect on the relative costs of "production" of the two components.