

Mountains of debt

As we count the cost of the response to the virus, it is time to sketch out what future plans for public spending might look like.

As one who thought the government had to spend whatever it took to combat the virus and to keep jobs and companies afloat once the government decided on a national lock down I am not in a panic about current levels of debt. All the time interest rates are kept so low this is affordable. It is a one off cost which can be repaid gradually in years ahead.

It has, however, to be a one off, with a substantial reduction in new borrowing next year and beyond as a result of the ending of the expensive special measures and the restoration of more normal levels of revenue and employment.

Over the next few days I want to explore how the government might bring its budget back into a better balance. So far interest rates have been kept low thanks to official action by the Bank of England. They have both lowered interest rates and bought large quantities of UK state debt up to keep its price high and the interest rates low as a result. Last month debt interest fell owing to lower inflation and the cost of index linked debt, despite the large increase in total borrowings. Again this is feasible for a period dealing with a one off collapse in demand brought on by regulations to stop activity for health reasons. It is not a policy for the future that can be sustained indefinitely, as it would then lead to higher inflation and the need for higher interest rates.

One thing the authorities can do today is to borrow longer. The UK debt management team have done a better job than many countries, so the average maturity of our debt is a lot longer than continental countries on average. Given how low rates are, why not issue some debt with no repayment debt, and more ultra long debt at these tiny rates?

The best way to bring the deficit down and start to limit the debt is to get a good recovery underway. State debt is rarely repaid. It is usually rolled over or extended. As growth returns the aim must be to reduce the debt as a proportion of a growing economy. There are some easy and obvious reductions in spending that can be made which I will discuss again in future posts. Let's start by ending EU contributions, which went up again in June.