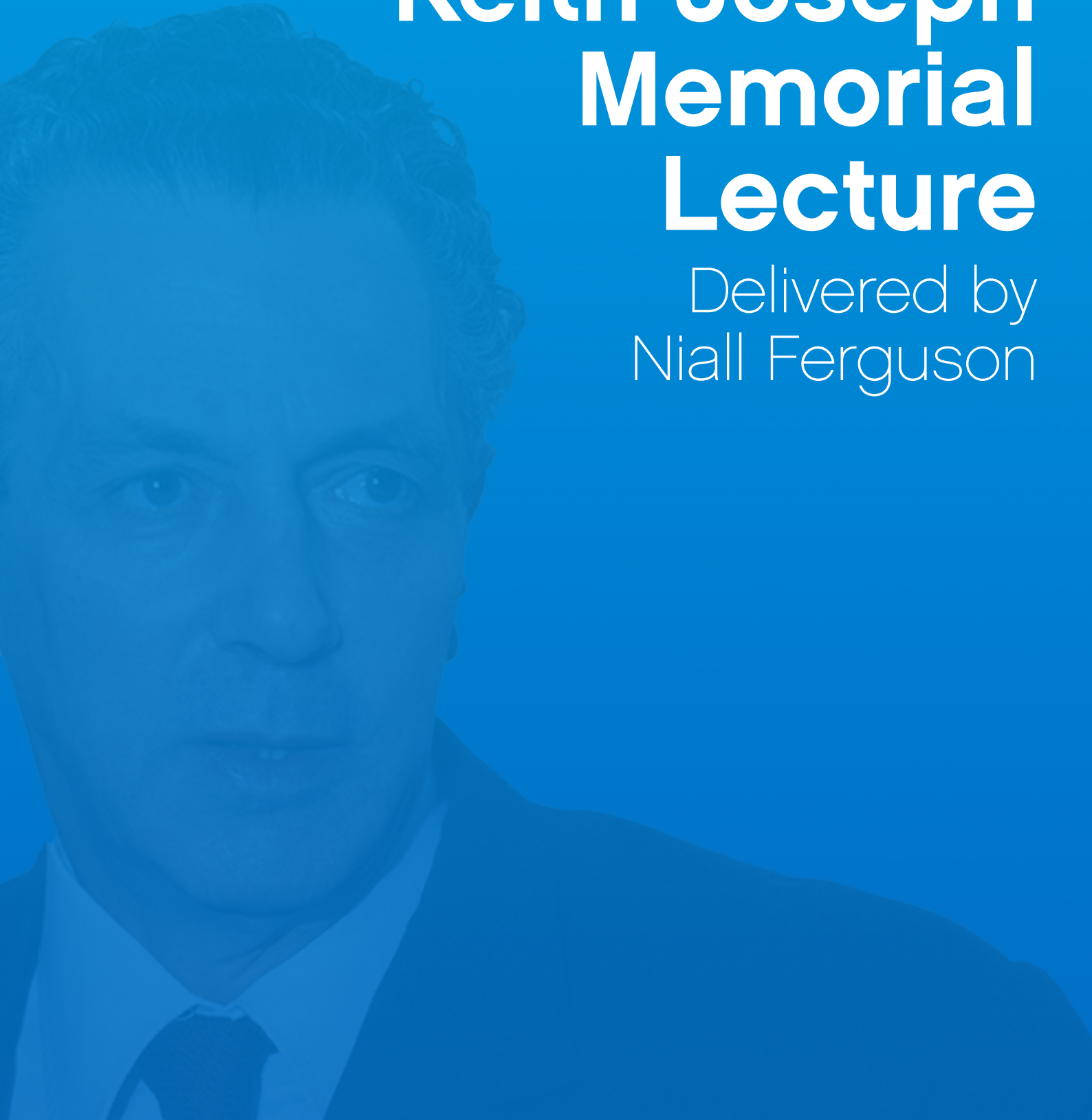




2023 Keith Joseph Memorial Lecture

Delivered by
Niall Ferguson



Back to the 1970s?
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What I am going to say tonight will not make me very popular. So let me apologize at the outset to my friends in the current government.

I saw many of them at Hampton Court on Monday, and listened with interest as they made the case for investing in Britain to an audience of foreign investors. They did a good job—a very good job. And I am not here to disagree with anything that was said on Monday about Britain as a destination for international capital. Still, I did find myself looking at my shoes on more than one occasion—and remembering how those feet felt five decades ago.

The soaring price of school shoes gave me my start in economics. My first-ever publication was a letter on that subject to the Glasgow Herald in 1974, when I was 10 years old.

Retail price inflation in the UK ultimately exceeded 25% in late 1975. Britain's experience was not the worst in the OECD—Portugal and Spain were worse—but it was pretty bad.

The roots of the inflation were partly monetary. The annual broad money growth rate exceeded 20% in 1972 and 1973. The Bank of England hiked rates in 1972 and 1973, but victory was declared prematurely and rates were cut in 1974, 1975-6 and 1977.

The roots of the inflation were also partly fiscal, with a succession of government deficits in excess of 4% of GDP.

Growth was also slower than in peer countries. It averaged below 2%, worse than most of the big European economies.

For investors, the 1970s were the worst decade since the 1910s, with negative real returns on both equities and bonds. Real returns on

stocks were terrible. Adjusted for inflation, the FT All-Share Index from 1974-79 sat at less than half its 1972 peak. And there was a housing bubble and bust.

What made the Seventies in the UK so much worse than in most developed economies?

I am afraid part of the blame lies with a Conservative government. With Ted Heath at the helm from 1970 to 1974, there was excessive fiscal stimulus, which led to the short-lived “Barber boom.” There was too-loose monetary policy: Competition and Credit Control by the Bank of England; the lifting of ceilings on bank advances; the breakup the high street banks’ cartel; a new reserve asset ratio rule. There was the relaxation of controls on property development and the abolition of the Land Commission, which Labour had established in 1967 with the seemingly contradictory goals of supplying land for development and imposing a “betterment levy.”

The bust that followed the boom was a rather familiar kind of financial crisis as novel financial institutions—SCOOP, London and County Securities, Cedar Holdings, Triumph Investment Trust—had to be rescued. The Bank of England had to buy five firms, including Slater Walker Ltd., and bail out the Crown Agents.

The Labour government elected in 1974 and led by Jim Callaghan after 1976 therefore inherited a considerable mess. It is often forgotten that the first effort to impose monetary discipline was by Callaghan’s Chancellor, Denis Healey. But, as Keith Joseph pointed out, monetarism was not enough.

All this explains why “Crisis, What Crisis?” was such a terrible headline for the Labour government in early 1979—though what Jim Callaghan actually said was: “I don’t think that other people in the world would share the view [that] there is mounting chaos.”

The reason those words rang hollow was that middle-class families were being hit painfully hard from all directions. “You can’t realize how near we are to catastrophe,” the historian A.J.P. Taylor wrote to his wife in July 1974. “Many serious judges think that all our banks may close their doors in a few months’ time. Prices have doubled within the year and are going up faster than ever. My income does not go up. Indeed, it gradually goes down.” Always a radical, never a conservative, Taylor was my hero when I discovered history. It rather shocked me to discover how much the 1970s had impoverished him. For him and many like him, it was one of the great mass muggings by reality of the modern age.

Keith Joseph’s 1976 lecture, “Monetarism Is Not Enough,” was a paradigm-shifting response to this very real crisis. In part, the lecture was a clever (and I think correct) critique of Milton Friedman’s dictum that inflation is always and everywhere monetary in origin.

“I have dealt with inflation, so far, as a monetary phenomenon;” declared Joseph. “It is other things besides.” The distinction Joseph drew was “between those economists who believe that monetary policies should be used to tackle monetary problems on the one hand and those on the other hand who believe that monetary policies can master non-monetary problems – such as union obstruction, lack of skills, overmanning, housing rigidity, lack of confidence – and non-monetary policies – like control of wages, prices and dividends – can master the monetary problem of inflation.”

For Joseph, “monetary control” was just a starting point. It was “a pre-essential for everything else we need and want to do; an opportunity to tackle the real problems – labour shortage in one place, unemployment in another; exaggerated expectations; inefficiencies, frictions and distortions; hard-core unemployment; the hundreds of thousands who need training or retraining or persuading to move.”

“Monetarism Is Not Enough” was also a critique of government fiscal policy. “Nearly two-thirds of our national activity flows in some way from the government,” lamented Joseph. In a footnote he noted that total

public sector expenditure in 1974 amounted to 56% of GDP. (This was actually a miscalculation; more on that later.) “Whereas cuts in public expenditure rarely eventuate,” he complained, “squeezes on the private sector are ‘for real’. The interest rate is increased, bank lending is contracted, taxes are raised, other old-fashioned deflationary measures are used. The private sector is punished for the state sector's profligacy.” His recommendation was “cuts in state spending” and “detaxing and the restoration of bold incentives and encouragements to business and industry.”

But Joseph's lecture was a critique of big government more generally: our socialist anti-enterprise climate: indifference, ignorance and distaste on the part of politicians, civil servants and communicators for the processes of wealth-creation and entrepreneurship; high taxation; very high marginal rates of taxation; perhaps most important of all – increasing capital taxation on the makers of wealth – whether self-employed, small, medium or large. ... By taxation, by inflation, by the remorseless flood of regulations and legislation, by controls and by the constant and arbitrary interventions of authority, successive governments since the war have cumulatively taken away both the pleasure and the rewards that once made risk-taking worthwhile. “In order to deal with the state bureaucracy,” Joseph went on, “the man-made environment of licences and permits, planning permissions and regulations, grants and write-offs, premiums and taxes, forms and forms and forms, business has become increasingly bureaucratized.”

Labour was of course in power in 1976 and had been for two years. Yet Joseph acknowledged that the country's situation was not only Labour's fault. And—importantly for my argument tonight—he offered an historical explanation of why Conservatives had mostly gone along with the various policy errors he had described. He condemned the post-1919 decision to return to the gold standard at the pre-war parity at a time when too-powerful trade unions made it impossible to restore competitiveness by deflationary methods. The Second World War had “further increased the actual role of the state, but also increased belief in the efficacy, indeed the virtual omniscience of state

intervention.” And Conservatives had also been responsible for “encouraging or at least justifying mass immigration of workers first from Commonwealth, later from non-Commonwealth third world countries on grounds of labour shortage.”

I believe that for future historians the great puzzle of the 2020s will be this: Why did a Tory government—if the singular is appropriate when we have had five prime ministers in 13 years, three of them in the last 15 months—end up unintentionally repeating at least some of the mistakes of the past?

Let me specify what I mean. In 2022 inflation surged into double digits on the back of broad money growth that exceeded 15%. And that year was not an aberration. Since 2010, the UK has had the highest inflation of the G7 countries. If one takes the 38 OECD members, 16 have had higher inflation rates since 2010, but the eight European Union members in that group are all former Eastern Bloc economies, with the exception of Austria.

The UK government deficit, which was on a downward path 2010-19, surged to £300bn in 2020. Relative to GDP, UK fiscal expansion was second only to that of the U.S. in the pandemic years 2020 and 2021. Net debt is now 98% of GDP, compared with 67% in 2010. The best that can be said is that Japan and Italy are worse and the U.S. is overtaking us.

Meanwhile, “real GDP grew by an average annual rate of 0.2% between 2020 and 2022, compared to 1.3% between 2008 and 2019 and 2.7% between 1998 and 2007.”

The most recent figures from the Treasury recall the dark days of the 1970s. “Figures for 2020-21 show [public spending relative to GDP at] the highest percentage (53.1%) in the period [since] 1999-00.” You will remember that Keith Joseph thought the figure in 1974 was roughly similar: 56% of GDP. In fact, using a [consistent measure](#), it was 42%. Today it is 44.8% of GDP. In 1990, at the end of the Thatcher era, the

figure was just 30%. Moreover, according to the Office for Budget Responsibility, “Net interest payments [rose] to 3.8% of GDP in 2022-23 – the highest since 1981-82.”

Saying that the fiscal trajectory of the United States is even worse is not consoling. The U.S. has the world’s principal reserve and transaction currency. A smaller proportion of the federal debt is index-linked. Indeed, at 25% of total debt, the UK has the highest index-linked debt burden of any G7 member, twice the Italian share. The “shortening in the effective maturity of the consolidated liabilities of the UK public sector” since the financial crisis from seven to two years has increased the UK’s vulnerability to higher interest rates.

And the UK also has the largest current account deficit in the G7. A “growing share of UK government debt ... is in the hands of foreign private investors,” up from 13% (2004) to 25%. Within the G7, only France’s share is higher. And “private sector buyers will need to absorb an average of 6.5% of GDP in new borrowing each year between 2023-24 and 2027-28, more than twice the post-financial-crisis average.” The “nasty fiscal arithmetic” when your real borrowing rate exceeds your real growth rate is not to be lightly dismissed.

The 1970s in fact had significantly smaller fiscal problems than these. But the problems of the 2020s may pale into insignificance alongside those of the 2070s, if the OBR’s recent projections are to be believed.

Meanwhile, taxes as a share of GDP are at a higher level than in the Seventies. Indeed, they are on track to match their peak in 1948. Immigration has surged, so that foreign-born workers are now 19.4% of all workers. Real household disposable income per person has contracted in five of the last 12 years. And the UK now relies on imports for between 30 and 40% of its total energy supply, a level last seen in the early 1970s, even as gas and oil prices rally.

Let me be put it bluntly. To a greater extent than is true of peer countries, Britain seems to be in danger of repeating the 1970s—rather

like one of those meticulously produced period dramas at which the BBC used to excel. This is very striking to a man of my generation, who has lived and worked for most of the past 20 years in the U.S. Not only has inflation made a comeback; not only are our public finances in a deeply concerning state. There are also larger shares of the working-age population out of employment than should be the case. Without being so funny, elements of the far left on certain university campuses recall Robert Lindsay as "Wolfie" Smith. Immigration is on its way back to being a wedge political issue again. And strikes are back as a feature of British life. Even public attitudes have reverted to new versions of "Oh well, mustn't grumble" and "Typical, innit?" when things don't work or the car hits a pothole.

And this is after more than 13 years of Tory rule! What on earth will it be like when Labour gets back in, under the leadership of man who advertises his admiration of Harold Wilson?

These are uncomfortable realities. It gives me no pleasure to spell them out. And their political implication is unpleasant, too. I fear that Brexit—undoing what was done in 1972-73, when Britain joined the European Economic Communities—will increasingly be judged a failure if its net result seems to be turning back the economic clock by fifty years.

So why, we must ask ourselves, did the Conservatives get into this economic predicament?

There are three conventional answers to this question.

1a) Brexit was not executed in the way envisioned by the proponents of a more liberalized economy—or 1b) Brexit was always bound to be much more costly than Vote Leave claimed.

2a) Covid was a terrible stroke of luck—or 2b) Covid was bungled by incompetent ministers or public health officials (or both).

3a) The Russian invasion of Ukraine was a bolt from the blue—or 3b) the United States and its allies first failed to deter Vladimir Putin from invading and then failed to bring the war to a swift conclusion after he failed to take Kyiv.

All of these belong to the Harold Macmillan school of historiography. They are “events, dear boy, events.” Note that two out of three of these events happened to other countries, too.

I would offer instead an explanation in the spirit of Maurice Cowling, one of the other great sages of the Thatcherite revolution. When I moved to Peterhouse in 1990 to take up first teaching post, I came much under Maurice’s influence and learned a great deal from him. And trying to answer the question—“How did we get here?”—sent me back to his three seminal studies of British high politics.

Permit me to treat you to some Cowling quotes that give a flavour of his brilliant, ironical mind. It should be noted that Maurice had a peculiar unholy trinity that he sought in his students: the combination of “irony, geniality and malice.”

From 1867

- “... the Reform bill of 1867 [was] an incident in the history of party ... its substantive merits as it was eventually passed were given prior discussion ... neither in Parliament ... nor in the Cabinet ... The deployments of principle [were] ... assertions of individual and party opinion and personal and party power in a battle—as private as it was public—not just to establish the best constitution but to decide who should establish it. ...”
- “Conservative governments were not the governments of the Conservative party, but the governments of Peel or Derby or Salisbury ... knives were never so far below the surface that a victor could ignore them. ... statements made, or actions taken, by any participant must be scrutinized, not as expressions of belief, but in their logical place in the chronological sequence.”

- “Between the closed world in which decisions were taken and the external pressures it reflected, the connections were so devious and diverse that no necessity can be predicated of the one in relation to the other. Between the inner political world and society at large on the one hand and between personal and policy objectives on the other, no general connection can be established ...”¹

From The Impact of Labour

- “Europe, Russia, Ireland, India and the Empire will be treated in the way politicians treated them—as incidents in the history of what was taken to be the central domestic problem. ... The political system consisted of fifty or sixty politicians in conscious tension with one another whose accepted authority constituted political leadership. ... High politics was primarily a matter of rhetoric and manoeuvre.”
- “Without understanding the perpetual nature of these motions, one can [not] ... understand the extent to which they were moved by antipathy towards their rivals. Antipathy, self-interest and mutual contempt were the strongest levers of action.”
- “The key lies in the minds of politicians who exercised ostensible power and in the relationship they envisaged with the society they wished to rule. ... we posit the existence of a network of plebiscitary demagogues whose ... chief purpose was to jostle each other as they picked their way through the limitations imposed by all these forces to a position of creative sympathy with an unknown public.”²

From The Impact of Hitler

- “principles are manifestations of personality more than interests or passions and ... all three form the context of political consciousness. ... foreign policy became central because politicians could fit it into the political battle which had begun in the 1920s. ... the domestic appeasement of the twenties was assumed in order to attack the the international appeasement of the thirties. The result was an alliance between a class-conflict

programme in the Labour Party and an international conflict programme in parts of the Liberal and Conservative parties.”

- “Halifax [was] ... the embodiment of Conservative wisdom, who decided that Hitler must be obstructed because Labour could not otherwise be resisted. ... [But] it was neither morally obligatory nor prudentially self-evident that Hitler should be obstructed in Eastern Europe.”
- “As a centre coalition, the government of May 1940 ... [left] it uncertain whether it was a Lib-Lab trap for Conservatives or a Conservative trap in which Attlee was the victim ... Through Churchill, Sinclair, Attlee and Eden ... and through Butskellism ... it lasted until Macmillan’s retirement, establishing inflation, disestablishing the Empire and permitting a receptivity in which the central features of Labour thinking became entrenched as normal.”³

All of this suggests a Cowling-esque answer to my question, how did the Conservatives get into this economic predicament?

Simon Kuper’s amusing book *Chums* ultimately misses the point because he has not read Cowling. The Tory leadership elite, largely focused on the complex game of high politics and ascending the greasy pole, taking it in turns to be prime minister, forgot that inflation is always and everywhere a political phenomenon. Brexit was pursued primarily as an instrument of party-political competition and only secondarily—if at all—as a solution to Britain’s economic challenges. Indeed, it was presented to voters as a free lunch, which, as a divorce, it was never likely to be.

The political elite then collectively decided that big government was needed in a public-health emergency—and might even be a vote-winner after the pandemic, as it had been beforehand (remember the bold spending and “levelling up” pledges of the [2019 manifesto](#)?). In doing so, they set aside not only the principles of fiscal responsibility but also, in the panicked embrace of blanket lockdowns, of limited government itself, a mistake that most, though not all, democracies

made. They thus unwittingly repeated the mistakes of the post-war Tories in believing the world had changed and that they, too, must move with the times.

Now, it is possible that Britain will avoid a repeat of the 1970s. I kept wanting to believe what I heard at Hampton Court on Monday. But the same foreign investors had presumably heard somewhat similar blandishments from members of the shadow Cabinet. One characteristic feature of the 1970s was that the parties took it in turns not to deal with country's fundamental monetary, fiscal and structural problems.

If the polls are right, and if Labour does come to power next year, then we shall really have our work cut out for us.

For, as Maurice Cowling long ago observed, Labour always has represented and always will represent a genuine ideological challenge to the established social and institutional order.

They really believe in big government. They really believe in higher public spending. They really believe in raising direct taxes.

That is why keeping them out of power has been such a very difficult challenge for Conservatives for more than a century.

That is why Conservatives need—regularly—the kind of reminder that Keith Joseph provided nearly 50 years ago. No matter what your shoes may cost, my ministerial friends, you need to be kept on your toes.

Notes

¹ Maurice Cowling, *1867: Disraeli, Gladstone and Revolution: The Passing of the Second Reform Bill* (Cambridge University Press, 1967), 2-6, 340.

² Maurice Cowling, *The Impact of Labour, 1920-1924* (Cambridge University Press, 1971), 3-12.

³ Maurice Cowling, *The Impact of Hitler: British Politics and British Policy, 1933-1940* (Cambridge University Press, 1975), 1-10.