

## Zimbabwe, Venezuela, Sri Lanka – three poster countries for price controls

Venezuela has been brought low by printing lots of money, by price controls and nationalisation. A potentially rich country with the world's largest oil reserves, Venezuela has seen its income per head fall from \$12,000 in 2011 to just \$1877 last year after a decade of price controls and nationalisation.

Zimbabwe, once a relatively prosperous agricultural state with plenty of food has seen its income per head fall to \$1362 a head and lived through food shortages. Compulsory land transfers and price controls have not been kind to the economy.

Sri Lanka has been less extreme but has seen its income per head fall to \$3698 last year and experienced food and other shortages as controls have been used. As a Professor at Colombo University wrote of their price control "it has never sorted out our supply shortages, but it has eliminated the quality goods from the market, and it has created a black market for good quality products, and it has not helped in any way eliminate poverty"

Food riots, protests against government, high inflation and damaging price controls have created misery in each of these potentially successful countries. Price controls have taken too many goods off the shelves, have bankrupted businesses that could otherwise have supplied more, have driven foreign companies out and put off more investment in capacity to supply. They have bred black markets, fostered smuggling subsidised and price controlled goods out of the country to sell at better prices elsewhere and prevented imports.

Why do so many people think they would work? Why will they not study what happens when they are used widely in inflation ridden economies?

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## Why price controls and windfall taxes do not work

Let me begin by making it clear I do want government to ensure everyone has sufficient money to be able to keep warm and do their cooking this winter. That is best done by allowing people to keep more of their income through tax cuts, or by giving people more in benefits to cover the bills who cannot earn. This blog is about the underlying problem of high prices and how you solve them.

Most people want there to be an easy answer to the ultra high prices of

energy. Some say just stop any price increase for any energy sold to anyone. Some say control the prices of oil and gas that producers from UK reserves can charge us. Some say stop the renewable producers charging the same price for their electricity that the gas based producers have to charge now the gas price has gone up. Maybe there is a way to do the latter that the industry would accept, but they do need to be able to make a profit on their investments and need some long term visibility on contracts. The first proposal would stop all price rises. The second and third would stop some of the price rises, but would leave us paying the new high prices for all imported fuels and for the items of domestic production they leave out.

All these schemes mean government to a greater or lesser extent stops price doing what price will always do, balancing available supply with available demand. Higher prices now surging if left in place will solve the imbalance. All those in business or on better incomes who can economise on their power use will now do so, reducing demand. The state will need to rein in its extravagant use of energy by reviewing its over night street lighting, its heating and lighting of little used offices and the rest. Better off households will reach for the thermostat or timers to slice a bit off their past use. So demand will fall.

More importantly the price signal will incentivise businesses to put in more capacity to produce energy. Oil and gas producers will be encouraged to bring forward marginal new prospects that used to be uneconomic for development. Renewable investors will have more profits to plough back into additional capacity or into all important storage. In the short term energy companies will sweat their current assets more to maximise output. In the medium term they will add to their stock of producing assets and in the longer term the whole industry stands a better chance of achieving major commercial throughs with nuclear, battery, hydrogen and other technologies.

If you stop the energy industries in the UK earning the extra revenue from high global prices you will divert profit and investment capital away to countries that do allow them the benefits. If you stop them charging world prices they will divert as much of their current product as possible to markets where they can charge more. Anyway you look at it, price controls prevent more supply and impede lower demand from energy saving. It is no accident that the countries that have relied most on price controls are often those in the lower income bands worldwide, short of domestic supply. I will deal with those who think that means the answer is nationalisation in a later blog. That too would make the position worse.

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## [An independent Central Bank](#)

I read various bizarre articles defending the Bank of England's independence against an imaginary threat from Liz Truss. I only know what she has said in

public, where she issued no threat to Bank independence. She said she favoured a review of the Bank's mandate to see if it met best standards in the world of independent Central Banks, and to find out what can be learned from the Bank's failure to forecast or prevent the high inflation we now suffer. The inference was she wanted a tougher Bank, not a Bank that printed more money and artificially depressed interest rates to suit the government.

The articles are bizarre because they always ignore the radical change to Bank policy launched by Mr Brown and Mr Darling and continued by all subsequent PMs and Chancellors. They agreed with the Bank a policy of creating more money and buying up state debt to keep rates down. Right from their start of this policy it has been a dual control policy, with the Bank needing the consent of the Chancellor and requiring a full Treasury guarantee or underwriting of the transactions. As this policy has dominated money policy between 2008 and 2021 we cannot say the Bank was then genuinely independent. It does have and did have throughout the sole power to fix the official interest rate. No-one in this debate is recommending taking that power away.

Going forward I would like to see the Bank introduce quantity of money and circulation of money as important information to monitor and take into account when settling interest rates. It has proved difficult to control inflation whilst allowing a large increase in the money supply triggered by substantial Quantitative easing. The Bank may not want to go back to strict money targets that were used in the early 1980s to end the last big inflation, but monitoring money and showing an awareness of its importance might help them make better calls. The current money figures show they have now reined things in considerably. They do not need to overdo the tightening from here to make the opposite error to being too loose as they were in the previous two years. The IMF does usually call for monetary discipline when it puts in a recovery programme for a state that needs financial help.

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## [The ONS makes life more difficult](#)

When Rishi Sunak announced a £400 payment to every electricity bill payer I was concerned about that way of offering some relief. I would have preferred tax cuts on energy which would directly cut the CPI/RPI measurements of inflation. The government thought these cash payments might qualify as reductions in energy bills and help the CPI figure. Instead after considerable delay the ONS has decided to call them "current transfers" to households that do not cut the price of power.

They rightly go on to remind us they have the legal power to make a judgement about such matters, They say "Decisions on whether to include rebates, subsidies and discounts in our consumer prices inflation statistics are taken

on a case by case basis". As these £400 payments cannot be withdrawn and spent on anything else but take the form of a cut in the electricity bills that need to be paid there is a perfectly good case to say this is a cut in the price of electricity for all users.

All this matters. Allowing the full bill cost to boost the CPI without allowing for the discount that is available means we face higher inflation with all the knock on effects. This decision will increase public spending and the deficit given the way some spending items are directly linked to the inflation index. It raises the repayment amount for indexed debt. The Treasury should have asked the electricity companies to put it on bills as a discount to the price of power, which is what it is. A sum equivalent is payable by the Treasury to the companies as a subsidy. This is another missed opportunity.

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## Why we need more gas

Many people argue that instead of producing more of our own gas to cover some of the energy shortfall we need to press boldly on with more windfarms. They argue that now wind energy is cheaper than current gas prices, so it makes economic sense as well as environmental.

If only it were that simple. Many have pointed out that the problem with wind energy is it stops when the wind does not blow. It does not matter how many windfarms with how much rated capacity you install if the wind does not blow. Wind turbines also cannot function in very high winds. But there is an obvious more practical problem for those who say the answer lies in a blowing wind. Most UK households this winter will heat their rooms and water using gas. Renewable electricity would be no use to them. Most industrial processes use gas rather than electricity. Most commercial premises are fuelled by gas.

Until most households, most factories and most offices have been through their own electric revolution we will need more gas as electricity cannot power it. The issue is do we produce the gas ourselves, with greater reliability and tax revenues flowing to the UK state, or do we import it with tax revenues and jobs flowing to the overseas provider? Is there going to be a hydrogen revolution, where it becomes commercial to use windpower to create large quantities of hydrogen which can be used to fire our boilers? If so that does not solve the problem for the next few years whilst this is planned and installed.

In all the grand green plans gas is down there as a transition fuel. In all the plans there is an acknowledgement that the world as whole will be using more oil and gas at the end of this decade than it did at the beginning. It will be more reliable, collect more tax revenue generate more jobs and vent less CO2 if we use our own rather than rely on imports.