

Managing the UK economy Fiscal and monetary policy since 1945

Week 5 – 1952-67: Fiscal activism and macroeconomic fine-tuning

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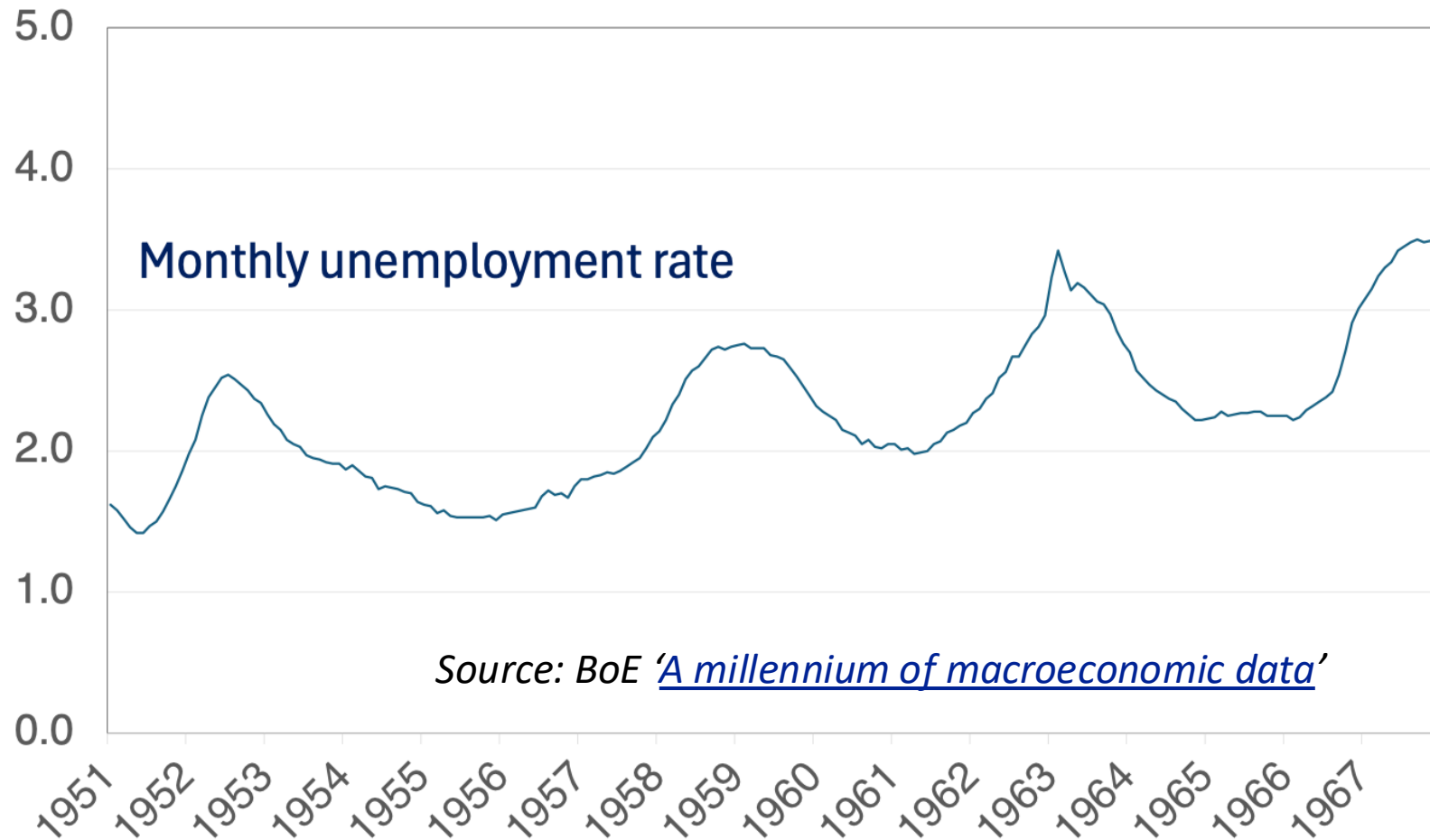
1952-1967: Overview

- Sustained growth, low unemployment, moderate inflation.

Change in Real GDP	Avg. annual GDP growth	Change in labour productivity	Avg. annual productivity growth
65%	3.2%	79%	3.7%
Real GDP per capita growth	Average unemployment	Max yearly unemployment	Average inflation rate
49%	2.3%	3.4%	3.6%

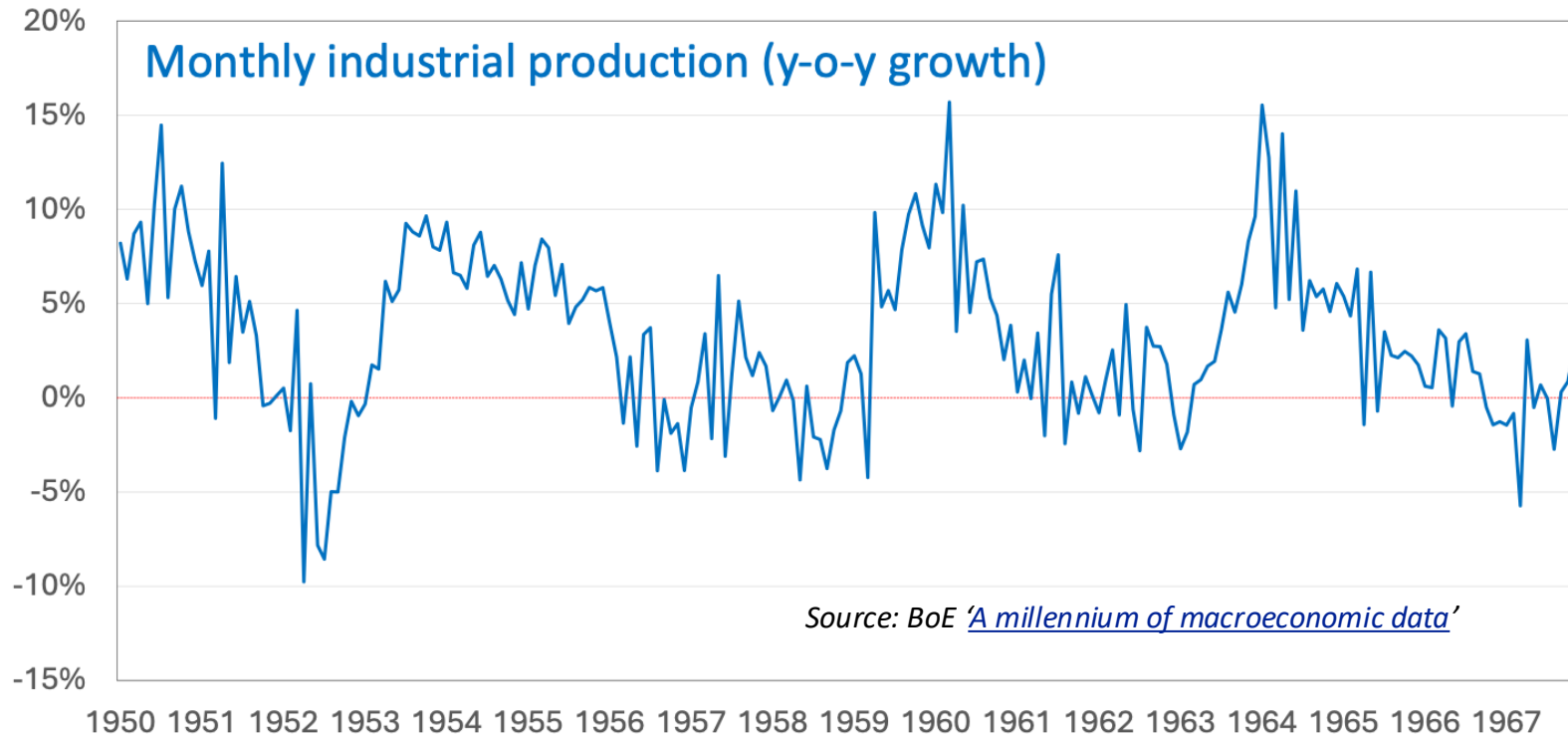
Source: BoE [‘A millennium of macroeconomic data’](#)

1952-1967: Overview



- Very low unemployment throughout
- Although in retrospect it was on an increasing trend.

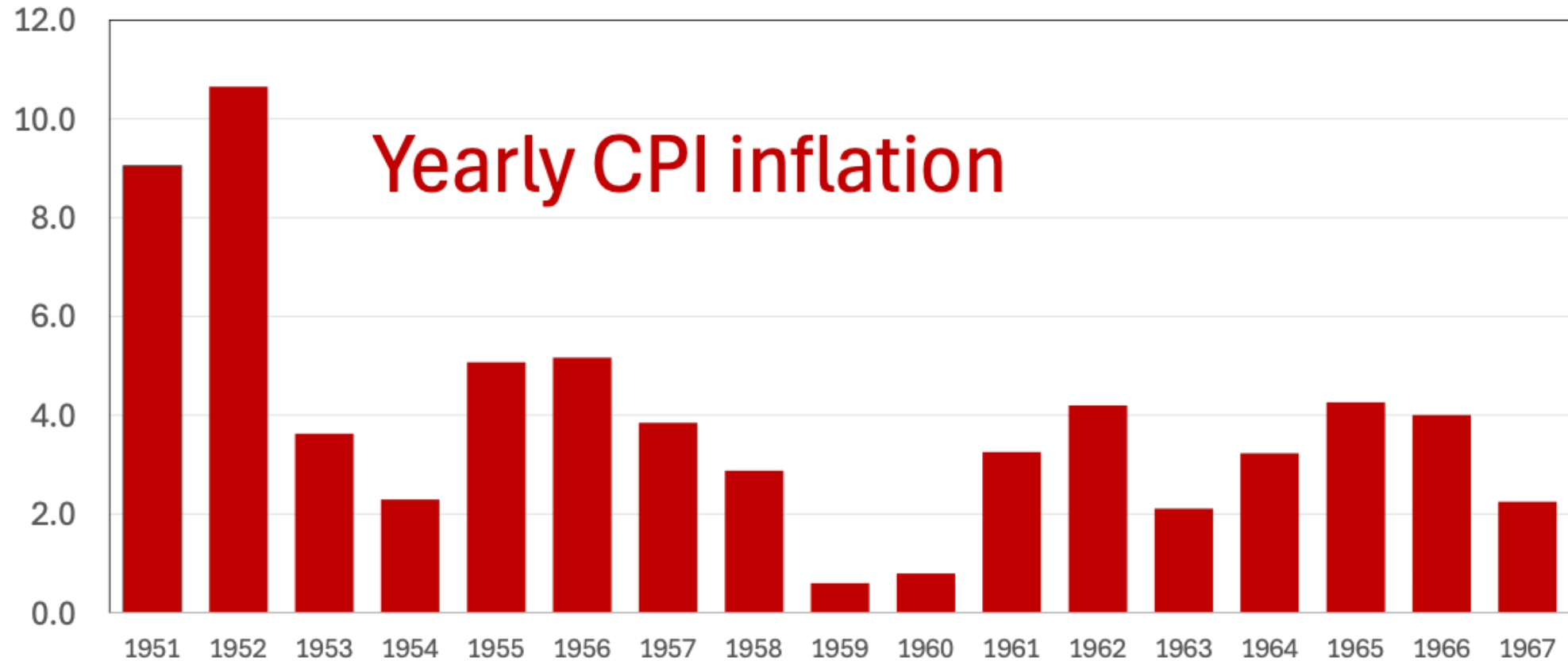
1952-1967: Overview



- Four cycles:
 1. Peaked in 1950-51
 2. Peaked in 1953-55
 3. Peaked in 1960
 4. Peaked in 1964

1952-1967: Overview

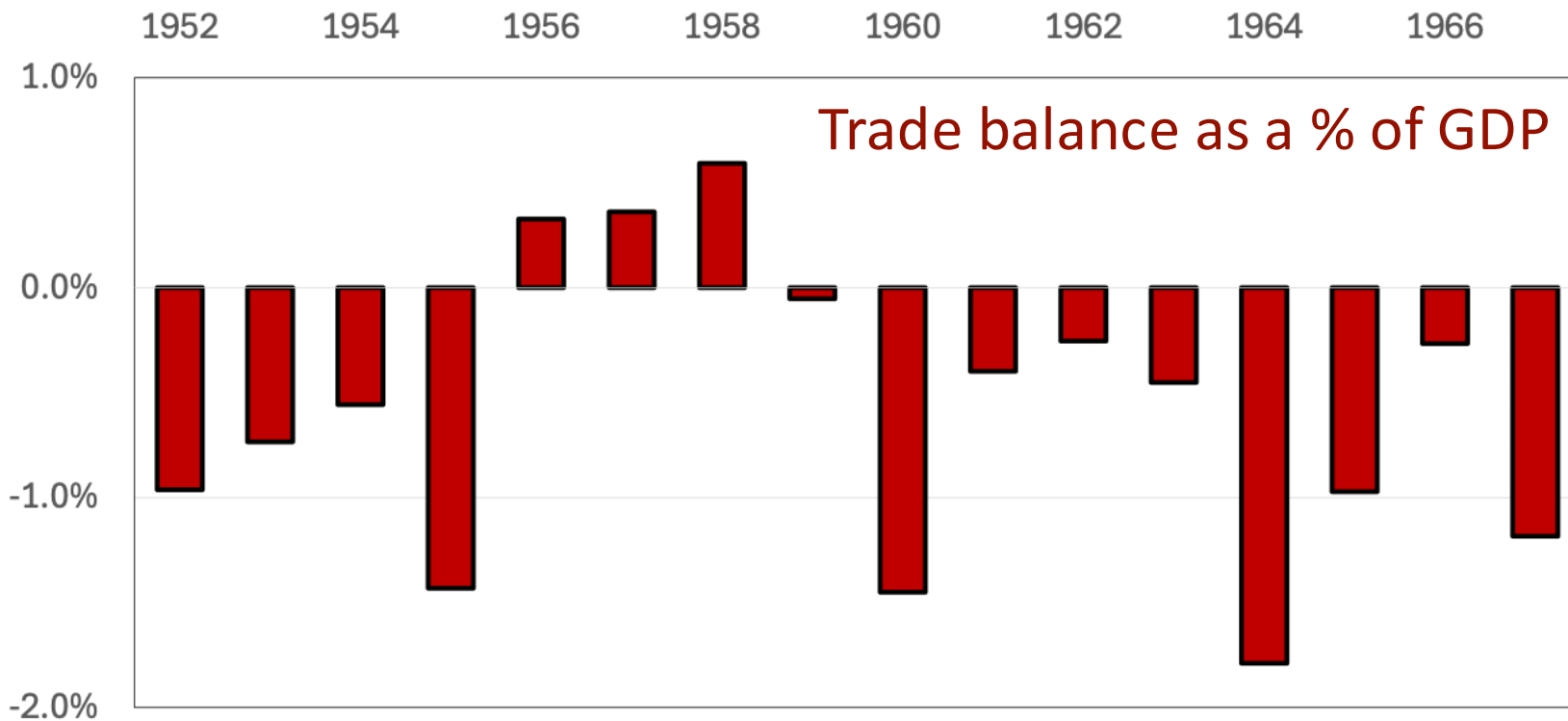
- After the Korean-war boom, inflation was moderate.



Source: BoE [‘A millennium of macroeconomic data’](#)

1952-1967: Overview

- Key constraint to economic expansion: the balance of payments.

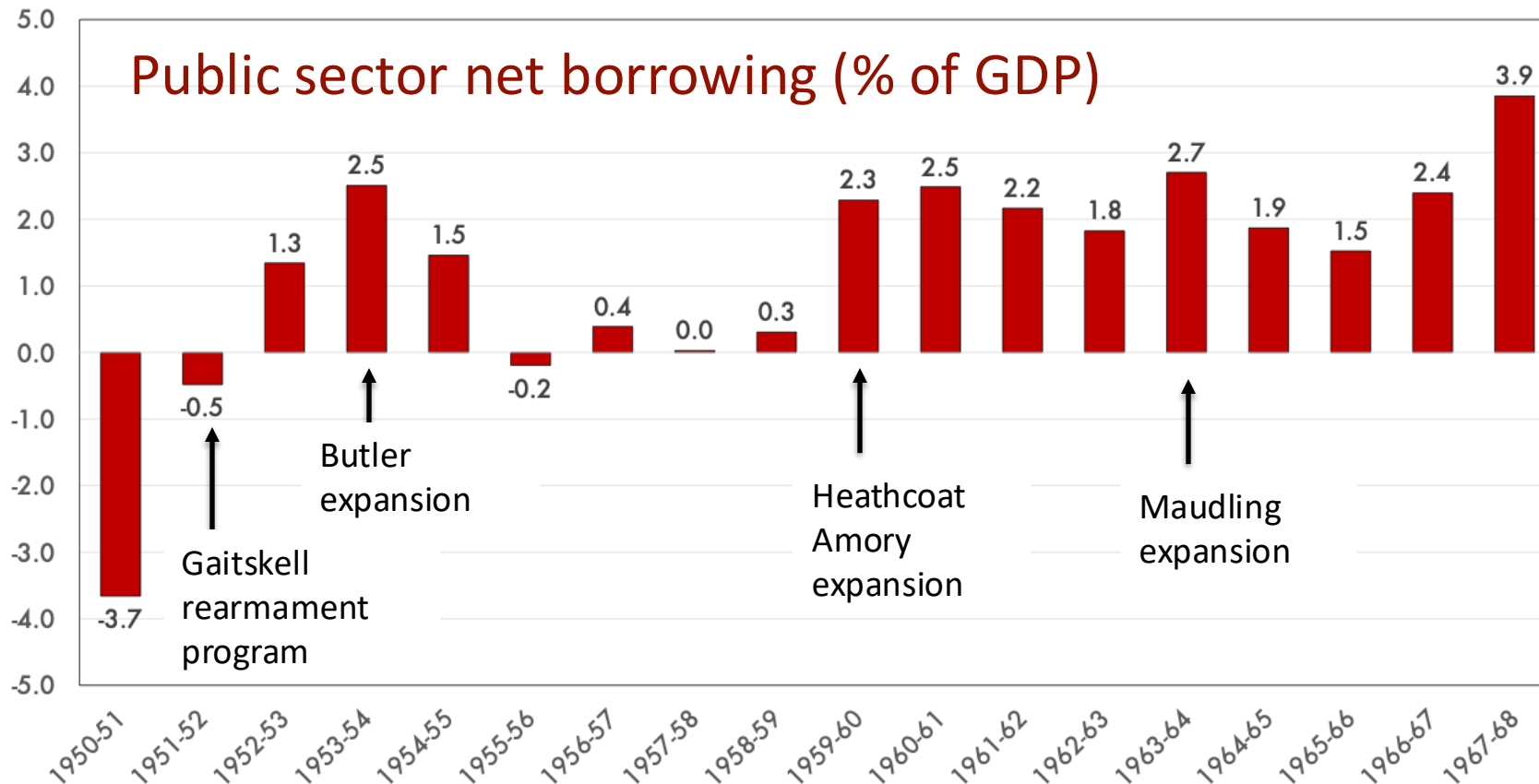


Policy dilemma: often the economy could withstand higher activity, but the balance of payment could not.

Source: BoE [‘A millennium of macroeconomic data’](#)

1952-1967: Overview

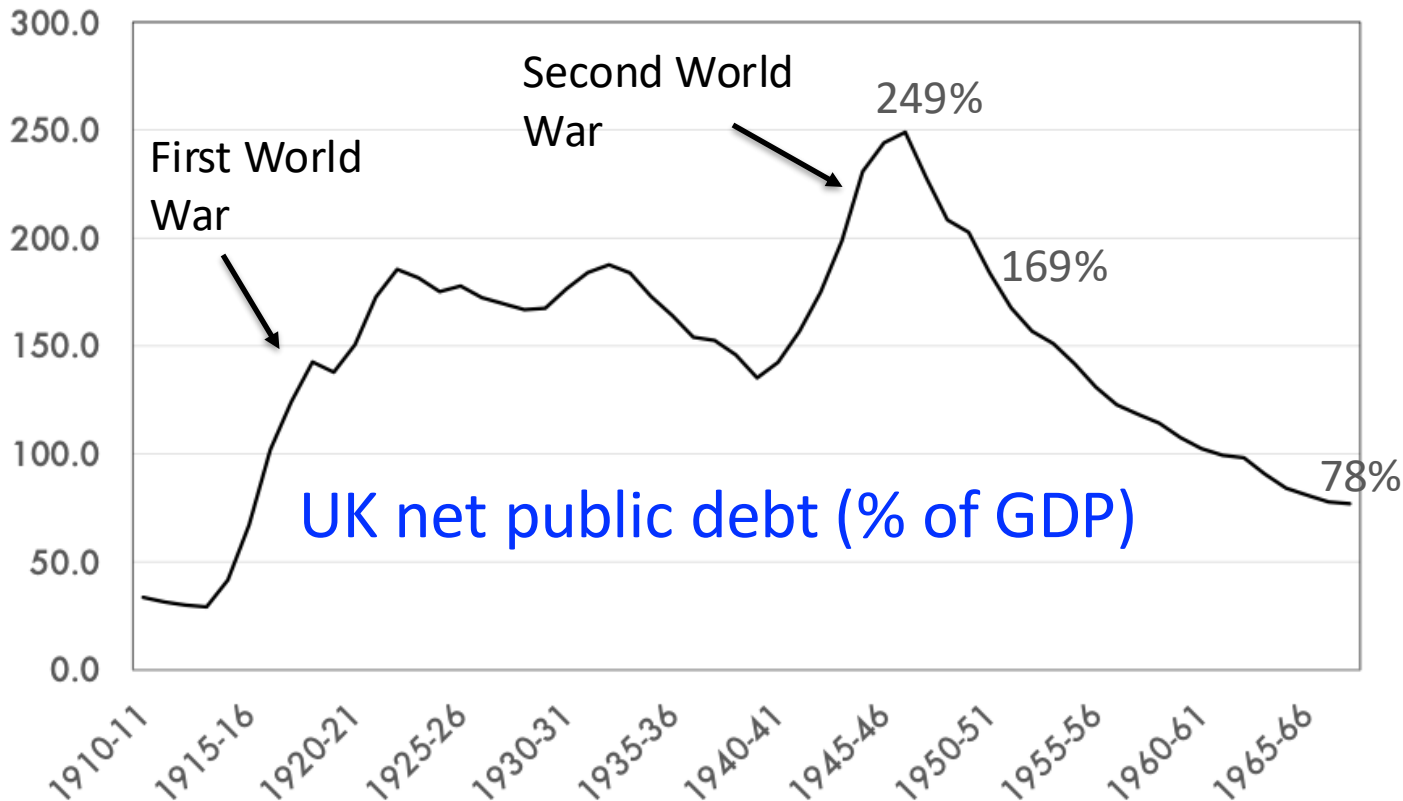
- Budget balance switches to deficit in the 1960s



- Mainly due to the Conservatives' fiscal expansions
 - Butler 1953-54
 - Amory 1958
 - Maudling 1963
- 1966-68 worsening due to (relative) weakening of economy

1952-1967: Overview

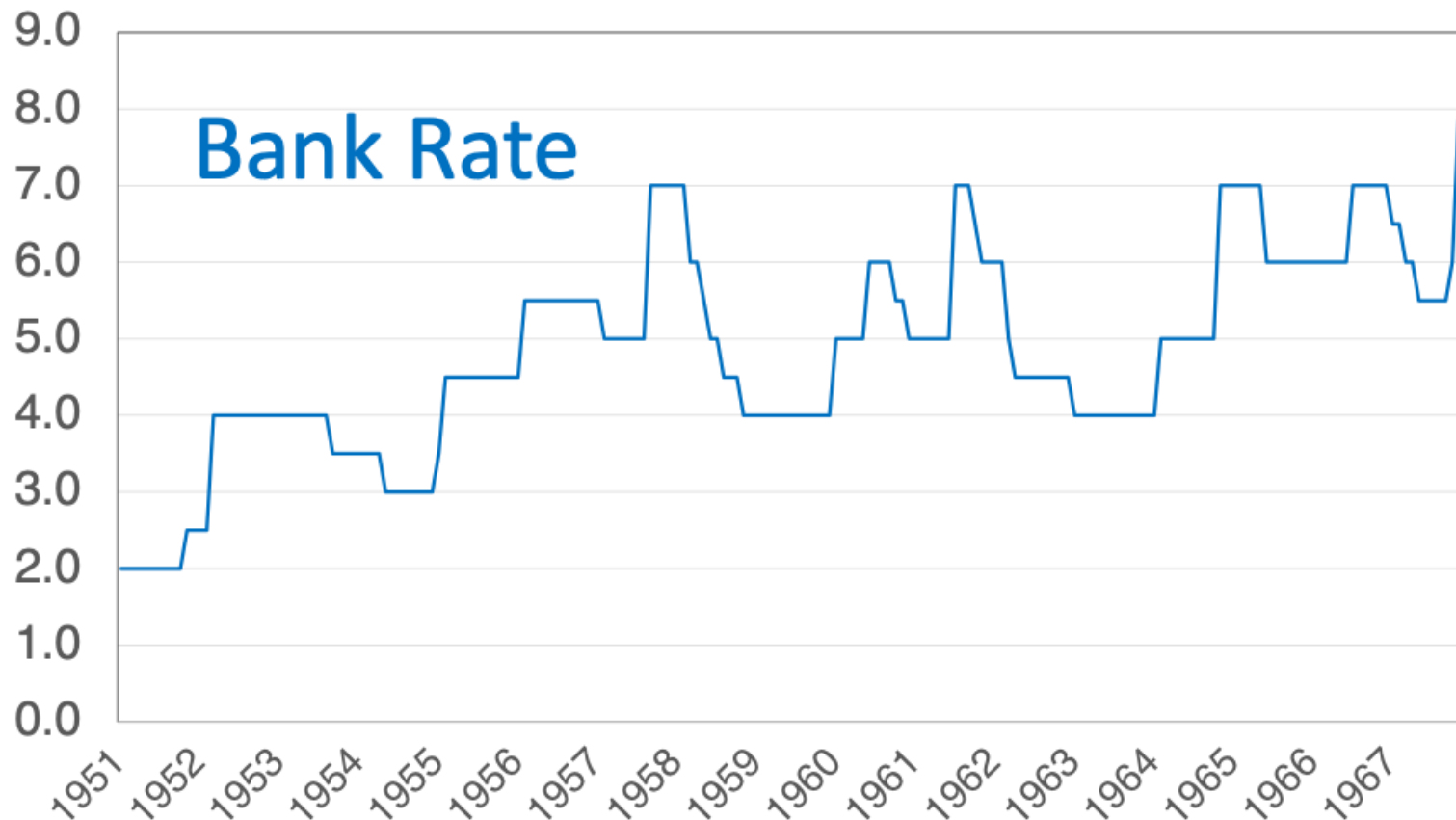
- Debt-to-GDP falls from post-war peak



- 1952: 169% → 1967: 78%.
- notwithstanding deficits in 15 years out of 17
- $g + \pi > i$ did the trick
- Avg. yearly nominal growth $g + \pi \sim 7\%$
- Avg. 10-year nominal rate $i \sim 5\%$

1952-1967: Overview

- Short-term rates higher & more variable

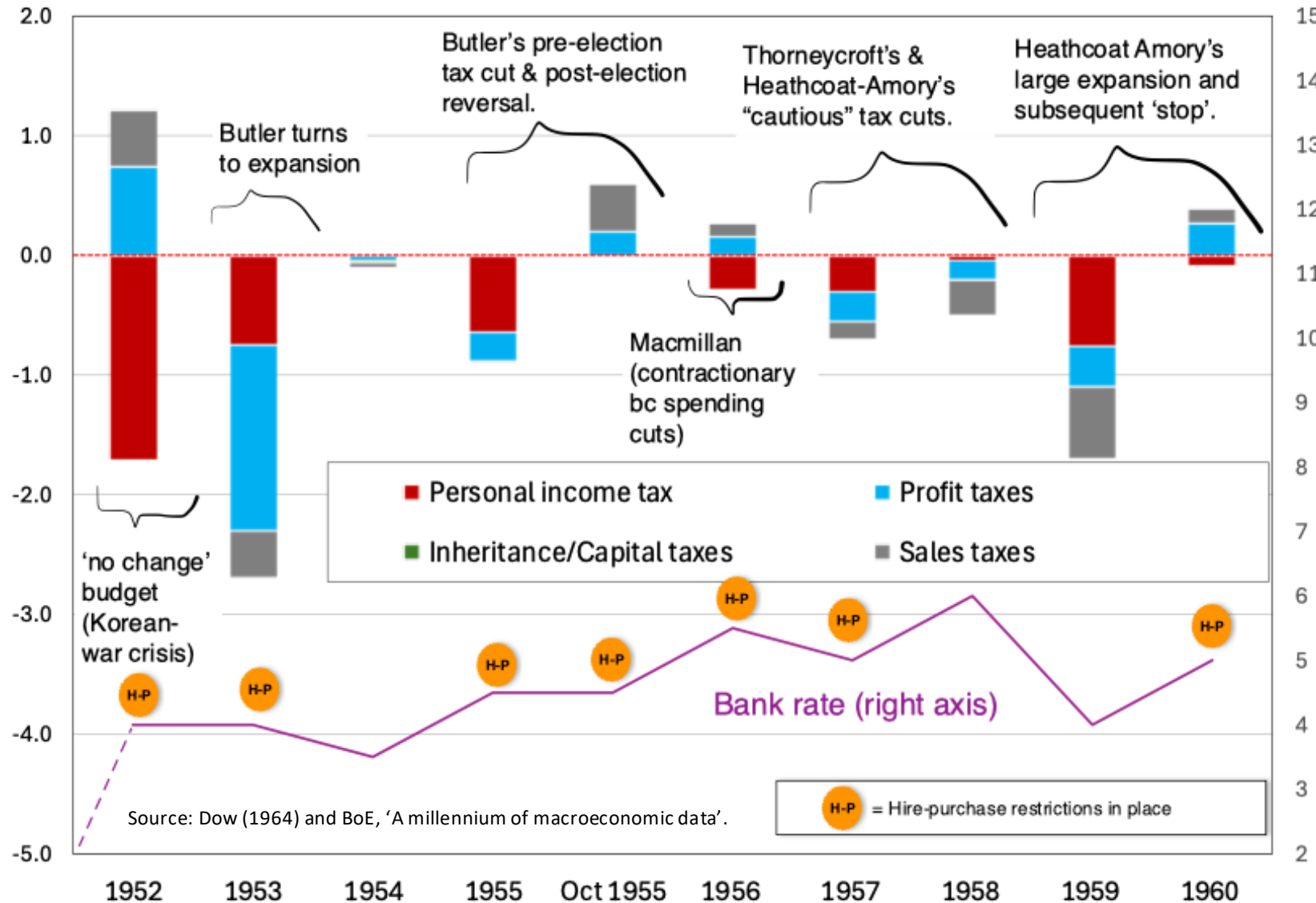


- Nov 1951: Tories re-activate monetary policy
- Cuts coincide with fiscal expansions
 - Butler 1953-54
 - Amory 1958
 - Maudling 1963
- Increases were to cool down the economy & improve balance of payments.

1952-1967: Overview

- Continuities in policy (*'Butskellism'*)
 - Welfare state & nationalized industries (except iron & steel) maintained
 - Demand management through counter-cyclical tax changes
 - Exception: re-activation of monetary policy
- “Stop & go” macroeconomic policy.
- Periodic balance of payments crises.
- Incomes policy.
- Attempts at economic planning.

Fiscal & monetary policy, 1952-1960



1951-52: Korean-war crisis

- Import restrictions

1953-54: shift to expansion

- Housing investment drive

1955: boom & overheating

- Inflation & trade deficit mount
- Apr 1955 budget makes things worse & gets reversed in Oct

Aug-Dec 1956: Suez crisis

- run on £
- Macmillan 'promoted' PM

Dec 1958: £ convertibility

Jan 1958: Thorneycroft resigns over fiscal policy

1959-60: Again, pre-election tax cut & then reversal.

- Special deposits scheme

1960-1962: Lloyd's Chancellorship

- July 1960: Selwin Lloyd Chancellor.
- Still feeling the aftermath of Amory's 1959-60 expansion
- **Apr 1961 Budget:** neutral (+£55m revenues)
 - *'Tax regulator'*: tax changes outside budgets
 - Increase in profit taxes & sales taxes
 - Personal income tax cuts
- **July 1961 emergency measures:** deflationary
 - Monetary: Bank rate hike (4→7%) + more special deposits
 - Fiscal: sales taxes up + spending cuts (£300m)
- **Apr 1962 budget:** neutral
 - But monetary policy relaxed (bank rate down to 5%)



1962-1964: Maudling's "Dash for Growth"

- **July 1962:** Reginald Maudling Chancellor.
- Fateful decision: '*dash for growth*' notwithstanding risks for the balance of payments.
 - **Nov 1962:** Sales tax on cars slashed (45-25%).
 - **Jan 1963:** Bank rate cut (4.5 → 4%)
 - **Apr 1963 budget:** large tax cuts (£638m in full year) & increased public investment.
 - "*I absolutely reject the proposition that a vigorous economy and a strong pound are incompatible*" [1963 Budget speech]
- **Early 1964:** balance of payments crisis starts.
- **Apr 1964 budget:** £100 increase in sales taxes.
- **Oct 1964 election** under a £800m BoP deficit & severe pressure on reserves.



1964-66: 1st Wilson government

- Triumvirate in charge of the economy: Wilson, Callaghan & Brown.
- They inherit a booming economy & a severe BoP crisis but reject devaluation or deflation.
- Strategy: affect BoP directly & try to increase competitiveness
 - Import surcharge & export subsidies
 - Tighten exchange controls
 - Incomes policy & industrial policy
 - \$3 billion loan from foreign CBs
- Nov 1964 & Apr 1965 budgets: mild fiscal consolidation
 - Increase in direct & indirect taxes (~ £164m, or 0.5% of GDP)

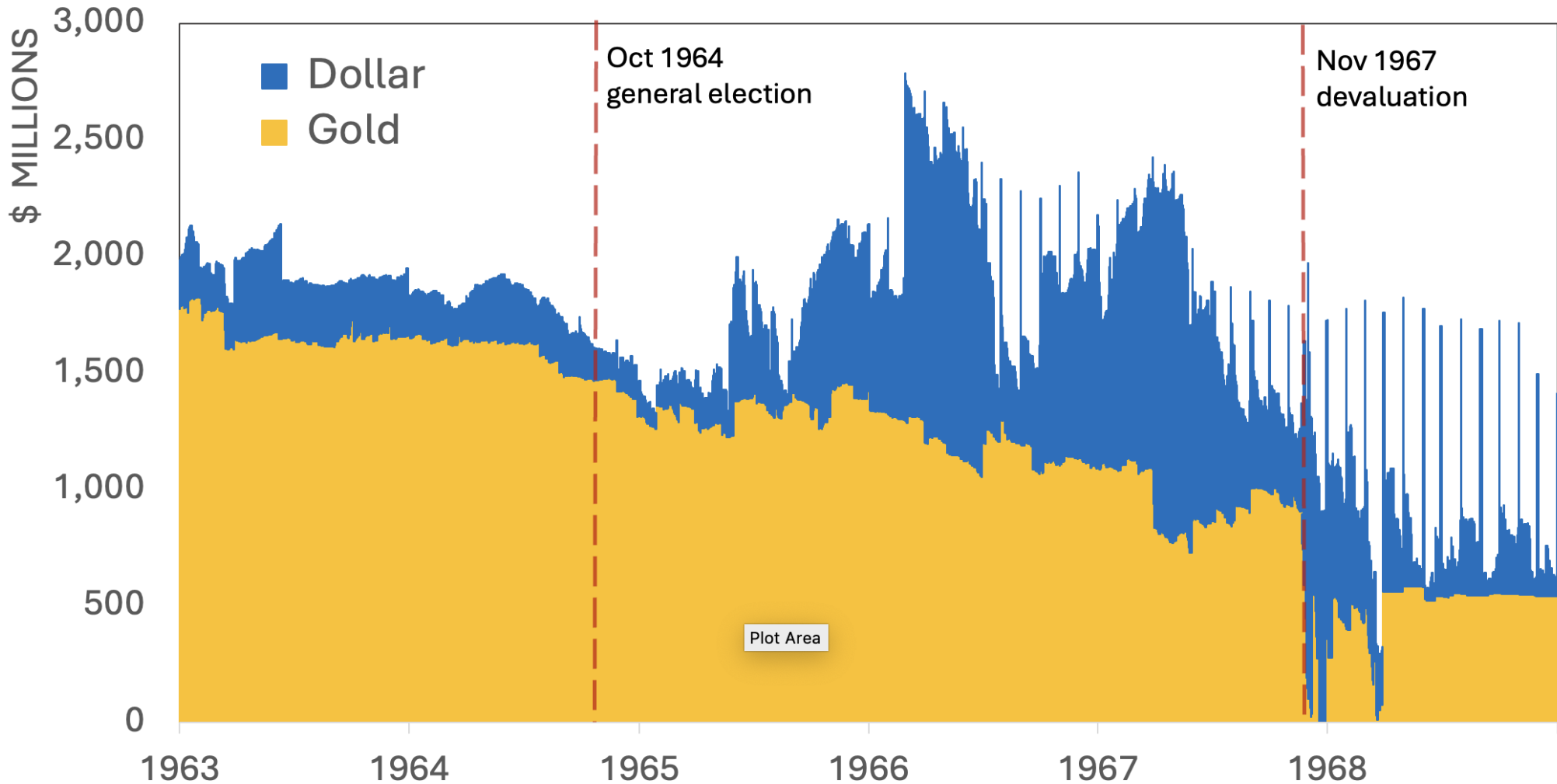


1966-67: Countdown to devaluation

- Mar 1966 election increases Labour majority
- Structural tax reforms
 - Corporate tax and capital gains tax (1965)
 - Selective Employment Tax (1966)
- Emergency measures July 1965 to July 1966
 - Further hire-purchase restrictions
 - Cuts in public investment (£200m)
 - Restrictions on new construction (excl. houses, schools, hospitals & industries)
 - 1966 freeze on wages and prices
- After temporary improvement, reserve drain restarts in Spring 1967
- November 1967 devaluation: \$2.80 → \$2.40 (15%)



EEA reserves, daily data, 1961-64



Incomes policy

- How to prevent a booming economy from igniting inflation and undermining the balance of payments?
- Gov't wants to go beyond 'stop & go', act directly on wages and prices.
- *“To keep the rate of increase of incomes within the long-term rate of growth of national production”* [1962 White Paper “Incomes Policy: The Next Step”]
- 1948-49: Cripps demands (& largely obtains) wage restraint from unions.
- 1960s: attempts to institutionalize income policy
 - 1962 *National Incomes Commission*
 - 1965 *National Board for Prices and Incomes*

Attempts at planning

- In 1960s, increasing attention to economic growth.
- European peers (Germany, Italy, France) growing faster than UK and generally more competitive in international markets.
- Labour & Tories see economic planning as key to faster growth.
- The model was France's indicative planning.
- 1962: National Economic Development Council ('*Neddy*')
 - Tripartite body that would study ways to increase growth and competitiveness.
- 1964: Department of Economic Affairs (DEA)
 - New economic department, responsible for economic planning
 - A more growth-oriented counterweight to the Treasury.
 - The BoP crises undermines its 1964-65 National Plan from the start.

Concluding thoughts on 1952-67

- Easy to highlight the policy mistakes
 - Conservatives' reckless pre-election tax cuts.
 - Labour's foolishness in addressing the balance of payments crisis.
 - The Neddy and DEA fiascos.
- But it was also a period of ambition and experimentation
- The pursuit of full employment, the attempts at industrial policy, incomes policy, planning, the 300k houses a year....
- Never before and never since has the government been so ambitious in trying to steer the economy.



Thank you for your attention