Funding the Future

Robert Peston on People's QE

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Robert Peston has written a long piece on Corbynomics. As he says:

Corbynism is a kind of collective howl - which can be heard in different accents all over the world - that it doesn't have to be this way.

He's right. And continues:

In this context, Jeremy Corbyn's most important policy is actually his most novel. And it is what he calls, alluringly, "quantitative easing for people instead of banks".

This is how he describes it: "one option would be for the Bank of England to be given a new mandate to upgrade our economy to invest in new large scale housing, energy, transport and digital projects".

Of this he adds:

For the avoidance of doubt, this is not same-old, same-old socialism; it is new, radical thinking.

For which I offer my thanks. I will return the compliment: he tries harder than most to explain and offer reasoned commentary upon People's QE, about which he then adds:

But in a world where globalisation and the free movement of capital are inescapable realities, so-called quantitative easing for people brings considerable risks. Some will see it as stupendously dangerous.

For detail on what it involves, Jeremy Corbyn prays in aid the campaigning tax analyst, Richard Murphy.

I have been called a lot of things: stupendously dangerous is, I think, a new one. So what's Robert Peston really trying to say? He effectively does a compare and contrast between People's QE and conventional QE. Of the latter he says:

But probably the most important point about quantitative easing as currently configured is that the debt bought by the Bank of England has to be repaid - eventually - by the Treasury.

In other words the £375bn of new money created by the Bank of England through quantitative easing will one day be withdrawn from the economy, through the repayment of debts by the government, when the economy is perceived to be strong enough.

He prudently adds:

Now it will be decades before all the £375bn is returned. And theoretically it could never be repaid, if the Bank of England simply decided to roll over maturing debts each time they are due for repayment (as it is doing at the moment).

But the important fact is that the debts still exist as a real liability of the Treasury - and that matters.

This is why he says that:

Central banks, like the Bank of England, have an extraordinary privilege and power to magic money out of nowhere. Which is another way of saying that money has no intrinsic value, and is only worth what we as a society determine it is worth. And, in the reality of global financial capitalism, it is currency traders who decide what sterling is worth, nano-second by nano-second.

So to avoid a collapse in the currency and rampant inflation, central banks have to be seen to be exercising great restraint in the creation of new money.

And, he notes:

The lore of central banks - which, rightly or wrongly, is almost universally accepted by investors - says that central banks should only look at whether there is too much or too little money in the economy in determining whether to increase or shrink the supply of money, and not at narrower economic questions such as whether there are enough roads or houses being being built in Britain.

So let me be clear, at a rather boring technical level I agree with him. Which is why I have been, and Jeremy Corbyn has also been, very keen to make clear that the Bank of England will not be investing in roads, or houses, or green energy. It would in fact be buying bonds from a National Investment Bank which would, under government direction and subject to government guarantees, engage in such investment issues. All that the Bank of England would do would buy some new forms of bond: it would not manage a single project or decide upon any investments. And as Robert Peston notes:

Probably Jeremy Corbyn and his counsellor Richard Murphy would argue that this is unduly alarmist - and that all the Bank of England would be doing would be to purchase new debt issued by energy or transport companies, presumably state-owned or state-backed, and this is surely not much different from the Bank of England's purchases of gilts or government debt.

I just did. So spot on Robert. And, as Robert continues:

That may be right, as a matter of theory, and even - in the case of America - in practice, in that the Federal Reserve in the US has subsidised housing finance for years by purchasing colossal amounts of state-backed mortgage debt.

No, not just the USA Robert: this is also going to be true in the EU as the ECB buys â‚¬1 trillion of bonds at the rate of â‚¬60 billion a month. So definitely not that unusual, after all. And [Mario Draghi] and [Mark Carney] have both made clear this form of QE is legal and possible. And as Robert makes clear is nowhere near as radical as some options:

What is more the former head of the Financial Services Authority, Adair Turner, has been arguing that in order to make meaningful inroads into the UK's massive debt burden, the Bank of England should consider going one step further than quantitative easing and - in a highly prescribed way - create money to actually annul debts.

Remember, he was considered a candidate for Governor of the Bank of England and is a former head of the CBI. So whatever the hard-left is, he (along Jeremy Corbyn) is definitely not a part of it.

But still Robert has his doubts. What are they? First, there's this:

But the dollar is still the world's reserve currency, and the Fed can take liberties with it that are not available to the Bank of England.

But the EU is going to do it. Oh, and in a way China has also just done so in a most unwise way by buying up on a massive scale crashing securities on its stock market. So let's leave that one aside.

And then there's this:

Also it is very difficult to conceive of a way in which the perception - the confidence trick perhaps - of Bank of England independence could be preserved, while obliging it (to repeat Jeremy Corbyn's words) "to invest in new large scale housing, energy, transport and digital projects".

That's apparently because:

Once it had those explicit objectives, investors would see it as politician's poodle and *conclude that preserving the value of sterling would be not quite the priority it has today.*

Robert adds that:

Which is not that the UK would turn into hyperinflationary Zimbabwe or 1923 Germany.

But the risk of investing in sterling and the UK would be seen to have increased. And therefore the cost of finance here would rise - which would mean that there would be even less long-term productive investment here, and a British malaise correctly identified by Jeremy Corbyn would be made more acute.

And that's where he ends. And if you like, where I really need to come in because Robert makes a number of key errors in this analysis.

First he succumbs to what Paul Krugman calls the paranoia of the 'confidence fairy', by which he means we must pander to the silly beliefs of the bond market or they might turn us over. My answer is simple: no they won't. How do I know? Because despite what many people (mainly mainstream economists) said from 2009 on - which was that unless we completely trashed the economy by balancing the books by 2015 then the markets would punish us so severely we would never recover - the truth is a) we have not had inflation b) the markets have bought every penny of debt the UK government has wanted to sell and c) base rates have stayed at 0.5%. So the markets do not behave as those who promote the confidence fairy suggest.

Second, I'd respectfully suggest that anyone who really believes that the Bank of England is really independent of the Treasury they has to first of all a) suspend their belief in democracy b) believe that Mark Carney does not heed what the Chancellor says and c) believe that running an economy without any consideration for what is really going on it is wise. I don't think any sane economist does that (or at least, I hope not). [I dealt with this here.]

Third, to argue as he does Robert has to believe that people's QE of maybe £50 billion a year (at most) is so massively influential that it does, for example, drown out the chance that the Bank could control the economy by a) politely refusing to buy more PQE bonds b) selling QE bonds at the same time as buying PQE bonds c) changing interest rates. I think all would at least theoretically be possible. If not, then Robert is already saying he does not think the Bank of England is independent and the whole confidence thing is really a myth as far as he is concerned anyway in that case.

Fourth, he ignores the fact that buying and selling bonds is not the only way to inject money into and withdraw it from an economy: tax can achieve exactly the same goal. Modern monetary theory makes clear they are substitutes for each other.

Or, in conclusion, what Robert argues is not logical from the perspective of current perceptions of Bank independence; is not logically consistent with democratic government; is not economically logical and, lastly, all comes down to paranoia about market power, which is precisely the issue to which Jeremy Corbyn will not succumb. Or, to put it another way, People's QE can work, whether or not it is radical new thinking; all that might stop it is a fear that bankers might not like it when its whole purpose is to exclude them from a decision making process on investment where they have very clearly failed.

Those supporting Jeremy Corbyn do not share this belief that markets are right. They do not do so for good reason: it is very obviously absurd to think they are, based on sound evidence. As a result those supporters of Jeremy Corbyn are looking for political alternatives that reject that notion. People's QE fits within that framework of alternatives and is economically sound, plausible and deliverable with the objections all coming down to a mistaken belief that central banks must be independent of democratic government and subject only to the will of bankers. Or, if you like, to a question of who governs.

Robert thinks it may be dangerous to upset bankers.

I think it will not be. What is more, I think that the time has come when they have to know that the economy is not run just in their interests.

But at least Robert Peston has had the implicit decency to make clear that this is where the frontline is on this issue. For that I am grateful.