



## LETTER FROM LONDON

### *Wrecking Crew*

**British PM John Major looks a mild and inoffensive man. It's hard to see him as the boss of a wrecking crew that has virtually demolished the British economy. Yet his unassuming exterior masks the disastrous combination of a fundamental aimlessness with an utter dogmatism about specific policies.**

Major is convinced, against all evidence, that getting inflation below 2% will restore the British economy to good health. Along with his lacklustre Chancellor, Norman Lamont, he believes that massive unemployment, unprecedented levels of bankruptcies and mounting numbers of house repossessions are a "price worth paying" to get inflation down.

It was John Major as Prime Minister who persisted in keeping interest rates high, driving Britain ever deeper into recession. It was John Major as Chancellor (Treasurer) who in 1990 took Britain into the European Monetary System (EMS) at the unsustainable rate of 2.95 Deutschmarks (DM) to the pound. That policy was foolish then; it was insane in September 1992. It was persisted in, despite all the growing

signs of impending disaster, at the expense of foreign currency reserves and the credibility of British monetary policy, until Major and Lamont were driven out of the Exchange Rate Mechanism by a tidal wave of selling in the markets.

Lamont forced the Treasury to stubbornly persist in buying sterling from holders who were only too happy to get rid of it in mid-September, throwing away billions of dollars to support the pound. By then the government was the only buyer and its actions were futile, since they only served to fuel speculation and drive the pound down still further. This interventionist folly came from a government whose key slogan has been: 'You cannot buck the market'. This is by no means true as a general rule, but in this case, with an almost universal belief in financial markets in the inevitability of a devaluation of the pound, it makes sense.

Major and Lamont have tried to save themselves by accusing the German Bundesbank of perfidy in not intervening to save the pound. But why should the Bundesbank throw good money after bad? The Germans had in effect offered the UK a devaluation as part of an orderly realignment of currencies within the EMS, along with the Italian Lira. The British government refused to consider the idea. Revaluation within the EMS at the beginning of September would certainly have been a U-turn, but it would have maintained Britain's position within the EMS. As it is the government has been forced into a precipitate withdrawal, and it has probably wrecked the system beyond repair.

Lamont and Major see themselves as victims of circumstances beyond their control, and their policies as essentially right. Given the chance, they would have continued to sacrifice the real economy to the god of 2.95. They are exactly like the mindless and rigid believers in 'sound money' who sacrificed Britain's poor to the Gold Standard in the 1920s. They still insist that the goal of negligible inflation remains intact and that they will keep interest

rates at a level necessary to achieve it. There will be some immediate relief for the economy from the beneficial effects of the devaluation. But high interest rates and a macho round of spending cuts in the northern autumn will ensure there is no substantial recovery.

And yet: what if Labour had won office back in April? Sadly, it would have done just as Major has done. The Labour leadership were all committed to the EMS and refused to accept that DM 2.95 was unsustainable. Current Labour leader John Smith as Chancellor would have doggedly held on to an overvalued currency. Labour had and has no more clue how to handle the exchange rate or domestic inflation than the Tories. And Labour would have had even less credibility with the markets.

The only real policy alternative available to Labour was twofold: first, to admit that the pound was considerably overvalued against the mark and that Britain would seek realignment within the EMS; and, second, to insist that domestic inflation be dealt with by an incomes policy (like the Accord) and not by interest rate hikes and public expenditure cuts. Yet those who advocated such policies before the April elections were informed by Labour 'pragmatists' that they would lose Labour the election.

Labour lost the election. It has been an ineffectual opposition ever since, because it has had nothing of substance to say about the EMS that differed from the Tories. It has refused to think through the hard issues on policy and has accepted feeble compromises and positions that make it indistinguishable from the Tories. Had it honestly faced Britain's problems before April, Labour could now take an unassailable political lead on the basis of having been proven right. Britain needs an Opposition as never before, and it doesn't have one.

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