Bank of England hits new low in its analysis and decisions

The latest MPC meeting was hopeless. There was once again no recorded discussion of money and credit. There were generalised banalities about overseas economies that sounded as if they been taken from a newspaper comment. There was no consideration in the report of how the fall in money will transmit through the banking system. There was no consideration again of why Japan and China had avoided the high inflation the Bank has created here. There was the usual alibi comment that rises in global prices like oil are a given and can cause inflation.

Worse still was there was no explanation of why they persist in wanting to sell £100 bn of bonds at large losses. There is no proper consideration of the impact this will have on long rates in the market and on money. Just as the Bank refuses to discuss or accept its extreme money printing and bond buying had any effect on the inflation so now they refuse to see the adverse impacts of the reverse. Indeed they seem to think these policies are asymmetric. They thought buying bonds at ever crazier high prices was a positive on prices and output when they thought they were fighting deflation. They now think there is no negative effect when they switch to selling bonds at ever lower prices and bigger losses.

The Treasury continues to reimburse them for huge and unacceptable losses. It should tell them to stop the sales. The ECB who made a similar inflationary error by creating money and buying bonds is not making the opposite mistake of selling them in the market at needlessly high losses. The Bank should on this occasion learn from the ECB. Instead they will not even talk about their error, just as they refuse to accept printing loads of money was inflationary.

Councils spend too much

In the three years to 2019 Councils spent £ 6.6 bn on buying up commercial property. I was against this at the time. Property had risen in value and the private sector was keen to offload shops and retail centres, seeing the rise of on line retail. The Councils were able to borrow cheaply thanks to the low interest rate regime, and expected rental income to exceed their costs.

Unfortunately for them covid lockdowns and new drives to on line shopping and working from home accelerated the negative trends for many of the shops and offices they bought. The collapse of many commercial property values will have hit valuations of Council owned property.

The Councils who had all this money to buy these assets often now claim to be short of cash. Maybe they should sell these assets to raise money where the values are still sensible. Maybe they should cut their losses when they can where they made bad investments as going forward they will be paying more interest on borrowings than when they first bought. They should stop adding to these portfolios. Wokingham taxpayers should not be made to buy a solar farm. The Council is not skilled in such an area and claims to be short of money. The risk is not acceptable for a public body.

Many Councils have redundant or surplus assets beyond these speculative portfolios some bought. They should be selling. Many Councils are spending far too much on consultants on top of the salaries of officers meant to be qualified to undertake many of the specialist tasks. Many are still annoying many drivers with expensive schemes to delay the vans and cars more. Save the money and spare us the aggro.

What is the most annoying waste of money from your local Council? How many extra admin staff have they taken on in recent years?

My Article in Conservative Home

Treasury briefing keeps telling us unfunded tax cuts will cause inflation. We have just lived through two years of surging and high inflation with increased taxes. That should lead them to question their bizarre view of inflation. If they believe that tax is the key to inflation why don't the Treasury think the tax rises also caused the inflation? In one sense some of them did, as they heaped higher taxes on energy as energy prices soared.

The Office of Budget Responsibility acknowledges that it has overstated this year's borrowing so far by £20 bn yet carries on asserting there is no scope to cut taxes. The reason borrowing is lower is once again they got their forecasts of tax revenue wrong. I read in the press they keep sending the Chancellor very different forecasts of how much borrowing there might be in five years time. The Government uses this to decide what tax cuts they can afford. The OBR forecasts though wildly fluctuating never seem to fluctuate to allow tax cuts according to the press briefings that filter out. Why does the government use the five year forecast to decide anything? It is bound to be wrong. The last three years have seen many overstatements of future borrowing by the OBR for the immediate year which should be a lot easier to get right than five years out.

The Treasury and Bank need to think again about the inflation they have just presided over. Let me give them some thoughts on what did cause it. The Bank should grasp that printing £150 bn and paying very high prices for bonds to keep interest rates close to zero was inflationary. The Treasury should understand that boosting spending by £350 bn a year over three years and borrowing the money to pay for much of the extra spending was inflationary.

They ended up borrowing it at overdraft rates from the Bank of England. These rates then surged as the Bank decided to hike them. It means it was very unwise to borrow like that. If they had funded it long it would have been a lot cheaper and arguably less inflationary. The Government needs to grasp that recruiting 103,000 more civil servants over six years and allowing a 7.5% collapse in productivity was inflationary.

They will reply that the surge in oil prices from the Ukraine war was inflationary. It certainly drove up energy prices but does not account for why UK inflation was already three times target before that happened. Nor does it explain how big energy importers China and Japan did not have a big inflationary surge as we did, but then they did not print lots of extra money and drive their interest rates lower.

The budget needs to cut taxes. It also needs to help bring inflation down and it needs to push downwards on the deficit. Far from being impossible to do these three things at the same time, the right policies will indeed do all three together. If only the Treasury had a model of revenues that picked up how increases in growth deliver higher revenues more accurately it would be easier to persuade them. If only they were better at controlling public spending and at avoiding big falls in public sector productivity that would help too.

Let’s have a go at a budget that they should grudgingly agree using their wayward models will achieve these ends. Let’s start with getting inflation down more quickly. Suspend the 5% VAT on domestic energy for heating for the year ahead. Take 5% off petrol and diesel by a temporary cut in fuel duty. This will give a useful nudge down to energy costs just as world prices are increasing again. Some of the revenue lost will be compensated by higher profit and windfall taxes on the energy companies as they benefit from higher world prices. Cover the rest with some of the proceeds of selling the whole remaining holding in Nat West shares. A lower rate of inflation earlier will also save some money on public spending which is very geared to the inflation rate.

The budget should proceed to expand the supply side of the economy to offset some of slowdown the Bank is creating. The VAT threshold for registering small businesses should be raised to £250,000 from £85,000. This would release a lot of new capacity quickly which in turn would produce a bit of downward pressure on prices. More importantly it would generate additional tax on incomes and profits as the small businesses did more. Treasury models will score this as a revenue loss so offset their fictional figure with rephasing some of the £20 bn carbon capture and storage spend. It is unlikely anyway that large scale projects with good business cases will be available to subsidise any time soon.

We have lost 800,000 self employed from the workforce since February 2020. Some of this may be Covid related. It is also the result of tax changes in 2017 and 2021 which make it too difficult for some to grow their businesses in the way they used to, particularly where they need business customers. Change the rules back. Again Treasury will claim a loss, though it should save government money especially where people move back into self employment from benefits. This could be more than offset by imposing a strengthened version of the civil service recruitment controls the Government is talking about. Natural wastage should slim the civil service after the increase of 103,000 in just six years.

Switch farming grants for the future away from stopping people growing food to supporting them for doing so. That will generate more business success to tax. It will cut imports which do not deliver any income tax, national insurance and corporation tax on the food growing,

Save on anti driver schemes the Transport Department helps fund, in accordance with the welcome new approach outlined by the Prime Minister.

There are many other places for reducing the costs of government. All this means we can have lower taxes, a lower deficit and lower inflation. This is a cautious package. It would be possible to move further and faster to generate more growth. Look at the USA which has managed to get inflation lower than us despite their Central Bank making the same mistakes as ours. It has also just recorded 4.9% growth.

Just do something to cheer us up. We are fed up with being controlled by wrong forecasts by the OBR. Nor should we have to pay further for the wild policy swings of the Bank of England who did much to give us inflation in the first place. We do need higher public sector productivity, lower costs of Government and a lower deficit. This can advanced with tax cuts which lower prices, create more supply and boost incomes and profits to tax at home.

Ministers and civil servants

Our constitutional practice used to be based around the fundamental proposition that government power must be accountable and this is best done by Ministers reporting to an elected Parliament on the conduct of government. Ministers have to defend the actions of their officials and departmental administrations, or explain what action they are taking to correct mistakes, reform policies and change personnel where things go wrong. Ministers are meant to decide and civil servants are meant to advise. In the toughest version of the doctrine Ministers had to resign for mistakes made by officials which they knew nothing about until they came to light with the damage they caused.

This practice could scarcely apply to a large number of areas of government activity when we were in the EU that came under EU regulation, directives and court decisions. There was no serious attempt to think through the consequences of these changes. Ministers usually shouldered the burden of responsibility for laws and decisions taken in Brussels, even where they had opposed them. The public decided to sort this out and reassert the need for genuinely accountable Ministers who could change laws and policies where needed by voting to leave the EU legal structures. With EU laws and policies Ministers could face failing policies which they were both blamed for and could not change.

In recent years under governments of all three main UK parties this has been further modified. There has a growing enthusiasm for so called independent bodies. Many politicians came to the conclusion that it was better to appoint specialists to run quangos that could take big decisions, make a wide range of rules under statute, enforce rules, impose penalties , spend large budgets and set out blueprints for the future. The Bank of England gained control of interest rates and money policy. The Environmental Agency set policy on water and flooding. NHS England gained more control over health budgets and management. The vast HS2 project was run by an independent highly paid team of managers.

As we survey the surge in inflation and the giant bond losses of the Bank, the flooded farms and the pollution of rivers from the Environment Agency, and the huge waiting lists at the NHS the public demands Ministers sort it out. They do not want to hear that the main budgets and powers are all exercised by highly paid managers who insist on independence from Ministers. HS 2 showed that high pay with plenty of independence did not necessarily produce a good outcome.

There is much to be said for reasserting the original idea that Ministers can direct and alter the management of these bodies as they will take the blame when things go wrong. Some things done by quangos would be better done directly by the sponsor government department, cutting overheads. Ministers may well opt for substantial management delegation, but need to find good managers they trust and who deliver to make that model work. They need to to be able to reward and promote them and in bad cases to remove them. They need full ,access to important information about the way the service and the policies are working out.

Appointing Ministers who know the subject or who have an enthusiasm for it would help. Keeping them in post for long enough to have an impact and to know the area well is important. A Minister like Nick Gibb was allowed to work in Education where he was a great advocate of synthetic phonics to improve reading abilities. More importantly he was allowed long enough there to make a big difference and see the results of his approach come through with better literacy scores. We need more of that.

The Treasury needs to think again about inflation

Briefing from the Treasury for over a year now has been rightly telling us inflation is too high, and wrongly saying what we need to do about it.

Their mantra is unfunded tax cuts cause inflation. No recognition that the last two years of high inflation have been years of tax rises, so there is no possibility the current inflation was caused by unfunded tax cuts. No mention that if unfunded tax cuts can cause inflation then so can unfunded spending rises. No mention of the huge surge in spending in the last three years.

They should think again. The present inflation was brought on by

The Bank of England printing £150 bn of extra money during 2021,a recovery year.

The Bank keeping interest rates near zero by paying ever crazier prices to buy up state debt and to enable the government to borrow huge sums at very low rates

The Treasury imposing high carbon taxes, fuel duties and windfall taxes on energy to give us very dear energy at a time of high market prices

The Treasury agreeing to a 103,000 increase in civil service numbers from 2017 to today and a 68,000 increase in other public administration posts , resulting in a 7.5% fall in public sector productivity over the 3 years 2020-22.

The big expansion of state debt this decade effectively financed on a Bank of England overdraft

Tomorrow I will examine how the right tax cuts offset by spending controls and asset sales can bring inflation down. I am not recommending more borrowing to fund tax cuts, but if you did borrow by issuing a longer dated bond to pay for a tax cut the bond withdraws the same amount of spending power as the tax cut injects, though from different people.