

BRITAIN

British industry gags on Tory medicine

Despite sterling's descent from its high of \$2.33, little relief can be expected for British industrialists whose groans over the effect of a strong pound on export profits have become more audible than usual lately.

The just-published quarterly survey of industrial trends put out by the Confederation of British Industry highlights the worst decline in export confidence since such questions were first asked in the late 1950s. The gloomy forecast is largely linked to government policies which have promoted a strong pound to the

detriment of exporters' price competitiveness and have squeezed company liquidity by jacking up interest rates to 14-15%, with no end in sight. Unlike Japan, British industry has no reservoir of technological capacity on which to rely to compensate for the pound's strength.

The CBI survey, which represents the polling of 1,891 firms in 44 different manufacturing sectors, concludes that optimism about the general business climate in British industry has "deteriorated to a significant extent" and is not expected to improve any time in the near future. High interest rates and the damage resulting from sterling's strength are squeezing company profits enough to choke off future capital invest-

ment, says the CBI. It forecasts the rate on industrial investment this year at "no more than 3 percent" which, it says, will hardly encourage new capital outlays.

These results from the first CBI survey since the election of Mrs. Thatcher stands as a stark comment on the Tory Government's economic policies, which were specifically designed to spur incentives in industry and boost "free enterprise." The increased industrial activity of the past few months is shown by the survey to have been only a temporary phenomenon, due mainly to business recovering from last winter's strikes. Current buoyant prospects for orders are seen as short-lived as business confidence slumps further, costs increase and the pound remains overvalued.

British companies that depend on exports suffer when the pound rises in value, as it makes their products more expensive in other currencies.

FOREIGN EXCHANGE

The vulnerabilities of the pound sterling

Behind sterling's dip in the currency markets the week of July 30-August 2 remains the basic fact of its overvaluation. In the near term, the pound will hold up; the 6 1/2-cent drop in its dollar rate July 31 appeared to reflect profit-taking and related adjustments rather than any deep reaction to Nigeria's nationalization of its British Petroleum holdings; and the City of London expressed satisfaction that the July 14 \$2.32 peak had been trimmed.

The volatile sterling forwards were at a discount Aug. 2, amidst continued statements from London that the pound's strength is unwar-

ranted. Lord Shawcross of London and Continental Bankers has projected a \$2 pound; Barclay's New York traders see it holding at the \$2.30 level until late fall when, they say, a miner's strike and other challenges to the Tory government could mean a return to 1974's three-day week, power blackouts, and chaos.

All of this has been basically pre-discounted, and meanwhile the Thatcher government is refusing to make concessions either to the U.K. exporters who are screeching about being priced out of the market, or to a broader array of businesses hit by the high cost of credit. Last week Barclays announced that it expects rates to move even higher—because of continued borrowing demand—softening both long and short-term

gilts prices. Finance Houses Association members proceeded to raise their commercial and industrial lending rate by 1 percent to 14 percent, while Thatcher's Trade secretary told exporters that they shouldn't depend on a cheap pound for their sales.

As Barclays commented to *EIR*, British manufacturing is in such terrible shape that even softer credit and a trade-worthy sterling rate wouldn't help matters all that much. Without North Sea oil, they added, sterling would be below \$1.25 today. And indeed, oil remains the key to the rigged pound overvaluation, one which London expects will keep a floor under sterling, and thus under its own pretensions to do more than juggle other people's money.

Deeper vulnerability

This brings us to sterling's deeper vulnerability. The Tory government announced last week that it was post-

The mighty Imperial Chemical Industries—bellweather of British manufacturing industry—had already started complaining when the pound rose to \$1.90 in the spring of 1978. As it went to a four-year peak of \$2.33 last week, ICI's new chairman told reporters: "We are now in real pain. But we have to live with it." The chairmen of British Leyland and Courtaulds, the large textile concern, echoes these sentiments, stressing the "drastic" effect of the pound's strength on future export margins.

Factory closures are now beginning to occur which are directly attributable to the overblown British currency. A frozen food factory in Lancashire, which used to export three quarters of its output to Germany, put up the shutters and sacked 80 employees because, according to the directors, the rise of sterling had priced them out of the market.

Conservative Party spokesmen

say they regret that the high pound is hurting exporters, but they are determined to let "market forces" determine the currency's value. Treasury officials say they won't compromise their new domestic economic programs, such as tight control over the money supply through high interest rates, to bring the pound's value down. They are pleased as punch that the pound sterling is now considered a "petro-currency" and are even entertaining notions of joining OPEC, according to continental sources. "A strong pound is like a mirror," said one government official. "We may not like the way we look, but it's better to see yourself the way you are."

Business spokesmen in Britain are not about to challenge the basic economic assumptions of the Tory government. Sir Ray Pennock, senior deputy chairman of Imperial Chemical Industries and president-elect of the CBI, said industry would

have to "learn to become more efficient" so as to survive with the present policies. "Industry should not moan and wring its hands," he told reporters. "It should say it is a rough situation and will have to learn to deal with it." According to press reports, the Confederation of British Industrialists will refrain from pressing ministers for any policy changes and will instead urge the government to spell out the need for wage restraint, a certain recipe for confrontation with the unions.

—Marla Minnicino

poning its decision on whether to join the European Monetary System (EMS) FROM Mid-September to late October or November, because the Bank of England fears pegging the pound into the EMS's fixed currency grid at an unviably high rate. But this raises questions beyond a delay until labor unrest shaves down sterling.

First, whether or not the Nigerian nationalization was a serious blow to BP and Britain, the fact remains that significant elements of the Commonwealth are up in arms against the Thatcher government's policies, and might go so far as to divest sterling and reorient important trading arrangements toward continental Europe. The same is true of major Arab sterling holders. Second, and this is the crucial question, if the EMS accelerates its moves to activate a gold-backed monetary arrangement and draws oil-producers into it, Britain would get a double

whammy. Poor in gold reserves, it would also be faced with the economic underpinnings of such an entente—a level of state-to-state, tolerably priced, guaranteed oil supplies for Europe that would clamp down BP and Royal Dutch Shell's speculative operations; and a level of energy exploration, development, and nuclear power proliferation that would return North Sea output to its rightful marginal, cost-ineffective status.

On the dollar, meanwhile, the July 28 *London Economist* ran a clinically accurate assessment of the prospects for Paul Volcker's "strong dollar" credit crunch in an article titled "The dollar falls." The *Economist* asserted that the dollar is headed for pre-November 1978 lows; a U.S. recession is the sole remaining remedy, one which will brake but not reverse the "secular decline" of the currency, because recession will erode the last edge of U.S. productiv-

ity that allowed capital gains on dollar assets. Then America will have to resign itself to "piecemeal" abandonment of the dollar's international role, while Japan and West Germany will choose between trade war and exchange controls or finally accept a reserve role for the mark and yen. As we report in *International Credit*, however, the Europeans, Arabs and other major foreign dollar holders will not write off the dollar so easily, and the expansion of the EMS's gold operations could be used to draw the dollar into this orbit.

—Susan Johnson