'New winter of discontent could be hard to avoid': Economic expert on the crises facing Britain

October 12 2021, by Steve Schifferes

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Everyone over the age of 50 remembers the year in which rubbish piled up in the streets and graves were left undug. With Boney M and Gloria Gaynor dominating the airwaves and "Superman" as the big Christmas movie, there was no one to save Jim Callaghan's ailing government from imminent collapse in 1978–79. Those famous Conservative election posters that would soon say that Labour Isn't Working summed it up with devastating simplicity.

Eighteen months into the COVID pandemic, another very difficult winter looks increasingly likely with fears about a resurgence of the virus combined with rising inflation and an energy and supply chain crisis. So what can we expect, and how meaningful are the parallels with the 1970s? We asked finance and economy specialist Steve Schifferes to explain.

What are the main threats this winter and how do you see them playing out?

The first is the pandemic itself. We still have a high volume of cases. We don't have as many deaths or hospitalisations as in previous waves, but the onset of winter, coupled with the more infectious nature of the delta variant, and the fact that many people are still unvaccinated, might mean more restrictions. When Boris Johnson recently announced a "plan B" with more restrictions, nothing was ruled out and masks and remote working were mentioned as possibilities. This potentially means more economic disruption.

A number of other economic problems have emerged during the recovery. Because the recovery has been faster than expected across the world, commodity producers have struggled to keep up, driving up global commodity prices.

The biggest problem is oil and gas prices, with UK wholesale gas prices having almost tripled since the beginning of 2021. Gas is still one of the main components of the energy mix in the UK, so consumer prices for gas and electricity have risen sharply, while lots of businesses are being affected—for example, steel and fertilizer plants have been temporarily closing.

Several consumer energy companies have already gone bust, and various others could be in trouble if they have a lot of customers on fixed tariffs and too little room to make a profit with the current prices.

Meanwhile, shortages of everything from lorry drivers to carbon dioxide are causing problems in retail and hospitality. We're seeing supermarket shelves increasingly empty. Brexit has made the whole situation worse because a lot of workers in the food supply chain came from the continent and are no longer allowed to work in the UK.

The government's idea that British workers will rush to fill the gap is misplaced. Even if they could be trained in time, many British workers, after being furloughed or working from home, are not that keen on working in low-paid jobs with long and irregular hours. Lots of pubs and restaurants are struggling to stay open either because they can't find enough workers or because of supply shortages. Employers in industries like hospitality and transport are already having to offer higher wages to attract staff.

The price and wage increases are producing higher inflation data. Whether this is temporary depends on people's expectations. If people begin to expect more rises, as they did in the 1970s, it will change their behavior. Firms will raise prices and more workers will want higher wages, causing an inflation spiral.

To keep the economy buoyant in recent years, the Bank of England has cut interest rates to record lows and put huge amounts of money into the economy in the form of quantitative easing. If it has to change direction because of higher inflation, this could have a big effect on asset prices, ranging from shares to houses, since they have all been bid up by cheap money.

Higher interest rates would also have repercussions for the public finances, which Chancellor Rishi Sunak is clearly very worried about already. It would mean that future government debt becomes more expensive, which could put a further squeeze on public spending.

How do all these challenges affect the public finances?

We are already seeing signs of the government taking steps to try and improve the public finances ahead of the critical three-year spending review and budget on October 27. The levy on national insurance to finance the NHS and social care reform is an obvious example, and so is the decision not to make the £20 universal credit uplift permanent.

These decisions will push more people into poverty, as could the end of the furlough scheme. Meanwhile, the decision to temporarily scrap the earnings-linked element of the "triple lock" will perhaps permanently reduce the generosity of the state pension. And the chancellor has already announced tax rises for businesses from 2023. Overall, almost every section of the community is facing either tax rises or benefit cuts, although the super rich seem to have escaped largely unscathed.

Despite these tax increases, Sunak appears to be setting very ambitious targets to stabilize the public finances, which are likely to require further big cutbacks. Public sector pay is likely to be squeezed, as it was in the last spending review. If it is frozen in cash terms again and if inflation stays higher, this will translate into a significant wage cut in real terms.

However, there are many other even less visible ways that chancellors can raise revenue or cut spending. We might see a rise in duties, for example on petrol taxes or road pricing, as part of the green agenda.

The stage is also set for a major conflict between Johnson and Sunak over leveling up. So far, the government has spent relatively little on this flagship agenda, except for the hugely expensive and much delayed HS2 rail service. With former Bank of England chief economist Andy Haldane newly made permanent secretary for leveling up, it's going to be interesting: his view is that if the government is serious, it will need to make a long-term commitment to spend much more than just the investment in HS2.

How does this compare to the 1970s?

In the 1970s, a series of economic crises caused major problems for the Heath and Wilson/Callaghan governments. The decision by Opec in 1973–74 (and later in 1979–80) to cut oil production to drive up prices hit the British economy hard, forcing the Labor government to go cap in hand to the IMF and cut public spending.

The trade unions were a lot stronger than today, and much closer to the government. The government's failure to persuade them to moderate their wage demands at a time when inflation was really raging—it spent most of the second half of the 1970s in double digits—led to widespread strikes during the "winter of discontent" and opened the way for Margaret Thatcher's 1979 victory.

Today, with more modest inflation and weaker unions, conditions are somewhat more benign—we probably won't have to live through the famous "stagflation" that dogged the 1970s. Yet the level of disruption caused by Brexit and the pandemic is unprecedented, as it the size of the public deficit for many years.

With rising world energy prices again adding pressure at a time when the public finances are straining, we could well return to the stagnation in living standards of the last decade. Poverty and inequality may well increase, and we are probably going to see strikes. There will be similarities and differences to the 1970s, but a new version of the winter of discontent certainly could be on the cards.

Provided by The Conversation