

The IMF says it is now time for the UK government to pr...

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I just got the heads up that the IMF is about to publish a media release that suggests the UK government now has a duty to starting expanding the UK economy. In advance they've released a blog on the issue. This is what [that blog by Ajal Chopra says](#):

The U.K. economy has been flat for nearly two years. This stagnation has left output per capita a staggering 14 percent below its precrisis trend and 6 percent below its pre-crisis level. Weak growth has kept unemployment high at 8.1 percent, with youth unemployment an alarming 22 percent.

The effects of a persistently weak economy and high long-term unemployment can reverberate through a country's economy long into the future-commonly referred to by economists as hysteresis.

Our [analysis](#) of such hysteresis effects shows that the large and sustained output gap, the difference between what an economy could produce and what it is producing, raises the danger that a downturn reduces the economy's productive capacity and permanently depresses potential GDP. Such effects could arise because of the erosion of skills from persistently high long-term unemployment, the scrapping of idle capital, and inadequate investment that erodes the capital stock and hinders innovation and the development of new technologies. This would be an enormous waste.

But policymakers are not powerless; their action can help avoid such bleak outcomes. Notably, policies to bolster demand will help close the output gap faster, reduce the risk of hysteresis, and insure against the predominance of downside risks. So how should demand be stimulated?

http://www.youtube.com/watch?v=6sa622tF71U&feature=player_embedded

Three policy priorities

First, monetary stimulus can be provided with further quantitative easing, which evidence suggests can continue to support demand by lowering long-term interest rates and improving banks' liquidity. In line with recommendations made in our report, the Bank of England's Monetary Policy Committee voted on July 5, 2012 to expand further its quantitative easing program. The committee should also keep under review the merits of cutting the policy rate. The recent sharp flattening of the yield curve may have increased the stimulative effect of this instrument, possibly outweighing potential negative effects on money markets and financial stability.

Second, credit easing measures can boost demand. Credit conditions remain tight because elevated bank funding costs have limited the quantity and maturity of lending to the private sector, despite significant monetary easing. We welcome recently announced efforts to lower private-sector borrowing costs through broader provision of bank funding against collateral with haircuts, including the "funding for lending" program. Depending on the effectiveness of these new programs, further credit easing measures may be needed, including purchases of private-sector assets on secondary markets.

The government is also considering taking advantage of its record-low borrowing costs to provide government guarantees to fund large, privately operated infrastructure projects. It is important, however, that the choice of projects and the modalities of their operation—public versus private, and financing by issuing public debt versus guarantees—is based on using public funds as efficiently as possible. They should also not be affected by attempts to artificially limit government gross debt or near-term expenditure.

Third, slowing the pace of fiscal tightening would be the main policy lever to support demand if growth does not pick up sufficiently even after monetary stimulus and strong credit easing measures have been given time to work. The government's reduction of deficits over the last two years has created the space for recalibrating fiscal policy, if needed.

Delaying fiscal consolidation could yield gains

Our [analysis](#), which extends recent influential work by [DeLong and Summers](#), suggests that delaying fiscal consolidation can generate permanent gains if fiscal tightening has a larger negative effect on output during a period of negative or weak growth.

The absence of growth, even after additional monetary and credit easing measures, would indicate that the ability of monetary policy to mitigate partially the contractionary effects of fiscal tightening is even more constrained than currently assumed, implying higher and more asymmetric multipliers when the economy is weak. This may occur, for example, if heightened uncertainty, including concern about tail risks, deters the private

sector from borrowing, even in response to significantly cheaper and more easily available credit.

In a nutshell, the priority for U.K. policymakers is to implement more expansionary economic policies, important elements of which are now in train. Without such policies, they risk weak demand that leads to persistently slow growth and high unemployment, which in turn will affect decisions made by consumers and investors, and permanently damage the long-run capacity of the U.K. economy.