

The twin deficits

The UK is currently running a large state deficit, with the government spending maybe £350 bn more than its tax income this year. Last year we also ran a £100bn balance of payments deficit. Whilst this fell sharply during the global lockdown and big hit to world trade, it is picking up again as world trade recovers.

Allowing a huge deficit for just this year by the state is affordable, as interest rates are near zero and at the same time the Bank of England is buying up £250 bn of the state debt for taxpayers. The US, the Euro area and Japan are all doing the same. It's still not a good idea to waste any of the money so borrowed, nor to think this is a long term answer to our economic challenges.

More serious is the balance of payments deficit. This now stems from two main causes. The first is the persistent large trade deficit with the EU. Our surplus with the rest of the world does not manage to get anywhere near offsetting all of this.

The second is the now persistent deficit on investment income account. Because for the last few decades we have imported so much more than we exported to the continent, we have had to sell companies, properties and shares to foreign buyers to raise the foreign exchange we need to pay for all the European imports. As a result we have changed from a country with a large surplus on our overseas investments prior to joining the EEC/EU into a country with a large deficit in investments, owing overseas investors much larger sums in interest payments and dividends than they owe us.

In future blogs I am going to return to the question of how once out of the single market and customs union we can reduce our trade deficit with the EU and stem the need to keep making our investment position worse by having to sell our assets. It is not a good economic model to be dependent on the goodwill of foreigners to buy your food or electricity, relying on foreign supply and on foreign finance to do so. The balance of payments has to balance, so if we import too much we have to sell off the country's assets to pay the bills.