Funding the Future

Let's not get hysterical about the UK's finances

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I did not say that: Martin Wolf did. And this is his reasoning which I think too powerful not to reproduce in the public interest. The fact that I've said some of the same things this week just adds to my sense that this analysis is spot on:

First and probably most important, according to the Organisation for Economic Co-operation and Development, the UK’s general government deficit this year will be 13.3 per cent of gross domestic product — indeed, a horrible figure. But the country’s current account deficit is forecast at only 2.4 per cent of GDP. This means, as a matter of arithmetic, that the country’s private sector financial surplus is, on a net basis, financing four-fifths of the fiscal deficit. The country is not going bankrupt. Rather, government deficits are offsetting the prudence of a crisis-afflicted private sector. These deficits can only be reduced substantially if the private sector starts spending more or the current account goes sharply into surplus.

Second, markets remain relaxed about the UK’s fiscal prospects, so far: the spread between German 10-year bunds and equivalent gilts is only 0.7 percentage points, even after the pause in quantitative easing by the Bank of England; the real interest rates on index-linked gilts is some 1 per cent; and the expected retail price inflation implied by the gap between conventional and index-linked bonds is 3 per cent. These are not data for a country on the verge of either a default or an inflationary meltdown.

Quite so.