NATIONAL INSTITUTE OF ECONOMIC AND SOCIAL RESEARCH:
PRESS CONFERENCE
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Opening remarks by the Director

Good morning. Welcome to the National Institute of Economic and Social Research for the release of our quarterly Economic *Review*. This morning we will concentrate on the outlook for the World and UK economy but also highlight a number of risks to the immediate outlook but first I want to make some brief points about economic management in the UK..

In a pioneering venture, Christopher Dow at the National Institute of Economic and Social Research helped establish the concept of demand management as the key objective of economic policy. He showed in his 1964 work that although demand management had prevented "the heavy unemployment that accompanied the pre-war trade cycle", the price paid was that of excessive year-to-year fluctuations resulting from policies that ultimately became known as 'Stop–Go'. A more damning indictment of policy over this period is that the emphasis on short-run macroeconomic control encouraged the neglect of the more fundamental issue of the long-run rate of productivity growth. Indeed in later work, Dow was himself acutely aware that labour productivity did not regain the path it had adopted in the long expansion after World War II. The tension between short-run demand management and long-run economic prospects is as much a current concern as it was over 50 years ago; accordingly, as we enter an election campaign that may be dominated by the question of Britain's exit from the EU. One again we are in danger of letting the urgent drive out the important.

Nearly ten years on from the start of our most recent economic crisis in 2007, which is fast becoming the UK's 'lost decade', we can observe that, despite considerable innovation in macroeconomic policies, income per head has not recovered especially well, it only passed the peak of 2007 GDP per head in 2015. In comparison to the recovery from previous postwar recessions, there has been a very disappointing growth in the level of GDP since 2008.

The path of output in the quarters after the start of every postwar recession and we can start to understand the depths of the problems faced at the end of the first decade of this century. Subsequently, income per head has barely exceeded its pre-recessionary level: that against a typical postwar expectation of growth in income per head of 2 or so per cent per year. The challenge facing policy is more over the frustrated expectations of economic progress rather than simply the management of economic rehabilitation. The key question facing any policymaker is how to bring about sustained growth in income per head, which is intimately tied up with the question of capital employed, total factor and labour productivity.

The lessons from the earlier period highlighted by Dow ultimately led economic policy to be conceived more in terms of the formulation of long-run plans or 'rules' in preference to discretionary policy. It was argued that these rules would help ensure that the plans of households and firms would be consistent with the stated aims of policymakers and so jointly it would be easier to achieve non-inflationary growth with full levels of employment. Many of these ideas led to the granting of operational independence to the Bank of England to pursue the government's inflation target on 6 May 1997. We also have had a long period of innovation with fiscal rules, culminating in the creation of the Office for Budgetary Responsibility in 2010. And yet both the Chancellor and the Prime Minister have shown in quick succession that rules are applied with discretion, with changes announced by the incoming Chancellor in last November's Autumn Statement about the date by which the fiscal deficit will be eliminated and also by the Prime Minister's calling of an early election with relative ease on 18 April, bringing forward the next election by some three years compared to the plan enshrined in the Fixed Term Parliaments Act of 2011.

The irony, to some great degree, is that the widespread adoption of rules for fiscal and monetary policy has not improved long-run performance and indeed may have done little to encourage addressing the more fundamental questions of productivity growth. Both total factor productivity and labour productivity seem to have descended to ever lower levels in the postwar period and this deterioration in the performance of productivity helps us understand the main continuing economic problems: low real wage growth; low levels of investment and a dwindling capital stock; uneven performance at the regional level; rising perceptions of income and wealth inequality; the risk in the household balance sheet from the emphasis on housing as a store of wealth; the lack of infrastructure and R&D expenditure; the concentration of financial intermediation in property based lending; and the evolving need for monetary-fiscal-financial coordination. These major problems are well understood and predate the issues raised by the decision to leave the European Union and yet may end up being neglected in the national debate.

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