

# Why we have inflation – printing more money

Modern Central Banks ironically do not think money matters. Most of them no longer target money supply, and many provide little or no commentary on it. This is surprising given the fashion they entertain to create more and more money to tip into circulation. They should understand that if you create more money and all else stays the same prices will rise, as more money will chase the same volume of goods and services. That is why money matters.

I guess their response is that as they create massive new amounts of money the velocity of circulation, the amount of use people make of that money, will fall. So it need not be inflationary. It is true that in the short term in the pandemic lockdowns more money was an offset to the collapse of demand, and use of the money tumbled as many people and companies hoarded what new found cash came their way.

It did however have a first round inflationary effect, as it was planned to do. It inflated asset prices, pushing up the price of government bonds which the money was used to buy. The people who sold the bonds to the Central Banks then often bought other assets like shares with that money, pushing their prices up even more than the bonds. So far so good. The governments could borrow loads of money on the cheap, and the inflation cheered up anyone with assets and did no harm to those without. I supported a vigorous Central Bank response to offset some of the worst economic consequences of the anti pandemic measures. I also thought governments would get away with a massive one off increase in borrowing, financing it at very low rates, all the time activity was so depressed. There did need to be a big offset and rescue packages given the economic severity of the policy.

If you carry on creating more and more Central Bank money to keep government borrowing rates low there becomes more danger that the money will start to find its way from asset markets into creating demand for goods and services. All those extra savings people made during lockdown as they saved their going to work costs whilst still banking their pay could be spent in a rush, driving up the velocity of money use. If commercial banks use the extra cash they have to expand credit that too creates more demand for goods and services. By these means more created money can lead to goods and services inflation if the money starts to create more potential demand than there is supply.

Central Banks in the USA, UK and the EU should stop their money printing and bond buying now to reduce this risk. They and the other bank regulators should ensure total money growth is sufficient to allow decent growth without encouraging too much extra inflation. That can best be secured by setting appropriate levels of permitted lending / balance sheet strength for the commercial banks using their existing powers. States should continue to cut back their deficits and borrowing substantially by promoting growth policies which will swell revenues and cut crisis spending.

---

## [My interview with Nigel Farage on Talking Pints](#)

You can sign up to receive John's blog posts by e-mail for free by submitting your email address in the box below.

The e-mail service is powered by Google's FeedBurner service. Your information is not shared.

John Redwood won a free place at Kent College, Canterbury, and graduated from Magdalen College Oxford. He is a Distinguished fellow of All Souls, Oxford.

---

## [End sewage discharges to rivers by water companies](#)

Since I and others raised this in the Commons last week during the passage of the Environment Bill the Minister has supplied additional information about how they are proposing to get rid of bad discharges to rivers as we all want:

- "Between 2020 and 2025, water companies will invest £7.1bn on environmental improvements in England.
- Of this, £3.1 billion will be invested in in storm overflow improvements specifically.
  - We have also made our expectations crystal clear in our draft Strategic Policy Statement to Ofwat where, for the first time, the Government will tell the industry's economic regulator that we expect water companies to take steps to "significantly reduce... storm overflows", and that we expect funding to be approved for them to do so.
  - In August 2020 we established the Storm Overflows Task Force to bring together key stakeholders from the water industry, environmental NGOs, regulators, and Government in order to drive progress in reducing sewage discharges.
- The Task force has agreed a long-term goal to eliminate harm from storm overflows.
  - We have committed to reviewing the case for implementing Schedule 3 to the Flood

and Water Management Act 2010 in England, which would set mandatory build standards for sustainable drainage schemes on new developments, and which many have called for. This action has the potential to markedly reduce quantities of water unnecessarily entering the sewerage system. The significant action I have detailed will deliver real reductions in the harm caused.”

---

## **“A low tax Conservative” Chancellor?**

The Chancellor tells us he believes in low taxes. In that case he has work to do. Let him prove his point in this coming budget.

First, abolish the tax on jobs he proposes for April with his National Insurance surcharge. The advisers who told him he needed to raise an extra £12bn next year, have now told him he has already raised an extra £46bn in tax in the first half of this year thanks to tax cuts and recovery. Their revenue forecast was that much out between March and September! Let's stick with a winning formula of lower tax rates and more revenue.

Second, end the attack on the self employed by cancelling the changes to IR 35. We need all the enterprising and self employed people we can get to power recovery and change the economy.

Third, remove VAT from green products. The government claims to be the greenest ever, so why charge VAT on boiler controls, on insulation, draught proofing and various other green energy products?

Fourth remove VAT from domestic fuel to offset some of the large rises in price brought on by the gas shortage. The gas price rise will act as a tax on consumption, cutting growth.

Fifth end the threat of higher corporation tax rates

Sixth, consult on setting the new world Minimum Corporation Tax rate to offer some tax competition to Ireland.

If he did these things he would indeed be a lower tax Conservative., He would also collect more revenue and have a lower deficit because the economy would grow more.

---

# Wrong official forecasts will produce the wrong budget

The Budget this week will doubtless be damaged and misdirected by wrong official forecasts. The Office of Budget Responsibility is meant to be independent, yet Chancellors seem obliged to use these forecasts and defend them. Given how wrong they usually are it places the government in a false position and misleads them over what is the proper policy response. Indeed, it leads officials to recommend advice which will slow the recovery and worsen the outturns.

The OBR and Treasury officials are wedded to Maastricht austerity economics. They slavishly publish the UK's position against the Maastricht debt and deficit criteria as if we were still in the EU and had to comply with the Treaties. They will doubtless inveigle the old Maastricht debt and deficit requirements back into a so called new statement of economic policy aims and controls for this Budget despite Ministers rightly wishing to review the framework.

If you are going to steer economic policy around debt and deficit figures you need to be able to forecast them accurately and understand what actions balloon deficits and which ones reduce them. Last year I drew attention to the wildly pessimistic budget deficit forecasts. The outturn was first published as an overstatement of a massive £90 bn in the deficit, even larger than I had dared to suggest. It was subsequently adjusted down to £64 bn by proposing that there will be some hidden losses yet to be determined to add to last year's figures. I repeated the claim that this year's budget deficit was also substantially overstated. At the half year stage it turns out the deficit was overstated by a whopping £43 bn in just six months.

The main reason is the OBR and Treasury underestimate the buoyancy of revenue in an upswing, and have false models of tax revenues which depress revenues when you cut rates without allowing for behavioural effects which increase transactions and output with lower rates. Thus we see that in the year to date Stamp Duty has risen by a massive 85% thanks to a mixture of unlocking and the lower tax rates the Chancellor wisely introduced. Corporation Tax is up 20% despite the Chancellor offering a super deduction for investment which officials are nervous about reading their latest published report.

The Chancellor should announce a strong commitment to low inflation, underlining the 2% inflation target which we are currently breaking. He needs to target tax cuts, regulatory actions and government procurement on scarcity areas where prices are under upwards pressure and offer supply side reforms to boost capacity. Energy, transport, domestic food growing, domestic timber and others are obvious areas.

There should then be a growth target, to send a clear signal to all of government that there is work to be done to boost the growth rate and the productivity rate with great education, training, network investments,

incentives for the self employed and small businesses and innovation.

The state debt is currently stated as £2.2tn or 95% of GDP. As the state will own £475bn of the debt by year end the true figure is £1.75tn or 75% of GDP. This is a manageable amount at current low interest rates. Because the OBR grossly overstate the deficit they will demand tax rises which will slow the economy , garage confidence and impede rectifying supply shortages.