

The magic money tree died

Inflation usually kills magic money trees. Responsible advanced countries normally tell us there is no magic money tree, knowing as they do that their growth is soon killed off by inflation.

The magic money tree has been renamed Modern Monetary Theory. The idea is the Central Bank creates money in its accounts as only it can do, and buys up government debt with the money. The government can then issue more debt as there is a willing buyer at a low rate of interest. The government can afford more debt because the rate is so low, and because it owns the Central Bank who buys up lots of their debts anyway. The state ends up owing lots of money to itself.

Using the Central Bank and government debt is just a complex way of disguising it. They could as well simply instruct the Central Bank to print the extra money and give it to them to pay the government bills. Indeed both the Fed and the Bank of England had powers to do this during the pandemic.

If you carry on doing this when the economy is near full capacity it is very inflationary. Government gives itself money to buy goods that others are trying to buy and to hire Labour working for others. Only by bidding up prices and wages does the state grab these resources. Others who still want them either go without or bid higher again. An inflationary spiral sets in.

Now the U.K. economy is back to pre pandemic levels with low unemployment there is no scope for magic money trees and considerable inflation risk. Inflation is too much money chasing too few goods. Government has to incentivise more production to help bring the price rises down. It needs to change its pro imports policies for energy, high energy using industrial products and food.