

The Treasury and Bank advice used to bring down governments

I am told grown ups follow Treasury orthodoxy and admire the Bank of England with its independence. The governments that have followed these luminaries have usually put the economy through a boom/bust cycle and have invariably lost if they own the bust.

Edward Heath accepted advice to introduce competition and credit control in the early 1970s when the dollar went off the gold standard. A big inflation was created, to be followed by a sharp collapse just in time for the 1974 elections which Heath lost. There was a secondary banking crisis and property slump. The Labour government which followed chose an inflation prone high borrowing high tax strategy of its own which ended in a further bust when it collided with financial reality.

John Major adopted Treasury and Bank advice by joining the European Exchange Rate Mechanism. Some of us warned this would be damaging and destabilising but the grown ups knew best. They brought on an inflation by printing too much money to keep the pound down, then a savage recession by slashing money to try to rescue a tumbling sterling. The Conservatives went down to a huge defeat even though Labour, the CBI and TUC had all backed the failed policy.

Gordon Brown and Tony Blair in the period 2005-9 accepted Treasury and Bank advice that they could allow a major expansion of banking credit and debt because there had been a new model of global banks that would magically smooth away the risks of excessive leverage. Indeed Gordon Brown didn't just accept this woeful official advice but was part of the world foolishness that generated the idea. The Parliamentary opposition warned against so much state debt and private borrowing. The official advice shifted to demanding a deep recession to wipe out the inflation and some of the debts. Gordon Brown as PM agreed and was thrown out of office as a result.

Today it is possible to avoid the bust. The official advice has already given us the big inflation. According to government and Opposition the Bank is independent and is responsible for enforcing the 2% inflation target. It has lamentably failed, allowing inflation to hit 11%. It blames external events beyond its control, yet it did not warn us of the big inflation coming and fails to explain how Japanese, Swiss and Chinese inflation stayed down if it was just a matter of high international energy prices.

As constitutionally the government is responsible for the huge balance sheet the Bank of England has created by borrowing to buy up a load of bonds, the government should tell the Bank to stop selling these bonds back into the market at large losses as they are currently doing. Taxpayers should not have to take the hit. Money and credit are tight. To avoid the recession action is needed now. The Bank has done too much too late to conquer inflation. Its inflation forecasts yo yo around undermining the credibility of its actions. How can anyone admire a Bank which deliberately bought too many

bonds at crazily high prices and then wants to sell them at much lower prices to make the taxpayers pay for the losses?