The twin deficits

For several years the UK economic debate has been fixated by the state deficit and borrowing requirement, and has largely ignored the balance of payments deficit. I presume this is because of official adherence to all EU rules and guidance, so they have been trying to get our budget deficit back down to Maastricht compliance levels at under 3% of GDP. There is celebration this month because at last we have got there thanks to a further surge in tax revenues that outperform the usual Treasury pessimistic forecasts that delight in getting it wrong.

I have not been worried about the state deficit for sometime, ever since Mr Brown found out that the UK state can literally print money to pay its bills. Mr Osborne, originally a critic of this in opposition, then discovered its charms in office as well. It turned out to have no adverse consequences on shop price inflation, though of course it caused massive price inflation in government bonds, because it was accompanied by severe pressure against bank lending to the private sector to avoid an inflationary blow off. I always adjust the outstanding debt by the £435 bn the state has bought up, as this is in no sense a debt we owe. So our government borrowing level (excluding future state pensions which some here worry about and which have always been pay as you go out of taxation) is modest by world standards at around 65% of GDP, and at current interest rates is affordable.

Most of the state debt we owe to each other anyway. The government owes it to taxpayers who own the debt in their pension funds and insurance policies. The state can always raise enough money to pay the donestic bills backed by the huge powers to tax, and as we have just seen when credit expansion and inflation are low it can also use liquidity created by the monetary authorities.

The deficit I worry about much more is our external deficit. That is the one where we have to buy foreign currencies to pay for it. It is the reason why we keep selling some of our best property and business assets to foreigners, and why we have to borrow abroad. Running at around 5% of GDP it is high by world standards, and means we gradually get into more debt or sell more assets to keep up with it. When you owe money to foreigners they may not accept money created to pay them off but will need real assets.

One quarter of the payments deficit is the government’s payments abroad for EU contributions and overseas aid. Stopping the EU payments halves that, and spending more of our overseas aid on the refugees who come to the UK here in the UK would help as well. Under overseas aid rules you can include the first year costs of refugees and migrants in your own country, and supplies and capital items you need to provide aid abroad. So lets make sure where appropriate we do spend the aid money at home or in the country we are helping, rather than buying imports from other advanced countries with it. One of the big wins from Brexit should be the opportunity to slash the big deficit in fish and food which is an important part of the burden of this overseas drag on our finances. I want the Treasury to take the balance of payments deficit more seriously and to act as a counter to those who want us to give more money away to the EU to perpetuate this large imbalance.