

Funding the Future

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I made my [position clear on fiscal surpluses](#) some time ago. I have not changed my mind. I won't be any time soon. We don't need them. But let's run through the arguments anyway.

We need deficits because people want to buy gilts

The simple fact is that as the economy grows, and as the volume of savings within it grows, and as the demand for secure homes for such savings increases, particularly with an ageing population, there is an increased demand for government debt. All of these situations exist at present. The only way in which this demand for government debt can be met is by running deficits or by borrowing to invest through a National Investment Bank. To deny people the gilts that they want at this point in time would be to undermine the stability of the UK savings and investment market. If that is what George Osborne is planning to do then he should be explicit about it and say why he thinks that is a good thing.

We need deficits to promote new economic activity

There are, right now, a number of unfortunate economic circumstances in existence at the same time.

The first is a savings glut i.e. people are being cautious and want to save money. This is especially true of the wealthy who do, of course, have most to save.

Second, the world's largest companies are, by and large, not investing nearly enough to create required levels of growth to keep the world's rising population in anything like the style to which it has become accustomed. This is almost certainly because there are very few obvious technological innovations that they either want to promote, or which they think will provide them with the returns that tweaking existing products can deliver. To put it another way, the world's global companies (and there aren't that many of them) appear to be pretty bereft of ideas on how to use money creatively at present.

Third, at the same time it is very obvious that there is a massive shortfall in public

investment. We do not have the social housing, transport infrastructure, broadband, flood defences, sustainable energy capacity, insulated buildings and so on that we need. There is a massive mismatch between the private capacity to save within the economy and the private sector inclination to invest and the need for public investment.

There are two, fundamental, ways to solve this mismatch of resource allocation: we can either tax saved wealth to fund public investment or we can borrow that saved wealth and provide it with the secure home that it is looking for at incredibly low interest rates and use the resulting funding for the purposes of providing the public investment we need. In the process we create the growth, employment, wage increases, modest levels of inflation, training and apprenticeships, long-term assets to pass to the next generation, technical innovation, private sector spin-offs and so much more that provides long-term prosperity for our country.

We need deficits to create money

Saving takes money out of circulation in our economy: it effectively destroys it. That is because **money is only created by lending and since saving is the opposite of lending (loan repayment having the same net effect as saving in economic terms) than a worldwide glut of savings leaves a shortage of something that we all need, which is money. UK money supply has fallen since the end of the quantitative easing programme in 2012. If this shortfall is to be made good then the only party capable of delivering the money we need to keep the economy going when the private sector insists, overall, on saving is the government and the only way in which it can create this new money is by running a deficit. This is the role of quantitative easing when the economy gets really tight: I would of course prefer People's Quantitative Easing to any other form because this does, of course, direct the funds to productive investment for all the positive reasons noted in the previous section.**

If the government runs a surplus someone else has to run a deficit

It is a simple fact of life that if one person borrows another one lends. There is no way around this fact. This is just double entry bookkeeping. There is nothing clever about saying this and yet there is an extraordinary reluctance to accept this truth. So, for example, Germany apparently thinks that every country can run a trade surplus at the same time, when by definition this is an impossibility because every surplus must be matched by a deficit, and likewise the current UK government appears to think it can run a surplus without somebody else being in deficit. In fairness the Office for Budget Responsibility is aware of this and, in clear indication of their supplicant role to the Treasury's wishes, have forecast (**as I noted in July**) that **UK consumers will take on record levels of debt and UK business will undertake record levels of borrowing to fund investment at a scale that they have not delivered for decades and that UK overseas trade balances will improve to a degree that no**

one could consider plausible in the current world market, all of which assumptions are necessary to deliver to George Osborne the budget surplus that he craves.

As I said before on this issue, I could be wrong: people may decide to stop saving and suddenly go into a borrowing frenzy, and likewise business might suddenly discover that it has investment needs that have been unrealised for decades, whilst foreign net inflows of funds into the UK may indeed change, but candidly I think that the prospect that all of those things might happen simultaneously is extraordinarily unlikely. To put it another way, the chance that deficits in the private and overseas sector of the scale required to ensure that the government can run a surplus is remote, in the extreme. So a surplus is just not going to happen.

The government's deficit is to some degree beyond its control, especially if it is pursuing a policy of austerity

What the previous section really makes clear is that the government's deficit is, to a very large degree, beyond its direct control. In fact, if it wishes to run a surplus then the only way in which it can do so is by delivering a situation where there is such a state of economic security and stability that people are willing to borrow because they feel secure as to their future income and are confident in the social safety net that will exist to help them if that income fails, whilst business is willing to invest because the solid foundations of infrastructure that supports that investment have been put in place by government. Austerity, and the lack of investment that goes with it, are in that case the absolute antithesis of what is required to create the basis for a sustainable budget surplus. Only a confident government using its power to promote growth can create that confidence and the austerity narrative of negativity creates the opposite sentiment.

What does all this mean for the government's so called Fiscal Charter?

What this might mean for the so called Fiscal Charter is that the plan it puts forward for a sustained surplus is complete nonsense without explaining how and why this will be maintained, which the government is not doing. In fact, it is worse than that: making such a surplus the goal when austerity policies are being pursued makes the achievement of any significant reduction in debt most unlikely - as the current year's borrowing record evidences. And this is why this Fiscal Charter should be opposed: it is an exercise in fiscal illiteracy. That's about the kindest thing I can say about it