

Face facts: the deficit will not be closed during the n...

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Politicians of all hues claim that they understand why people do not trust them, but if they do then I see no evidence that the comprehension they claim to have is influencing their behaviour.

Take the deficit as an example. In 2010 Alistair Darling passed a ludicrous Act declaring that the deficit would be halved during the term of the next Parliament. He might as well have passed an Act declaring that there was going to be no rain in April during that same Parliament. He had no control over either outcome, and each was equally ludicrous. Despite this obvious fact, and the fact that this pointless gesture had no impact on Labour's election prospects, we now find ourselves in a situation where in 10 months time we will be asked to choose between George Osborne and Ed Balls, both of whom will be offering us the equally ludicrous prospect that they will balance the government's budget.

To put this promise in context, balancing the budget is an extremely rare event. It happened in 1988 and 1989 on the back of a property bubble. It also happened between 1998 and 2001, in this case on the back of the dot.com bubble. Both bubbles burst and budget surpluses soon disappeared. This lesson is, however, important. Not only does it show that balanced budgets on the part of government can be considered to be more or less aberrational behaviour, it also shows that they can only happen when the economy has been booming.

As I have said time and again on this blog, this is not by chance. There is a fundamental economic equation that always holds true which is that governments will always run deficits if consumers and business choose to run surpluses (in other words, they save) and there is an overall trade deficit. In these situations a government deficit is not a matter of choice: it arises as a simple matter of fact. When everybody else chooses to save them the government has no choice but to borrow. As the creator of currency, and as the lender of last resort, that is the role that the government inevitably gets in this situation.

This role is not, however, a difficult one. It is only popular narrative that suggest that's

the case. There is a simple explanation for this claim. When almost everyone in the economy is being cautious, which is the case at present, then the last thing that they are seeking to do when saving is take significant risk. That means that they're looking to save by buying the safest product in town. It so happens that this is government debt. The self balancing nature of the economy is such that this means that if the government has to run a deficit then there is, at least, an almost guaranteed market for its debt, and at a modest price because there are ample buyers for it.

So let's face facts. First of all, it is a simple statement of fact that unless any political party has a credible plan for boosting the economy then it cannot claim that it can and balance the government's budget at any time during the course of the next Parliament, or any time thereafter. That simply cannot happen. Balanced budgets only result from economic growth, whether that be sustainable or not. Given that we have grown wary of bubbles, this does, in effect, now mean that to win an election and promise a balanced budget a political party has to have a policy for sustainable growth. No party has come near offering such a programme at present. As a consequence I can say with absolute confidence that neither George Osborne or Ed Balls will balance the budget during the course of the next Parliament.

And when we're facing facts let's also make clear that no amount of cutting will change this situation. In fact, it was simply make it worse. If the government tries to cut whilst consumers are in net terms saving (which includes paying off mortgages), business is not investing and we continue to run a trade deficit, then all that the cuts achieve is a reduced rate of economic growth, increased unemployment, lost output and lost future capacity. What those cuts cannot change is the overall level of the deficit: that continues to be set by the level of surplus that households, business, and the trade deficit determine. This is why cuts to date have had so little impact and why recovery has been so slow.

So, in that case let's face another fact: austerity is no way out of this situation. It literally cannot work. It is an economic impossibility that it can.

There are things that could make a difference. Those will be the subject of another blog.