

The role of profits

Angered by the cost of living squeeze and sky high energy prices, many people are now hostile to the whole idea of company profits. It is encouraging them to demand ever higher windfall taxes to confiscate more or less the whole profit, and leads on to demands for nationalisation. It is perhaps time to remind ourselves what profit making enterprises have achieved to raise our living standards, to provide well paid jobs and drive growth. It is also time to ask why countries like Venezuela that went the whole way in nationalising and imposing price controls ended up in poverty with large shortages. Many Venezuelans are fleeing the country to live somewhere where profits are allowed and living standards are higher.

The UK's own experience with nationalisation was poor. A nationalised steel industry put in five large integrated plants but could never sell enough of the steel given their cost levels and spent the next two decades arguing over how many people to sack and how many plants to close. The nationalised railway had a poor record on safety, punctuality and service. It sacked many staff as its market share of the travel market plunged downwards. It lost a fortune for taxpayers who had to pay the bills. A nationalised phone company fell years behind the USA where competing private sector companies leapt ahead with better service and newer technology. In the UK there was little choice of phone, long waits to get a line and rationing including having to share a line with the neighbour for many customers. The electricity industry relied on coal power stations when cleaner and more efficient gas was available. The industry leapt ahead driving costs and emissions down by putting in combined cycle gas plants as soon as it was privatised. The coal industry was in long term decline, with bitter disputes about job losses and mine closures.

Wherever price controls have been tried investment falls and supply reduces. This makes the problem worse. Rent controls seem like a great and popular idea, but as rent controls come in so people withdraw properties from rental and shelve plans to build more. This usually makes the property shortage worse and results in higher rents in the medium term than if controls had not been introduced.

The combination of double corporation tax, a planned rise in the rate of business tax by 31%, and windfall taxes that will be imposed for several years whether there are windfalls or not is putting companies off investing in UK oil and gas production. These taxes will not only mean we import more and become ever more dependent on high and volatile world prices, they will also mean we collect less revenue in future. We will lose out on taxing good cashflows from oil and gas fields under UK control, and watch as we pay high taxes to foreign governments to import their energy instead.

Profits are used to pay for investments in extra supply, which in turn sustains more and better paid jobs. No profits, means no investments. Fewer investments means lower living standards.