



SUMMER ADDRESS

# Monetarism and Morality

Brian Griffiths



CENTRE FOR POLICY STUDIES



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a response to the bishops

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This is the edited text of the second Patrick Hutber Memorial Lecture, delivered by Professor Brian Griffiths at the Ironmongers' Hall in the City of London on 2 May 1985, under the aegis of the Institute of Public Relations (City and Financial Group) and of Gresham College.

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The views and arguments expressed in this Address are those of the author alone. The Centre never expresses a corporate opinion in its publications.

### **Introduction**

It is a very great privilege to be invited to give this lecture in memory of Patrick Hutber. For those of us who knew him and indeed for anyone who has read his books or columns, it was clear that he was interested not only in the narrower issues of financial life, but the broader issues as well, and in particular the relationship between economic life and the underlying values of our society. It is because of this that I have chosen 'Monetarism and Morality' as my theme for this lecture. I am sure it is a subject of which he would have approved and indeed, on which, had he lived, he would have written not once, but many times.

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## The Moral Indictment

Over the past few years, 'monetarism' has become a generalised term of abuse in public debate in this country, comparable in its way to racism, sexism, colonialism and fascism. It is used as a wholly negative term, evocative of inhumanity, injustice and strife. Yet monetarism was first used in the late sixties as part of a highly technical debate among professional economists. In this lecture I am concerned to examine the relationship between monetarism and morality, to explain why it has become a term of such abuse, and to analyse the attack which has been launched against it on moral grounds, especially by those in positions of leadership within the Christian church.

Let me begin by giving some examples of the criticism which surrounds it.

In a recent debate in the House of Lords (13 November 1984), the Bishop of Lincoln argued that 'monetarist policies are about freeing the market. One of the obstructions to this aim is monopoly of any kind, and one of the monopolies here applied, as the Government seems to see it, is the monopoly of trade unions in the labour market. This means that building the needed climate of confidence in the nation becomes impossible'.<sup>1</sup>

At the time of the last Conservative Party Conference, the Archbishop of Canterbury, in a thoughtful interview with *The Times*, raised the question, 'How long can we wait for jam tomorrow?' – and answered it:

Economic growth, better living standards, higher pay for those in employment, the recovery of national pride, are all self-evidently worth aiming at; but if the human consequences of such aims mean unemployment on an unprecedented scale, poverty, bureaucracy, despair about the future of some communities, inequitable sharing of the sacrifice called for, then the objectives must be called into question.<sup>2</sup>

A few days earlier, the Rt. Rev. Hugh Montefiore, Chairman of the General Synod's Board of Social Responsibility, warned that:

If this government insists on continuing the policies of confrontation, we shall never find a national consensus on how to face the future. And so the future will continue to be a source of fear,

whereas it could be a source of opportunity . . . Those in authority will never gain the goodwill of the powerless unless they begin to show a more caring face – and not only show a caring face but make it clear that they do care about others.<sup>3</sup>

In the General Synod debate the following month (November 1984), the Bishop of Lincoln argued that he believed there were 'powerful influences at work in this country which have sought to raise a certain set of economic theories into an entire philosophy of life.'

Economic theories cannot be made to symbolise a whole philosophy without doing damage. The whole of life cannot be motivated by market forces. Working people are not just 'costs'.

On the basis of this analysis he called for new policies:

I do not believe the unrelenting pursuit of the free market can bear the full implication of our unemployment situation. So I believe a new political initiative is also required, as a new context in which a free market may do its work.<sup>4</sup>

In reporting the same debate, the *Church Times* wrote that the Bishop of Durham 'drew applause when he said that, if action on monetarist principles steadily increased the number of the poor and made the rich even richer, then it must be challenged: and that it was no answer to say 'but this is the only way forward'. That was as dogmatic as the claims of Marxist socialism.'<sup>5</sup> The same theme was taken up by the Bishop of Liverpool, who said that there were many alternatives open to the government and that There Is No Alternative (TINA) was simply not true.<sup>6</sup> Since that debate the Bishop of Liverpool and a number of other distinguished church leaders have signed the Charter for Jobs, recommending increased public expenditure and public borrowing as a way of reducing unemployment.

In the Hibbert Lecture given recently, the Bishop of Durham developed and extended his attack on the government's economic policies, and in particular the relationship between the welfare state and the market economy.

To give up the central concerns of the Welfare State and the Beveridge Report because we have run into difficulties is sheer

faithlessness and inhumanity. To return to the ethics of 19th century entrepreneurial individualism is either nostalgic nonsense or else a firm declaration that individual selfishness and organised greed are the only motivations for human behaviour . . .

. . . to promote a materialistic market-oriented individualism as the key to human social progress is to make an equally destructive mistake about the possibilities and needs of men and women and to turn one's back on real political and social progress which has been made. Realism about sin should not lead to cynicism about altruism and justice or pessimism about the possibilities of collective organisation and communal care.<sup>7</sup>

The criticisms have not been confined to the bishops of the Church of England. In describing the Twenty-first Assembly of the British Council of Churches, which included representatives of the free churches, held in December 1984, Canon Paul Oestreicher spoke of 'the almost unanimous critique of many government policies'<sup>8</sup> expressed by the delegates.

The moral indignation of these statements is clear enough. In general terms they raise four major concerns regarding the 'monetarist' aspect of government policy: its objectives, namely, control of inflation and public expenditure, and the pursuit of efficiency, which are held to be short-term and narrowly conceived; its philosophical foundations, which are said to be unbridled individualism and materialism; its style of implementation, which is confrontational, uncaring and apparently unconcerned with developing national consensus; and its effects, which are alleged to create unwarranted levels of unemployment and to be socially divisive. This is a comprehensive indictment.

The intellectual basis of these criticisms is the bishops' view of the meaning of Christian justice. Even though the different bishops start from different theological positions – conservative, liberal and radical – they are all agreed in arguing that on the basis of a biblical view of society, present policies are not only wrong but also unchristian. While professional economists have attacked monetarism primarily on scientific grounds, and politicians primarily on the basis of expediency, the clerical attack has fused these two elements with a third, namely the Christian view of man and social justice.

It is at this point that I must make a personal confession. I am a loyal member of the Church of England and in that connection have great respect for the authority vested in the bishops of the church. As



a professional economist I have been identified with the development of monetarism since its inception in the mid-sixties, before the term monetarism was even coined. I have always believed and continue to believe that the advocacy of monetarist economic policies is perfectly compatible with a Christian view of the world, and indeed that if such policies are seen as part of a general economic strategy to reduce the power of the state, give more power back to people, and to increase the participation of the individual family in economic life, then their basis is distinctly Christian.

In this lecture I would like to argue that for those who share Christian standards of morality and a concern for poverty and unemployment, there is another way forward that does not involve higher public spending and inevitable inflation; that this way is based on certain economic facts of life, as well as on orthodox theology; that it can answer the charges which are held against it; and that far from being indifferent to the present level of unemployment, it is constantly leading towards new and innovative solutions to reduce unemployment and create jobs. That way forward is what is now generally called monetarism.

## Monetarism

### Definitions

Before we examine the validity of the attacks on monetarism, it is important for us to do two things: to clarify the term 'monetarism' – because as we have already seen, it has come to be used in a number of confusing ways; and to look at the Christian basis for making moral judgements in the field of economics.

I would like to explore four uses of the expression 'monetarism': firstly, technical monetarism; secondly, monetarism as represented by the medium-term monetary and fiscal policies of the present government; thirdly, economic conservatism; and fourthly, as a libertarian ideology. If we use Occam's Razor, we arrive at the first and narrowest of all concepts – something which we might call *technical monetarism* – which is the most generally accepted meaning of monetarism among professional economists.

#### 1 *Technical monetarism*

Technical monetarism is based on the proposition that there is a stable and predictable relationship between the rate of growth of the nominal stock of money and the rate of growth of money demand. The proposition holds strictly only in a closed economy or one in which the exchange rate is free to float; in an economy with a fixed exchange rate, as was true in most developed countries in the 1950s and 1960s, there would be a stable and predictable relationship between money creation and the balance of payments – with excess money creation producing a balance of payments deficit, and a restrictive money policy producing a balance of payments surplus.

The major implication of technical monetarism therefore is that any sustained and excessive creation of money by the central bank will result, after a period of time, in the growth of total money demand in the economy or, in an economy with a fixed exchange rate, a balance of payments deficit. This implication depends on two key assumptions being met: first, the demand for money (or the velocity of circulation of money) must be related in a reasonably stable way to income, wealth and interest rates, so that changes in the demand for money do not offset changes in the money supply; and second, that it is possible for the monetary authorities to control the money supply.

Separate from this general proposition, but still a part of technical monetarism, and certainly held by most, and probably by all, people who would be described as monetarists, is the view that the medium-



term growth of real output is independent of the growth of money demand: that is, that the growth of industrial production, the growth of the service sector and the growth of output in the economy as a whole cannot be changed by changing the level of monetary demand. The supply side of the economy can be changed through increased efficiency, greater enterprise and improved flexibility within companies and markets, which result from improved incentives, greater competition, less regulation and lower taxation. In other words, increasing the level of money demand through increased public spending or increased money supply may have a temporary, but not a permanent, effect on the level of industrial production. Increased money means higher inflation but not higher output.

Similarly, increasing money demand more rapidly than the growth of the economy will have no lasting effect on the level of unemployment. Jobs are created by enterprising people and firms, with new ideas and new products, which can be sold at prices which are competitive in world markets, and produced at unit costs which offer a reasonable rate of return on capital employed. The same basic proposition holds: increased money means higher inflation, not more jobs.

Monetarism used in this rather narrow and technical sense is not new. Since the origins of scientific economics in the seventeenth century, the fundamental concepts have been accepted by the majority of economists, including Hume, Smith, Ricardo, Mill, Marshall and Keynes.

It is important to remember why monetarism as a concept was revived, especially among professional economists, in the late nineteen sixties and early seventies. For the previous few decades the standard paradigm among politicians, policy makers and academics was that full employment was the major objective of macro-economic policy, and that it could be attained through rigorous demand-management policies.<sup>9</sup> In the late fifties the concept of full employment was elaborated into a trade-off between unemployment and inflation. Unemployment could be permanently reduced but only at the expense of a permanently higher rate of inflation. During this period the level of unemployment which prevailed was much lower than either Keynes or Beveridge had expected at the time of the Beveridge Report on Full Employment in 1944, and the level of inflation was low.

In the UK the beginning of the debate over monetarism was linked to our borrowing from the IMF in 1968. The devaluation of

sterling in 1967 was coupled with an easy credit policy in 1968 and the balance of payments deteriorated. At a time when the British government did not even publish statistics on the money supply, the IMF was insisting that if the balance of payments deficit was to be reduced, money supply growth must be brought back under control. It was this more than anything else which sparked off controversy, and it related to the intellectual question of whether or not there is a necessary link between excess money creation and the balance of payments deficit.

More generally, however, the late sixties and early seventies saw two important developments throughout the western world which had not characterised the previous four decades: one was the recognition of inflation as the dominant economic problem; the other was the phenomenon of unemployment rising alongside inflation, in seeming contradiction of any stable negative trade-off between inflation and unemployment. It was the inability of the Keynesian analysis to explain inflation and the rising unemployment brought in its train, which accounts for the development of monetarism.

## 2 *The medium-term financial strategy*

Distinct from technical monetarism is a second use of the term, associated with the monetary and fiscal policies of Mrs Thatcher's government. These are embodied in the Medium Term Financial Strategy which was established by Sir Geoffrey Howe in 1980 and modified by Nigel Lawson since 1983. This concept of monetarism is associated with the following propositions:

- one, control of the money supply is a necessary condition for reducing inflation and for economic recovery;
- two, total government borrowing must be controlled if interest rates are to be kept down;
- three, if the supply side of the economy is to be revitalised then taxes must be cut and, to make this possible, public expenditure as a proportion of GDP must be reduced;
- four, inflation can be reduced and recovery and employment sustained if monetary and fiscal policies are incorporated in a medium-term strategy rather than if they are changed annually on a discretionary basis;



- five, unemployment can be reduced in a non-inflationary manner only by tackling rigidities, restrictive practices and controls in the labour market, rather than by general reflation;
- six, incomes policies, even when initially successful, have not in the longer term succeeded in controlling inflation, raising productivity or creating jobs, and should therefore not be used.

It is important to notice that although control of the money supply is one instrument of policy, a medium-term financial strategy relies on more policies than simply monetary control.

The source of a medium-term financial strategy can be found in Professor Milton Friedman's work, *A Strategy for Monetary Stability*, first published in 1948, in which the case for medium-term rather than short-term policies was put forward on the grounds primarily of uncertainty over the time-lags involved in economic relationships.

### 3 *Economic conservatism*

In the context in which the medium term financial strategy has been implemented, there is another and third concept of monetarism which needs to be stated – namely, the vision of economic life associated with Mrs Thatcher's policies, which can be thought of as a particular interpretation of *economic conservatism*. The principal features of this vision are:

- first, a property-owning democracy in which families are encouraged to develop attitudes of self-help;
- second, the transfer of assets from the public sector to the private sector through a policy of privatisation;
- third, a movement away from the corporate state by giving less emphasis to the National Economic Development Council and tripartite gatherings of the government, the CBI and the TUC; and
- fourth, a recognition that although government has an important role to play in the provision of welfare, the welfare state is in need of radical reform – with a special emphasis on charity, the value of individual citizens caring for each other in organised ways out of their own sense of responsibility.

### 4 *Libertarian ideology*

The fourth and broadest interpretation of monetarism is as a *libertarian ideology*. This is the view popularly associated with Milton Friedman (as put forward in *Free to Choose*) that free markets, unhindered by government, should be established in as many areas of the economy as possible. This would imply not only the privatisation of airways, telecommunications and shipbuilding, and the deregulation of financial markets and planning controls, but also the privatisation of education, and of much welfare and health care, the removal of immigration controls, as well as the removal of regulation in more contentious areas such as drugs, marriage, prostitution and censorship.

Libertarianism is not just the advocacy of certain economic policies but a philosophical position which has roots extending back to the eighteenth century, and in particular to the Scottish philosophers of the Enlightenment such as Adam Ferguson, David Hume, Josiah Tucker and Adam Smith, and which has been developed in our time by F A Hayek and Robert Nozick. As a philosophy it is an attempt to explain society and its institutions (law, money, markets, morals) not as the result of some conscious design, whether by man or God, but rather as the result of a process of spontaneous evolution, variously associated with Adam Smith's principle of the invisible hand and natural liberty, with the Darwinian survival of the fittest, and with Hayek's concept of catallaxy – that 'special kind of spontaneous order produced by the market through people acting within the rules of the law of property, tort and contract'.

### **The value of these four distinctions**

These then are the four most significant uses of the expression 'monetarism'. The value of these distinctions is that they show quite clearly the differing moral content of the term monetarism in each of the cases I have outlined. At one extreme, *technical monetarism* is a scientific concept without any moral content whatever. As a scientific hypothesis, it is open to refutation by empirical evidence, using the criteria of the scientific method. Because of its scientific status, it is not based on political or moral judgements, and is therefore not open to attack on moral grounds.

The other three uses of the term monetarism all involve some element of moral judgement, though to differing degrees. *Libertarianism* is a social, economic and political philosophy with a



distinct view of man and society, in which the establishment of individual liberty is the touchstone by which any social institution or social policy is to be judged. As such it makes fundamental assumptions which fit uneasily, if at all, into the framework of Christian morality.

By contrast, *economic conservatism* does not have the same conception of the state and the individual as libertarianism, and many of its proponents have developed their case with a conception of the good which extends beyond the freedom of the individual, even though at times the emphasis on pragmatism has concealed the moral underpinnings.

The areas of moral judgement involved in assessing the *medium-term financial strategy* are more difficult to disentangle. Much of the basis of this strategy (as is clear from the six elements which I outlined earlier) is a view of the way in which the economy works, and in that sense is a combination of economic fact and economic judgement. The area of specific moral concern is harder to pinpoint, but *inter alia* it must cover concern about inflation and its effect in raising unemployment, the application of gradualism as opposed to shock treatment in reducing inflation, the incidence of public expenditure and tax cuts, and their impact on the distribution of income.

### **The Christian basis for moral judgements**

Before I discuss the criticisms which have been levelled against monetarism, it is important to be clear about the basis on which moral judgement is to be made. As the most severe criticisms have been made by bishops of the Christian church, and as much of the culture and institutions of this country has been moulded by Christian tradition, I am particularly concerned with the Judaeo-Christian basis for moral judgements. I do not underestimate the strong moral stance which is taken by other faiths but I am concerned to focus attention on something specific, close at hand and voluble.

Although theologians over the centuries have emphasised different ways of relating the Christian faith to society – St Augustine and the concept of the two cities, St Thomas Aquinas and the concept of natural law, Calvin and the Reformers with their emphasis on creation and biblical laws, the Oxford Movement and the importance of the Kingdom of God, and contemporary liberation theology with its attempt to relate the Exodus to revolutionary Marxism – nevertheless they all attempted to struggle, in reaching their conclusions, with the

complexities of the biblical text, even if one has to admit that they only achieved varying degrees of success.

While it is impossible to develop a Christian blueprint for economic life, I believe it is nevertheless possible to discover certain fixed points or guidelines which hold true both for the individual and for society, however uncomfortable it may be to acknowledge them. In this respect, not the least of our problems in attempting to apply the Christian faith to social and economic life is that the fashionable words of Christian theology which are so much the currency of current clerical comment – love, peace, justice, compassion and fellowship – need to be taken alongside those unfashionable expressions which seem to be in such scarce supply – sin, judgement, evil, lust, hell. Not only this, but in laying down guidelines we must also be very careful that our selection of themes and ideas is not simply a justification of prior opinions.

If we attempt this exercise, then I believe that one fixed point in a Christian view is the significance of the individual. The Christian starts from the profound conviction that the world in which we live is God's world and that our identity and purpose can be understood only as part of that creation. At the very centre of the created universe is man, created *imagine Dei*. It is because of this image that Christianity is a religion which attributes infinite worth to each individual, however insignificant he or she may be in the eyes of society. The commandments of Sinai, the Beatitudes of the Sermon on the Mount and the warnings of Jesus were all addressed to the individual conscience. Similarly, the compassion of the Good Samaritan was shown to an unfortunate individual, and not to some discriminated against group or disadvantaged social class. The invitation of Jesus to follow him is addressed to people as individuals, and not as representatives of a particular social class or income bracket.

It is because each individual is created in God's image that we are endowed with a conscience and provided with freedom of action for good or ill: the consequence, of course, is that we are also held personally responsible for our actions. Personal responsibility for our use of time, money, talents, however much or little we may possess, is explicit in the creation mandates and laws of the Pentateuch, as well as in the teaching of many of Jesus's parables, such as the Talents and the Virgins, and also in such well-known stories as those of the rich man and Lazarus and of the wealthy farmer. Most of all, the concept of accountability is at the heart of the idea of a Day of Judgement, which



is fundamental to the Christian view of history.

Although to the Christian, therefore, the individual is possessed of infinite worth – and responsibility and accountability for his actions are the inevitable consequences of being created free – this is not a basis for individualism. Individualism, interpreted as the autonomy of the individual freely to determine his behaviour and values without an obligatory concern for others, is totally inconsistent with the Christian view of God, who is a trinity of persons. The Christian concern with community in society is ultimately a reflection of this fact. Individuals are created to live in community, the most immediate of which is the family. Throughout biblical times, the family was the primary economic unit, so that individual responsibility was exercised in the context of family life, and family responsibility in turn was exercised in the context of the tribe and the nation. I believe that the major purpose of the emphasis on private property rights in the Mosaic law, crystallised in the eighth commandment 'Thou shalt not steal' and categorised in many minor laws in much greater detail, was to provide the underpinning which would enable the individual and the family to live and act with responsibility in society.

Alongside the dignity of man, however, the Christian faith also confronts us with the tragedy of man – egotistical, proud, rebellious, uncompassionate – and the indescribable suffering and injustice which he has caused. It is because of this that the government has the important function not only of preserving property rights and maintaining law and order, but also of dealing with injustice: first, by remedying its causes, and secondly, by helping the afflicted. Throughout the Old Testament the state had a responsibility to look after the disadvantaged. It was not an indiscriminate redistribution of income to the lower paid, but was exercised on the basis of a distinction drawn between the deserving and the undeserving poor, an attempt to help those who were in real need. Again in the Gospels, our responsibility to others is something which Jesus continually emphasised, though it is in an individual and not a corporate context.

Any concept of anarchy, and of a state which is unconcerned with distributive justice, is totally alien to the Christian view. But to advocate the positive benefits which are yielded by these functions of the state is very different from statism.

For in the twentieth century we have witnessed a major assault on the freedom of the individual and the family through the growth of the state. In its most extreme form this can be seen in corporatism

under fascist governments and socialism under Marxist governments. In a less extreme form it can be seen in democratic countries such as our own, in which the relentless growth of government, and the steady drift towards the corporate state, have been coupled with a loss of freedom and a growing sense of powerlessness among individuals and families – very clearly exemplified in the public sector housing projects of the inner cities of our country, the lack of parental involvement and control in state secondary schools, the complaints about the National Health Service, and the sense of frustration of ordinary members faced with militant trades union leaders.

In order to avoid this polarisation of life between the individual and the state, the Christian must surely endorse the development of what Professor Peter Berger (the eminent sociologist) has termed 'mediating structures': that is, those institutions which stand between the individual in his private life and the state – the family, church, school, neighbourhood, the corporation and voluntary associations. A major Christian priority should be to strengthen these structures.

I have great respect for the Bishop of Liverpool and in particular the work which he has done in two of our great cities. But if the powerlessness of individuals in the inner city is at least partly the result of large government and the lack of mediating structures, I cannot understand why he and other church leaders advocate solutions which involve more public spending, bigger government, and our continued acceptance of the increasing politicisation of our lives – all of which tend to *increase* that feeling of powerlessness which he rightly identifies as dehumanising.

It is because the Christian faith has such a high view of the dignity of man, created in the image of God, that it also has such a positive view of work and wealth creation. We have been made not only with a need to work but with a desire to be creative and productive. There is no basic dualism in either Judaism or Christianity, as there is in some other world religions, between the material and the spiritual: there is indeed an explicit reconciliation. This is not to deny that materialism as a creed is the enemy of spirituality. Our Lord's words, 'You cannot serve both God and Mammon', show the irreconcilable conflict between spiritual development and material idolatry.



# Morality

## The criticisms

We have seen that there are four distinct ways of defining monetarism, and we have also seen certain of the insights of Christian theology. It is now time to bring these together in discussing the bishops' critique of government policies.

In the first place, certain propositions associated with monetarism are essentially analysis of how the world works. As such, like all scientific hypotheses, they are open to testing and are ultimately either true or false. Each of the propositions of technical monetarism – the stability of the demand for money, the most appropriate measure of money (M0, M1, M3, £M3), the techniques of monetary control – fall into this category. They are outside the domain of moral and political debate: they have essentially nothing to do with political choices or objectives: they could just as well be held by socialists or capitalists, conservatives or libertarians, Christians or atheists.

Secondly, to the extent that monetarism is interpreted as an ideology, then it is perfectly legitimate for it to be scrutinised by the church on the basis of a Christian world-view. If it were true, as the Bishop of Lincoln has argued, that a certain set of economic theories had been elevated in this country into 'an entire philosophy of life', then I for one would accept the validity of his criticisms. The science of economics is concerned with means in relation to ends but not with ends in themselves. It can provide powerful insights into how markets work, the effects of creating money, and the unintended consequences of interference with markets and excess money creation, which we neglect at our peril. But this does not mean that the most efficient solution is always the best, or that the market should be extended into all areas of life. Because there are certain values which are by nature absolute, I believe that there are certain services which should never be placed on the free market. If monetarism is made into a religion, then the Christian has no alternative but to denounce it as incompatible with the Christian faith.

Between technical monetarism on the one hand and libertarian ideology on the other, and in the third place, is the present government's medium-term financial strategy, which is being implemented in the context of what, for lack of a better expression, I have described as economic conservatism. Because the medium-term

financial strategy is frequently discussed in public by professional economists in a mechanistic way with reference to analytical models and measurements – M0, £M3, PSL2, PSBR – it appears as if this use of monetarism is technical and mechanistic and bears no relationship to any moral concerns. Such, however, is not the case.

## The morality of monetarism

In the first place, monetarism was developed to solve one of the most insidious and cancerous of economic problems – inflation. What is not commonly recognised is that inflation is at heart a moral problem, because inflation is theft. As Keynes so forcefully argued in his *Tract on Monetary Reform*, inflation is a form of concealed taxation. It is a tax levied on the holders of money balances through higher prices brought about by the excess creation of money. If the government through the Bank of England issues a £5 note with the words 'I promise to pay the bearer on demand the sum of £5', signed by the Chief Cashier for the Governor and Company of the Bank of England, but with the expectation, for example, that inflation will proceed at 20 per cent a year, it knows that in terms of purchasing power that note will be worth only £4 one year hence. Similarly, for any individual or group to support inflation – or 'reflation' – knowing (as we must now be deemed to know) that this will prove a covert means of obtaining wealth from others which they would not willingly concede, of reducing debts by cheating lenders and of giving pledges with less backing to them than appears at first sight, is morally indefensible. These are all forms of theft and deception, and their enshrinement at the very heart of the financial system exerts a disturbing and corrupting influence.

It should not surprise us therefore to find that in the 1970s inflation was both a cause and effect of our moral decline in this country. It was a cause in that it strengthened the resolve of monopolies to exercise their power (the most notable but by no means the only one on a world scale being the decision of OPEC to act concertedly over the price of oil), increased the incentive to evade taxes, and helped lead to the nationally debilitating strikes, such as those in the winter of 1973-4, and the 'winter of discontent' 1978-9.

Inflation results in a wholly capricious redistribution of income: from the weak to the strong, from the saver to the borrower, from the pensioner to those still in employment, from the cautious to the speculator. Do those bishops who advocate substantial increases in public spending really want the present – or indeed any – government



to 'cure' unemployment by robbing the weak to pay the strong, by stealing from the pensioner, and undermining the cultivation of at least two of the cardinal virtues? Surely not? Yet this in fact is what is being recommended and, as a result, both the reasonableness and the efficiency of the economic system are undermined.

However, the most insidious and totally unexpected result of the inflation of the 1970s was the rapid rise in unemployment. Although the rising level of welfare benefits, the increased cost to companies of shedding labour, and the costs of enforcing legislation dealing with equal opportunities, must all play some part in the explanation, the high and unstable rate of inflation of the seventies linked to the two oil price shocks of 1973-4 and 1979-80 is the most important factor in explaining rising unemployment.

Control of inflation which was the major objective of launching the medium-term financial strategy or 'monetarism' is, therefore, based on the moral principle that such capriciousness at the heart of the economy is incompatible with justice: not only that, it is difficult to see on moral grounds how any government can be content to consent to a permanent positive rate of inflation, in the knowledge that in issuing currency it is misleading its citizens as to what its 'promise to pay' really amounts to.

There is a second and equally important moral strand in the government's medium-term financial strategy: it is the attempt to move away from the corporate state and to enhance the economic position of the individual in the context of the family. The government's efforts to reduce the power of the TUC and the CBI as pressure groups for large institutions, and to limit the power of the state in general in order to increase the power of the individual – by, for example, changing trade union laws; by the sale of council houses to tenants, by the privatisation of companies such as British Telecom and the sale of shares to its employees, and by providing stronger incentives to establish small businesses – all contribute to this objective.

Underlying these policies is a moral concern: to encourage and develop private ownership by families, whether of their own homes or of the firms in which they work, and to enable people to pursue their jobs free of the restrictions of monopolistic trade unions. As such they constitute a fundamental step forward in the creation of a more responsible and healthy society.

Far from being immoral, the monetarist policies of the present government are, therefore, an expression of profound moral concern.

Recently the Rev. Professor Peter Baelz, Dean of Durham, described a Christian morality as one concerned with creating 'a just, sustainable and participatory society'. It is an expression which sums up admirably the belief which underlies economic conservatism.

The policy is just or fair in that it attempts to remove inflation, to allow a greater proportion of earned income to be retained by those to whom it accrues, and to remove monopolies and restrictive practices in the labour markets, in the City and in services generally. Unlike the experience of the 1970s when the growth of government spending and of money supply outstripped the growth of real output, the policy is sustainable in so far as inflation and the growth of government are now under control, the recovery of the economy is entering its fifth year and, barring external shocks or domestic monetary and fiscal mismanagement, looks likely to continue. The one element which is not sustainable is a permanently high level of unemployment: to that I shall return later. However, not only is the policy just and sustainable, it is also participatory. It is not participatory in the sense of accepting the politicisation of economic life, of supporting the development of the corporate state – but rather it is an attempt to encourage direct participation of individuals and families in the economy, through ownership.

### Objections

It is now time to deal with some objections to the case I have argued.

One argument is that the present policy of sticking to the target numbers of the medium-term financial strategy is too rigid, too cautious, too unprepared to take the risks necessary to reduce unemployment. It is an approach which is epitomised by the recently launched *Charter for Jobs*, which recommends increased public spending on infrastructure and health, a cut in employers' national insurance contributions and, if inflation begins to accelerate, the imposition of a comprehensive prices and incomes policy. Increased inflation is better, so it is argued, than 'doing nothing to reduce unemployment'.

Present policy is regarded by the signatories of the *Charter* as deflationary, and as the main cause of the increase in unemployment since 1979. They point to the low level of the government budget deficit relative to the crisis years, 1974 and 1975, and to the increase in the average personal tax burden. In doing so, they fail to allow for the fact that North Sea oil tax revenues should properly be excluded from any



comparison with earlier years. Once this adjustment is made it is clear that the 'onshore' PSBR has been and remains very large by historical standards. Then, they ignore the fact that post-tax real earnings have grown by an average of over 1½ per cent per annum over the last five years. Increased personal taxation has merely trimmed excessive wage increases.

This tendency for real wages to rise more rapidly than labour productivity across the whole economy is at the heart of our economic problem. Prior to 1982, unit labour costs in the UK were rising very much faster than those of our overseas competitors. During the past three years this pattern was reversed, at least for manufacturing industry, but the tide has recently turned again. Lack of overseas competitiveness has not been the only consequence of above-average unit labour costs. Over the past ten years corporate profitability, measured by the real post-tax return on equity employed, plummeted by 1982 to an all-time low.

The profits recovery that has occurred over the past three years has restored the incentives necessary for increased output in many industries. If the advocates of reflation and 'job guarantees' had had their way, higher wage and price inflation would have aborted the private sector profits and output recoveries at an early stage. Worse still, the inevitable expansion of job guarantees would quickly lead to a planned economy.

However we wish to label the *Charter for Jobs*, it turns out to be nothing more than a concerted demand for reflation linked to an incomes policy. If this was a novel idea, it might be worth experimenting with. But demands such as this have been made many times during the past few decades, and the last three reflations give clear evidence as to the likely effect of their implementation.

If we define a period of reflation as a time when the PSBR rose sharply in relation to nominal GDP and remained at this level for at least two years, then the last three reflations, which occurred in this country were in 1966-7, 1973-4 under Mr Heath, and 1978-9 under Mr Healey. The effects of reflation have been unambiguously disastrous: unemployment, inflation and interest rates were all higher after the reflationary process than before. Although reflation may have had initial successes, such as reducing inflation in 1966-7, unemployment in 1973-4, and interest rates in 1978-9, these were all temporary.

On the basis of this evidence there is no reason to think that another reflation would be different. If public expenditure or taxes

were increased and the PSBR rose sharply, interest rates would rise, the pound would fall and the money supply targets would be under great pressure. Uncertainty as to the future rate of inflation and growth would increase, investors would lose confidence in the UK economy, and the nation would once again find that the road to hell is paved with good intentions and trodden by some of the most humanitarian people imaginable.

The other major objection on which I should like to focus concerns the attempt by the government to strengthen the market economy, the workings of which are described by the Bishop of Durham as 'individual selfishness and organised greed' and 'materialistic individualism'.<sup>7</sup> The triple charges of individualism, selfishness and materialism are not new: indeed they have a distinguished intellectual pedigree from Ruskin through to T S Eliot.

It might be that by the absolute standards of the Gospels ours is a society of selfishness, greed and materialism. But these were also criticisms made by Jesus of first-century Palestine and by Amos, the prophet, eight centuries previously. Their societies could hardly have been described as market economies as the expression is used today. Selfishness, greed and materialism are the consequence of sin, not of particular economic systems. Materialism as a way of life is certainly not confined to capitalist economies.

Similarly, the charge of individualism is misplaced. The market place depends on trust, especially here at the very heart of capitalism, the City of London. Trust can only flourish within a community. More than that, the most distinctive institution of the market economy, the private company, is in fact a body corporate. I believe that at the root of this attack is a confusion between philosophical individualism, which is an attempt to analyse the social order by reference to the individual rather than the collective, and the practical workings of the market economy.



## The way forward

There remains one fundamental issue connected in the minds of many with monetarism, which I have not yet confronted: unemployment. The present level of unemployment can be divided into two parts: that which is transitional and will be eliminated through the normal workings of the labour market (even though the length of this process may be intolerably long, due to the inertia built into the system through existing institutions and conventions); and that part, sometimes referred to as the non-accelerating inflation rate of unemployment (NAIRU), which is compatible with stable inflation.

The NAIRU should not be thought of as a fixed number. From a base of about 3 per cent, or  $\frac{3}{4}$  million people in the 1950s, the NAIRU has risen to between 9 and 12 per cent, or between 2.2 and 3 million people, according to various estimates. A significant part of the increase has been due to the acceleration of the pace of structural change following the two oil-price shocks.

This level of unemployment is not the result of any law of economics but simply of institutional practices in the labour market. Unemployment at this level, however, is intolerable in human terms and clearly must be addressed by policy makers. It cannot be changed by reflationary policies or even by achieving a policy of price stability. It can be reduced by reforming the institutional practices of the labour market.

The present policy of the government is to persist with the medium-term financial strategy and firmly to reject any calls for reflation, while simultaneously introducing a number of measures to alleviate the problem – especially for young people – and to improve the efficiency of the labour market, by means of the reform of wages councils, the abolition of the national insurance surcharge, and by the reduction of national insurance itself. As a result of this policy, inflation has fallen dramatically from its 1979-80 rate and has remained at roughly 5 per cent per annum, recovery has proceeded for the past four years, the rapid growth in unemployment has been halted, and employment itself has grown by 600,000 over the past two years. With the prospect of inflation remaining under control and of continued recovery in the economy, it is probable that unemployment will start to fall.

One alternative to the present policy would be to introduce some form of incomes policy which effectively depresses wages and so prices

people back into work. To be politically feasible, it would probably have to be accompanied by some reflation. The problem with such a policy is, as I have shown: *one*, the risk of inflation; *two*, the ultimate failure of all such policies ever since Stafford Cripps in 1948; and *three*, the damage it would cause to the workings of the market economy through creating random shortages in certain skills, and arbitrarily influencing the profits of certain firms.

I believe that the government is fundamentally right to stick to the policies of the medium-term financial strategy. Nevertheless, the estimate of NAIRU is unacceptably high in both human and economic terms. Monetarism is not equipped, and indeed was not designed, to deal with the problem of high structural unemployment. Monetarism was developed to deal with the problem of inflation. Through controlling the money supply our success in reducing inflation has been dramatic. But if unemployment is to be tackled then I see no alternative to radical institutional reforms in the labour markets.

One route would be to confront head-on the problem of trade union privilege embodied in the 1906 Trade Disputes Act, by repealing it. Another, and conceivably less confrontational route would be to deal with the problem through profit-sharing and new forms of ownership in industry. The basic problem with the present trade union structure in this country is the system of national collective bargaining carried out by monopolistic institutions. But an equally important problem with many of our large companies is that they have succeeded in insulating their staff, especially managerial staff, from the direct risks and rewards of the market place. Many of our most prestigious companies have effectively become mini-welfare states. If as a nation we are to meet the challenge posed by present unemployment, then it is just as essential to change the incentive structure for management in large companies in order to encourage enterprise, as it is to change the monopolistic behaviour of trade unions.

One method by which the security of trade union membership and the security of managerial employment in large companies could be reduced is by relating a significant proportion of the pay of workers and managers directly to the firm's performance. As a consequence, enterprise would be rewarded directly, and the problem posed by the failure of wages to respond quickly to changed market conditions (for example, in a recession) would disappear. Pay would fall during a recession for employees and management alike, but on the other hand people would not find themselves being made redundant. During a



recovery and boom both employees and management would benefit with the recovery of the markets.

At the same time, I believe these changes need to be linked to a major initiative for wider share ownership in British industry, which would reinforce the involvement of all staff with the performance of their companies.

I am certain that these kind of proposals would have wide appeal. Without financial incentives, however, they are unlikely to come about. What is necessary is for the government to take the initiative and for the Treasury to introduce preferential tax treatment for all firms which implement the proposals. The advantages would need to be sufficiently attractive financially for existing trade union members and managers to campaign for the necessary changes in their respective organisations.

## Conclusions

Let me now conclude this lecture. *First*, I have tried to show the complexities of the term 'monetarism' and the ways in which it is used and misused in public debate. If monetarism is to continue to be the subject of attack, especially from a moral position, then both the object and the grounds of the attack need to be made much clearer and more explicit. *Second*, I have shown that the medium-term financial strategy of the present government is not the apotheosis of Adam Smith's principle of the invisible hand, but has a strong moral basis – both in tackling inflation, and in attempting to reduce the power of the state as a step towards redressing the powerlessness of people. *Third*, I have argued that monetarism can solve, and indeed has largely solved, the problem of inflation. But monetarism cannot solve all our economic problems. It was not designed to solve the problem of long-term structural unemployment. A stable and low rate of inflation is a necessary but not a sufficient condition to reduce unemployment. This can be achieved partly by changing incentives: but it will remain serious and continue to be a problem until there are major institutional reforms in the labour market. I believe that as a nation this is the major problem on our present economic agenda, and that it will remain so until it is squarely faced.

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Meanwhile, however, there is one issue on which the church is remarkably silent, yet I believe it to be one of the greatest insights of the Judaeo-Christian faith in the economic field.

Over the past few decades we have seen the secularisation of our society proceed at a rapid pace. The spirit of our age is one of creativity, spontaneity and freedom; with little acceptance of authority, tradition or rules. Religion in a traditional sense, and the traditional values of the religious person, have been set aside. The ideas that money creation should be fixed by reference to some external standard, that budgets should be balanced, that one should accumulate savings rather than borrow from banks to finance increased consumption, that saving is a good thing in itself, that in terms of personal lifestyle modesty or even frugality is the ideal, and that work should be seen as a calling, to most people seem strange, quaint and rather old-fashioned.

In many parts of our society the consequences of secularisation are all too apparent. One need think only of the statistics of family breakdown, crime, violence, drug abuse and alcoholism. There are many ways in which what the Bishop of Lewes recently described as 'the desire for more' can have an unsettling and harmful effect on economic life in the longer term. Nor can I believe that our economic problems are unrelated to our more general social problems, nor that they are unconnected with secularisation.

It is in addressing this issue that the spiritual impact of the church today seems at its weakest. We are this evening in a livery hall very close to the place commemorated by a plaque where on 24 May 1738, it says that John Wesley found his heart 'strangely warmed'. We are all, I trust, aware of the impact of that clergyman on the economic and political life of this nation. Economics is familiar with the concept of unintended consequences; if the church is really to have an impact in the creation of a just and united country, perhaps it should ask itself whether it too has not succumbed to the process of secularisation, and whether its best contribution might not be to proclaim those eternal verities which it is its unique duty and privilege to guard.

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- 1 *Hansard*, House of Lords, 13 November 1984
- 2 *The Times*, 8 October 1984
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- 7 Rt. Rev. Prof. David Jenkins, Bishop of Durham, Hibbert Lecture, *The Listener*, 18 April 1985
- 8 *Church Times*, 7 December 1984
- 9 This view was not unanimously held: among politicians the resignation of Thorneycroft, Powell and Birch from the Treasury in 1958 and the establishment of the Radcliffe Report reflected an unease over Keynesian orthodoxy.
- 10 This is derived from *Perspectives on Economics*, and was originally taken from a statement of the World Council of Churches.



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