The original documents are located in Box C22, folder "Presidential Handwriting, 6/5/1975" of the Presidential Handwriting File at the Gerald R. Ford Presidential Library.

THE WHITE HOUSE

WASHINGTON

June 5, 1975

ADMINISTRATIVELY CONFIDENTIAL

MEMORANDUM FOR: JIM CANNON

FROM: JERRY H. JONES

The attached was returned in the President's outbox with the following notation:

-- Circulate to the Domestic Council.

Please follow-up with the appropriate action.

Thank you.

cc: Don Rumsfeld
Alan Greenspan

THE PRESIDENT HAS SEEN

THE CHAIRMAN OF THE
COUNCIL OF ECONOMIC ADVISERS
WASHINGTON

June 3, 1975

GRF Circulate to Domestic Council

MEMORANDUM FOR THE PRESIDENT

A major philosophical issue which will emerge in the months ahead will be the role of government in economic planning and control.

The Economist of London has done a short post-war historical summary of the experience of the United Kingdom. It is the best testimony in favor of a competitive free enterprise system I have seen in a long time.

Alan Greenspan

AMERICAN REVOLUTION BICENTENNIAL 1776-1976

Schools Brief

Government and industry

Britain has a mixed economy. Part of it—eg, the National Coal Board or British Rail—is publicly owned and run. Part—from Imperial Chemical Industries down to the corner sweetshop—is privately owned and run. Part—eg, British Petroleum and International Computers—is a mixture of the two.

Even in the private sector, there is extensive public intervention, negative and positive.

This mix seems natural today. It would not have seemed at all natural to our grandfathers. And the proper proportions of the mix, the extent, aims and methods of public intervention, are still acutely controversial.

In Britain today 6½m out of 25m workers are employed by the public sector; of these, just over 4½m are employed by local and central government, providing services, or goods, which are mostly not sold in the market (eg, police services, defence services, etc); while 2m are employed by public corporations, mostly making things which are sold in the market

Forward in waves

Intervention in postwar Britain in the production of things sold in the market has moved in two waves (with a third now on the way):

(1) Nationalisation. The first postwar Labour governments, 1945–51, took into full public ownership the coal mines, railways, airlines, electricity, gas and steel. Partly for practical reasons—the railways were broke—but more for political ones: the Labour party was committed to take over the "commanding heights" of the economy (but concentrated on taking over the commanding heights of yesterday's economy, rather than tomorrow's—it did not lay a finger on the banks, except the Bank of England). Steel was denationalised in 1953 by the Conservatives, in government from 1951 to 1964, and renationalised by Labour in 1967. Waterways, most ports and some road transport are also state-owned.

(2) Since the early 1960s, both parties have tried a host of measures to promote industrial development (especially in "development areas"—those with high unemployment), and specifically to increase the level of private industrial investment. Both, but mainly Labour, have tried to reshape certain industries, with company mergers greased by public money. Both have flown to the aid of "lame ducks"—firms that would have gone bankrupt but for government assistance.

(3) Since Labour returned to power in early 1974, it has combined plans for new nationalisations (shipbuilding, the remaining ports, aircraft construction and, through "negotiation", 51 per cent of North Sea oil) with plans for much wider intervention in private industry through information and "planning agreements" between government and large companies.

(4) In addition, all governments, but especially those of the past 15 years, have influenced the economy in sectors whose orders have come largely from public bodies: notably the aircraft industry, shoved—against even the airlines' doubts—into the commercial disaster of Concorde, and the nuclear power industry.

The record

Most of the various forms of intervention tried so far have a poor record.

(1) Nationalisation made it possible to slim down certain industries without too much social pain: coal shrank from 600,000 employees in 1960 to 250,000 in 1974, railways from 515,000 to 190,000. But the job has never been completed and nationalisation slows down some desirable contraction. Sir Monty Finniston, for example, chairman of British Steel, says that around 10 per cent, or 20,000, of his workers should be made redundant over the next few months. But to date the government's policy has been to delay closures of out-of-date plant to save jobs.

This leads straight to the much heavier complaint: the nationalised industries' huge losses, partly because of their sheer size and bureaucratism, partly because governments have not allowed them commercial freedom. The Conservatives, for instance, in 1971–73 held down their prices in order to restrain general inflation.

Nationalised industry today employs 8 per cent of Britain's employed population, and takes 24 per cent of its investment in plant and equipment. It is doubtful if such large resources are being employed as efficiently as they could be. Output per employee is rather above average; but output per unit of capital is strikingly low.

(2) The many instruments for intervention in the economy at large have included:

(a) Indicative planning. A spectacular failure at national level. The first attempt was made in 1963 by the National Economic Development Council (Neddy) set up by the Tories in 1961. This discussed the implications of 4-per-cent-a-year growth from 1961 to 1966 for the nation and 17 selected industries. But within two very short years the 4 per cent growth rate proved to be mythical. Nonetheless, in 1965, Labour's newly established Department of Economic Affairs produced a full-blown National Plan, so titled. This aimed at 25 per cent growth between 1964 and 1970. Ten months after that, panic "freeze" measures blew it back into the fairytale books. Neddy's "little Neddies" for various industries have produced sectoral plans, but there is little evidence that they influence industrialists.

(b) Medium- and long-term finance. Since 1945, the Bank of England has promoted and (in partnership with private financial institutions) partly financed two bodies, the Finance Corporation for Industry and the Industrial and Commercial Finance Corporation to aid investment. By 1974 their combined investments totalled the relatively trivial sum of £270m. In late 1974 this operation was enlarged. The Bank, inspired by government, pushed the financial institutions into offering up to £1 billion for a new holding company, into which the two had been incorporated, in 1973, Finance for Industry.

A far more drastic proposal has recently come from the Secretary for Industry, Mr Tony Benn: that financial institutions should be compelled to funnel part of their income, up to a total £1.5 billion a year, into manufacturing investment.

(c) Investment incentives. These have normally been combined with attempts to induce investment into specific regions, or into manufacturing. Labour in 1966 introduced investment grants, of 40 per cent in development areas (covering about one-fifth of the whole working population) and 20 per cent elsewhere, towards the cost of new plant and machinery in manufacturing (services were excluded); plus 25 or 30 per cent grants for buildings in development areas only. The Conservatives, arguing that grants encouraged unprofitable investment no less than profitable, switched, during 1970–72, to the system, completed by the Industry Act 1972, which is still in force today: (i) nationwide "free depreciation"—ie, the whole of plant and machinery investment (but only 40 per cent for buildings) can be instantly set against tax on profits; service industries are included. (ii) Cash grants of 20–22 per cent in development areas, graded according to their need. (iii) Selective loans or grants in development areas. (iv) Finance for industry anywhere if the government thinks it is in the national interest and the money cannot be procured elsewhere. Mr Benn has used this Tory carte blanche (subject to a £5m maximum before parliament's approval is needed) to help worker co-operatives set up amid the ruins of their ex-employers' failures.

(d) Discriminate taxation or subsidy, with the same purposes. Since 1967, employers have received a regional employment premium (now £3 per week per man in manufacturing, in a development area). From 1966 to final abolition in 1973 there was also a selective employment tax, hitting employees in services but not in manufacturing. At various times, this also had regional variations.

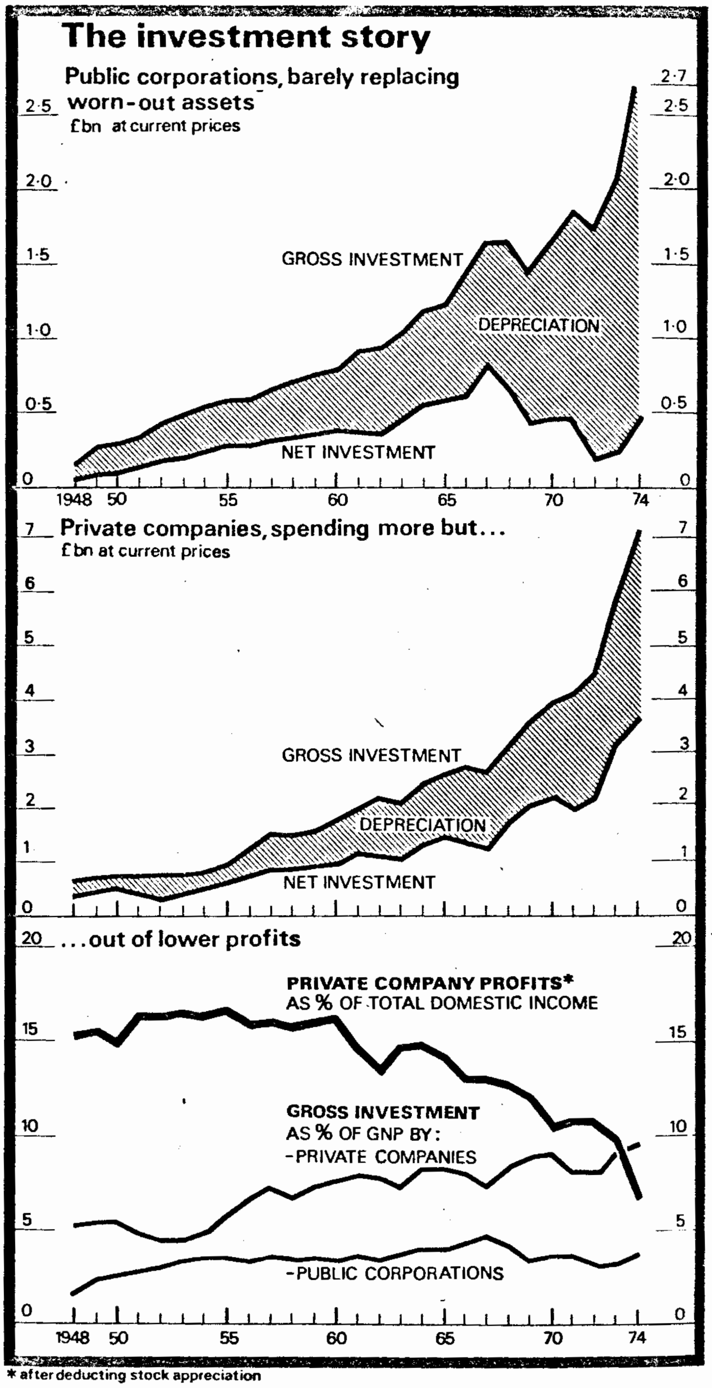
(e) Discriminate physical controls—eg, the Industrial Development Certificates system and control on building offices in central London—or inducements to move to the regions such as 'advance' (ie, spec-built) factories, development of new towns, road improvements, dispersal of central government work.

(f) Sectoral subsidies—eg, to shipbuilding (grants and cheap credit guarantees) or in 1969–74 to hotelbuilding (grants). Neither of these was tied to improvements in efficiency, and Britain today has too many grossly inefficient shipyards and too many high-priced (but not enough low-priced) hotels.

(g) Rationalisation of a sector—modernising, cutting out unneeded unnecessary capacity, merging firms, etc. There has been one success here: a modest £15m scheme under the Industry Act in the wool industry. There may be more: the Neddy family are looking at other modest projects, and the ferrous foundry industry was named as one in the April, 1975, budget. These apart, the picture is spotty; the question is whether doing nothing would have been still worse.

The Labour government in 1966 set up a state agency to promote rationalisation: the Industrial Reorganisation Corporation. It was supposed to identify desirable mergers and help them along, taking an equity stake if need be, but later selling out (which proved much harder than getting involved). It promoted, notably, the mergers that produced the motor giant, British Leyland, and the only significant British computer firm, ICL.

The IRC was allowed to die by the Conservatives, who came to power wanting to stop pouring money into "lame ducks". This proved easier said than done; when Rolls-Royce, caught in a money-losing aero-engine development, went bust in early 1971, the government picked up the aero-engine pieces; the car factory was sold to the public by the receiver in 1973.



* after deducting stock appreciation

Issues

British Leyland, ICL and Rolls-Royce raise key issues of public policy in today's continuing debate on state intervention.

(1) How far should government rather than the market, choose and conduct an industrial policy at all? ICL was formed, Rolls-Royce picked up, to keep Britain in these high-technology (and defence-related) fields. Investment in, say, paperclips, might have been more profitable; American computers or aero-engines cheaper; mergers with foreign firms a better solution.

(2) High policy apart, does government know better than the market? Healthy Leyland was encouraged into merger in 1968 with unhealthy British Motor Corporation—and the whole ramshackle giant has been a financial disaster.

(3) Is there, in practice, a policy at all, or does the state merely rush in to save lame ducks?

(4) Should the state confine itself to lame ducks? Why lumber public enterprise with whatever is worst, while—as the Conservatives did with Rolls-Royce and proposed for nationalised industries—parting with profitable segments like Rolls cars or British Rail's property developments? The same argument applies to Mr Benn's pioneer worker co-operatives: they are the ones least likely to succeed.

(5) Should lame ducks be rescued at all? They are usually rescued to prevent high unemployment. But might there be better uses for the men and material resources? What price, in discipline and some lost jobs, should trade unions pay for saving other jobs?

(6) Should the state take an equity share in return for its money? And a role in management? It will do so now with British Leyland, Ferranti (electricals), Alfred Herbert (machine tools) and other queuing ducks. That implies extension of the public sector in every serious recession.

Benn's Neb

The new 1975 Industry Bill, still before parliament, raises all these issues and more. It springs from Labour's belief in public industry and the public accountability of private industry; from the fact that investment is low; from Mr Benn's belief that that means "industry is failing the nation" (to which industry replies that the failure is government's for providing an economic climate of stop-go and shaving the profits industry needs for investment); and from the belief—quite separate, though Mr Benn holds both—that workers should be consulted on and influence the management of their firms.

The bill (for details, see *The Economist* of February 8, 1975) provides for:

(1) A National Enterprise Board to manage state holdings and entitled to buy and keep a stake in any manufacturing company, including profitable ones. Neb is allowed finance up to £1 billion.

(2) Government's right to get information from significant manufacturing companies on their plans, notably details of output, productivity, sales, mergers, take-overs, closures, investment, etc.

(3) Government's duty (subject to some safeguards) to pass this information to the trade unions concerned.

(4) Planning agreements between government and firms, offering (in effect) shared information, security and subsidies to firms that agree to shape their plans as government thinks they should.

Most private industrialists fiercely dislike this bill. In particular, because the disclosure means that commercial secrets will go not just to government, or even to employees, but to trade union officials outside the firm. And what positive use, industry asks, is Whitehall equipped to make of the information? (The answer, today, is very little.) Why do not government (or trade unions) have to reveal their plans? (An amendment to the bill says it should do so to planning agreement partners, but it might be defeated.)

Neb arouses less dislike. But business still fears it might take holdings in companies that wanted no part of it.

The Conservatives have said that they will repeal this bill when they regain power. Understandably. Labour's nationalisation plans, including those setting up a new British National Oil Corporation to handle state North Sea oil interests, represent an extension of the existing public sector. The Industry Bill could represent a far-reaching change in the management and climate of the whole of British industry.