

# *Economic Recovery and the Countryside*

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## **Introduction**

In the context of British economic circumstances in early 2011, an analysis of the prospects for the resident population of the English countryside is developed in what follows.

## **The Rate of Exchange**

In 2007, one pound sterling (£1) was worth two US dollars (\$2). Three years later (2010), £1 was worth \$1.54. In 2007, £1 was worth €1.46; in 2010, €1.17. The intervening years (2008-09) are the period of the great global financial crisis. Prior to the crisis sterling had been regarded as overvalued (Cobham, 2006) and this conclusion had also been reached as part of HM Treasury's assessment of whether to adopt the euro (Wren-Lewis, 2003). Some long-run average values for sterling (over the period 1975-2006) are \$1.71 and €1.50.

Comparing sterling's exchange rates before the crisis with those prevailing afterwards one observes that there has been a devaluation of the pound by 20% in terms of dollars and euros. This devaluation is also reflected in terms of the index of sterling exchange rates, which encompasses a fuller range of currencies used by countries trading with the UK (HM Treasury, 2011).

## **A Shift of Resources**

Changes in the international value of a currency are important when the country against which the currency is secured has a substantial fraction of economic activity associated with products or services readily available from sources overseas. This is because, in the absence of constraints on overseas trade, prices are translated into sterling from the international markets in which they are determined. Following a devaluation, sterling prices (sometimes called 'local' or 'domestic' and equivalent to 'export' prices) of all these internationally-traded products or services should rise.

Not directly affected by devaluation should be the prices of those products or services that are required locally and can only be provided from local or national resources: housing (domestic property) or personal care (domestic help) and many public services would come into this category: they are described as 'non-traded' because they are not internationally traded and thus have no international price.

So, when a devaluation occurs, prices of traded goods and services increase whilst prices of non-traded goods and services do not. This suggests that conditions favour expansion in the traded sector of the economy and, in the absence of spare capacity (e.g. an appropriate workforce presently unemployed), a shift of resources from the non-traded sector.

## **Where to Expect Expansion**

The UK has a substantial presence in a broad range of international markets for physical as well as financial products and services. Export sectors seemingly well-placed to benefit include: medical and pharmaceutical products; office machinery and computers; transport equipment; chemicals; mechanical engineering; radio, TV and communications; scientific and photographic appliances (Buisán et al, 2006). These sectors may be considered 'hi-tec' (i.e. technologically advanced).

Based on the competitive advantage of London, the UK financial sector accounts for a significant fraction of the international trade in currencies and financial instruments (BIS, 2010). This activity had returned to 2007 levels by 2010. However, whilst the financial sector is a significant fraction of the UK economy as a whole, a significant proportion of domestic financial activity may be linked to local property markets that have contracted.

Although the UK is a net importer of many raw materials (e.g. agricultural commodities), domestic producers will benefit from higher prices in international markets (e.g. for wheat).

## **Stagnation and Contraction**

As noted above, non-traded sectors of the economy such as domestic property and public services are liable to stagnate or even contract in the aftermath of devaluation. As domestic property prices have stagnated so the housing market has suffered a contraction in volume of activity.

Government revenues have reduced sharply because of the reduction in economic activity caused by the crisis in banking and international finance. This has resulted in a public sector budget deficit. Plans by HM Treasury to rebalance the budget involve increased taxation (e.g. raising VAT) and reduced commitment of spending for public services.

## **Employment Consequences**

Expanding sectors of the economy are expected to increase the number of people employed. However, people presently workless may not have the levels or mixture of skills required by expanding sectors of the economy. The same may be true of those employed in public services or the domestic property or financial sectors, where stagnation and contraction could otherwise encourage people to seek a change of job. Furthermore, new employment opportunities may be incompatible with existing locations of the potential workforce, and geographical mobility may be limited. These factors could extend the period required for economic recovery to show itself in the shape of increasing aggregate employment. The possibility that foreign immigrant labour will be a feature of the recovery has also to be considered.

## **Timing and Transition Costs**

There is a danger that the speed with which the sectors that face stagnation and contraction reduce their workforce will be faster than the speed with which expanding sectors increase theirs, adding to the transition costs of temporary or 'frictional' unemployment experienced by the country as its economy rebalances towards the traded and away from the non-traded sectors.

Nevertheless, there are strong signals that the expected expansion in traded sectors is emerging (Markit, 2011a). This complements the recovery in the international financial sector alluded to previously (BIS, 2010; King & Rime, 2010) and evidence that economic growth is increasing abroad thus raising effective demand for exports (Markit, 2011b).

## **Implications for Rural England**

Different definitions of rural England give different figures for the proportion of the population living there: these vary from about 10% (OECD, 2011) to about 20% (CRC, 2011) and in-between (Parsons et al, 2007). Despite this variability, the occupational characteristics of the resident population are described in similar terms: farming and tourism, together with small-scale manufacturing and self-employment (including consultancy), are key features; public service and administration is consistently cited as particularly significant. Given the relatively low levels of worklessness amongst rural households (Parsons et al, 2007), economic recovery may imply increased in-migration or inward commuting to rural areas and/or significant employment switching within the rural population (from the non-traded to the traded sectors of activity).

Agricultural produce as well as ores and minerals extracted from the countryside will increase in value not only because of devaluation but also because of rising prices in global commodity markets.

## **Social Enterprise**

In conjunction with the government's attempts to eliminate the budget deficit there has been even greater pressure to transfer responsibility for delivery of public services from public authorities to social enterprises. This has been a long-term government policy objective in the UK (Parsons, 2010) and there have been suggestions that rural England might constitute an appropriate economic environment for such developments to be successful (CRC, 2011; CRC-ResPublica, 2011; Parsons et al, 2007).

## **The Risk of Inflation**

On occasions it is necessary, even desirable, for the relative prices of raw materials such as energy and food to increase in order that the resources of the world as a whole are husbanded according to precautionary assumptions. Given the national dependencies inevitable in an economic system driven by international exchange, government policy makers have a responsibility to accommodate such real price increases. As a direct employer, consistency with this accommodation requires that productivity of the public service workforce must increase sharply to avoid declining real wages or redundancies. To avoid fuelling a greater general price inflation, money wage-rates in the public sector will have to be restrained unless productivity gains are large enough to justify otherwise.

At a more general level of monetary policy there is a danger that the expansion of the monetary base (as a result of the Bank of England's 'quantitative easing' programme and government influence over publicly-owned banks' lending policies) protects prices in the domestic property sector and thus increases the scale of price rises required across the traded sectors of the economy (due both to devaluation and to higher international market prices for raw materials).

How the Bank of England would respond to a continuing annual rate of inflation above 2% is not easy to forecast. A rise in the rate of interest (desirable for households dependent on savings) might have consequences that could be negligible or severe according to the international economic context in which the change occurs (and the Rumsfeld Conjecture - the existence of unknown unknowns - applies in these circumstances *a fortiori*).

### **Long Run Considerations**

The emergence of an economic recovery in Britain will probably owe a lot to the long run advantages enjoyed by London as a financial centre: an independent currency; a legal environment with elements of compatibility both with the United States and the European Union; and the English language.

Likewise the countryside as an environment conducive to businesses engaged in international aspects of the Knowledge Economy (consultancy as a service *per se* and also as part of 'hi-tec' export sales) should supplement farming and other small, specialist production industries in providing a platform for prosperity and a preferred residential environment.

Much has been made of demographic change in the context of the future social and economic circumstances of rural England. Whether coping with this contributes to economic recovery or is dependent on economic recovery may be debatable.

### **Conclusions**

The economic recovery will be characterised by a shift in emphasis of economic activity favouring internationally-traded production and services rather than domestic property and local public services.

The pace of the recovery may be retarded by the difficulty of reconciling inflexibilities in the existing workforce, and inadequacies of the educational system, with opportunities created for productive employment.

Social enterprises are seen as crucial to the reconfiguration of resources required to improve productivity in welfare services to cope with the likely consequences of demographic change (increasing numbers of elderly people)

London and the countryside may be expected to fare better than the rest of Britain (especially the metro-urban centres in post-industrial areas).

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