

# We don't need to cut government spending because we're ..

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Last week I wrote a blog explaining why all the data being published about government borrowing is wrong. We haven't right now got government borrowing in total of about £1 trillion; [we have instead, I argued](#), because of the Bank of England's quantitative easing programme got government borrowing of about £725 billion.

In December the UK money supply fell by 1.4%. ([Table A2.1.1 here](#)). In other words, more was being repaid to banks as loan repayment than they were lending. The consequences are painful: business has less to spend, consumers have less to spend, demand falls, and we all head for recession. That's hardly surprising given that we have relied on commercial banks to create our money supply through their lending and we know that they're failing on all their lending commitments. So, the banks would drive us into recession if we left them to the job of creating money right now, and since this fall in money supply would also lead very quickly to deflation which has the effect of reinforcing recession because people defer spending as they think things will be cheaper in the future the outcome is really pretty bleak.

Which is why, of course, more quantitative easing is inevitable. [Larry Elliott reckons it will be £75 billion](#) and very soon and I tend to agree.

Today the IFS said the government will borrow £124 billion this year. Let's assume they're right and plug that number into my forecast, also allowing for the £75 billion of QE announced in October and the £75 billion now anticipated and we get this overall borrowing data:

Year Net borrowing QE Net		
£bn £bn £bn		
2005	35,736	- 35,736

2006 35,543 - 35,543

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2007 37,182 - 37,182

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2008 66,368 - 66,368

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2009 147,878 200,000 -52,122

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2010 147,686 - 147,686

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2011 124,000 150,000 -26,000

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Average 7 years 34,913

Remember the basis for this calculation: since the Bank of England is buying government debt which has no chance whatsoever of being resold to the market and the Bank of England is wholly owned by the government that debt is effectively cancelled once bought by the Bank of England. The only proper accounting for this debt is to recognise the government can't and does not owe itself this money and as such it should be cancelled out even if it technically still exists.

The net impact is that this year the government will not borrow at all: it will repay £26 billion of debt. And it can do that because the only effective economic activity keeping the economy going is government spending and that spending needs to be financed by the creation of new money made out of nothing by lending - as all money is made (remember that fact - [if you doubt it, read this](#)).

Now we happily live with banks creating money to fund private sector growth if it happens and don't panic about it. We should be just as relaxed if the government is doing that if inflation is unlikely as a result. And there is no chance of inflation as a result of this activity right now. That's because there is so much slack in the economy we have real wage deflation - so there is no chance of this extra money reversing that. Of course green quantitative easing would eliminate that risk entirely, but [it's practically zero anyway](#).

So what does this mean? Well, actually government debt is falling right now: yes, I mean that.

And it also means we can afford to run a deficit. Indeed, we can't not afford to run a deficit.

And it means that because that's true the only spending that could possibly need cutting is that which we can't afford to fund net of QE, but since over the last seven years borrowing net of QE will have been less than £35 billion on average a year or less than 2.5% of current GDP and not a person thinks we can't afford to fund that we actually have no need for a programme of cuts right now. And nor will we do so until such time as employment rises and the prospect of real wage growth returns, which seems a distant prospect at present.

In that case the whole Tory economic narrative is wrong: we can afford the current deficit and must spend at current levels to ensure unemployment falls, wages rise and tax revenues increase to clear it unless we want to keep printing money for good. Since I'd rather people worked than print money I'd go for that stimulus option now. And to do that I would, I admit, have to borrow more. But when net borrowing is negative right now of course we can and should borrow more when the cost of doing so is near enough nothing: net real interest rates are about zero or even negative for the government at present.

This is the only sane economic policy option we have. All that's stopping us taking it is the completely false story that a) we're borrowing more than £100 billion a year when we're not and b) that debt is rising when this year it will not.

And yes, I'm aware how bizarre this will sound to many people. But just remember that Schopenhauer absolutely right when he said that truth goes through three stages. In the first stage, it is ridiculed. In the second stage, it is violently opposed. And in the third stage it is accepted as self-evident. We'll be at stage 1 with this idea right now. I give it a couple of years to reach stage 3.