

The failure of Osborne's austerity is not a minor cause...

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The UK is in recession.

The IMF has told it to prepare a Plan B because the balance of risk is that things will get worse.

Nick Clegg is saying the Coalition has got it wrong and is planning to invest in new housing to stimulate growth.

Across Europe austerity is being rejected.

Germany stands in isolation in the EU and G8 under a barrage of criticism that will surely sweep Merkel from office like Sarkozy before her.

I could say this is all entirely predictable, and is as I predicted, but that's not a useful observation, and nor does it add to debate. The observation would also be superficial, as if what was going on was simply a matter of a minor change of direction. The reality is much more important than that: what's happening is not just the rejection of a particular government's economic strategy; the rejection of austerity is the rejection of a whole way of economic thinking, and that's much, much more important.

To understand this it's important to realise what Osborne believed when promoting austerity. He believed that his policy of "expansionary fiscal contraction" would deliver growth for the UK. The fact that many disagreed with him from the outset is not the point: let's take it at face value that he did genuinely believe that his policy was right.

If that was the case then his assumption was that people and companies would genuinely believe that he had the intention of cutting the share of spending undertaken in the economy by the government with the result that they would also believe that the share of total national income to be spent by companies and individuals would rise. As a consequence he thought, or at least he was told he should think, that people would act on this information as rational economic agents and as a consequence would believe that if he was going to cut the share of national income spent by the government in the future there would, eventually, and inevitably be falls in taxation

and as a result they could borrow now in the belief that they would have more income in the future so that they can afford the repayments on that borrowing when they fell due because their tax bills would be lower at that time.

Now, I know that for most people that would appear to be a quite incredible argument. It requires that people believe politicians, and most don't. It requires that people believe that there will be no change in government policy, and those are commonplace. It requires people to believe that everybody behaves rationally and in the same way, which is highly implausible, but that is what economists tell us they do.

This whole idea, seen in this way, is very clearly based upon the fundamental assumptions of neoliberal economics. That is, we have people who want to maximise their consumption, which is why they would borrow now at low interest rates if they thought they could repay those loans in the future out of an increased income as a result of tax cuts, and that we are dealing with people who are totally rational and are able to appraise information on future expectations without emotional engagement but do so purely on the basis of factual analysis within known parameters of possibility, all of which can be probabilistically stated, giving rise to certain inevitable courses of conduct for everybody facing that circumstance.

Does that make George Osborne sound mad? Would you trust a man who based his whole economic policy on such a wild assertion? I never did! But nonetheless this is precisely why he adopted the course of action he did in June 2010 that has plunged us into the current recession and into unnecessary austerity. And what is now very obviously, and entirely predictably to most of us, clear is that all the assumptions underpinning this economic policy were completely and utterly wrong.

We do not live in a country made up of economically rational people.

We do not have a population of people who calmly, rationally and probabilistically appraise data to inform their behaviour in highly predictable ways.

Or alternatively, if we do have such people, they discount everything that politicians say about the future as nonsense, which means that the same net outcome results!

But such simple statements of what might, slightly impolitely, be called the bleeding obvious (although it is beyond the wit of most economists to appreciate it) fundamentally change the basis on which any government must manage an economic crisis. The whole of the political right wing's approach to economic management in such a situation is based on the assumption that if they only change the rules of engagement between government and the economy then people will respond in the rational way that George Osborne assumed and as a consequence of the government changing the rules, and reducing its own activity, they will deliver growth through market based activity. But candidly, as we now see, that assumption is simply and straightforwardly wrong. People don't behave like. As a result the whole logic of supply-side reform is

wrong.

Now, in saying that I'm saying that means there is no reason for regulatory change, nor for removing unnecessary regulation, but what I do quite clearly say is that people do not rationally respond to those processes by creating new economic activity. That is just a myth.

In that case - and as I argue in *The Courageous State* - what we need now is an entirely different approach to economics and an entirely different breed of politicians to implement the resulting policies. Politicians like George Osborne have backed away from making any decisions. They have thought that by denying their responsibility for the economy they can leave the market to determine outcomes and take praise for doing so whatever happens. They are wrong. That isn't what people expect. It isn't what good managers do. Least of all, it is not what competent politicians do.

The job of a politician in a democracy is to provide leadership and to win a mandate from an electorate to deliver their vision of the future, which is an interventionist and proactive policy of delivering reform through the state, by the state, for the benefit of the people who have put those people in charge of the state. That the exact opposite of what Osborne has done, and the failure of his policy should now encourage all politicians not just to look for minor tweaks to the way in which we apply neoliberal economic thinking to the economy, but to rethink their whole approach to not just economics but politics itself for the benefit of the people of this country.

The failure of Osborne's austerity is not a minor cause for celebration; it should signal the start of a new political era.