Getting the economy growing faster

The combined policies of a fiscal squeeze – eliminating the deficit – and monetary tightening – cutting back on car loans, mortgages and consumer credit – has predictably slowed our growth rate in recent months, as forecast here. Last year the government produced a budget where the deficit undershot by £19bn over the course of the financial year. The Chancellor could report much faster and better progress with cutting the deficit, but in so doing took more money off us in tax than planned which helped slow the economy.

If he had spent all the £19 billion on a mixture of lower taxes and higher spending as identified in recent posts, there would have been up to a 1% boost to output. This in turn would have generated more revenues, allowing the deficit to come down a bit as well. The good news is this would reduce the amount of extra borrowing a bit more. The amount we borrow is quite sensitive to the pace of growth of the economy. When growth speeds up more revenue comes into the Treasury from people earning and spending more. As more people get into jobs, so the cost of their benefits goes down.

The UK economy has the potential to expand at more than 2% per annum, so we should be aiming to boost its current growth rate which is below that level.