

The real problem we might face in the UK might be unpla...

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Inflation is a curious beast. That is, it is if you think about it [a little more than the average economist does](#).

The central banker's view is that all inflation is ultimately down to the availability of too much money in the hands of those consumers who must work for a living. This either creates demand-pull inflation, because those in work have already been paid too much, or it creates cost-push inflation because those workers are demanding to be paid too much in the future. In either case their answer is the same. The income of those in work must be crushed. Jobs must be lost. Poverty must be imposed. Recession must be endured. And it's all the fault of greedy, overpaid employees, whose spirits must be destroyed by forcing them into expensive debt for a significant period until such time as they learn their lesson and stop being greedy.

In the real world inflation is nothing like that. The current inflation has been caused by three things. One was the disorderly and unpredictable reopening after Covid, which few could have predicted when it happened because the pandemic was very clearly not over by then. This created short term demand that disrupted supply chains could not match. Inflation resulted.

The second cause has been continuing disruption in supply chains, whether for energy or other products, having been exploited by rent-seeking, profit maximising companies willing to exploit consumers who they believed had money to spend. In the confusion of reopening this profit-seeking behaviour became possible as price expectations had become disrupted during lockdowns that were released far too quickly, and without any, let alone adequate, planning.

Third, there has been war, which has exacerbated the energy price inflation dramatically and added in food price inflation in various ways.

In all this wage inflation has been below consumer price increases. Consumers have too little and not too much to spend right now.

The cause of the current inflation is in that case nothing like that which the central

banker's model suggests. Their prescription to cure inflation is also, inevitably, wrong in that case. So, more than ever what they are doing simply looks like a case of class warfare being waged by them rather than any form of rational economic policy. Interest rate rises, themselves inherently inflationary because they increase the cost of money, are no solution to this crisis.

What is then? The key to answering that question is to understand what is likely to happen in the medium term, once the short term inflationary pressure we are now facing ends. I make three assumptions. The first is that the war in Ukraine will end, or (and I am aware of how heartless this sounds, and it is not meant to be) it will be contained in a continuing war of attrition around which the world economy will be reorganised. I think either of these is very likely. I accept the war could escalate, which changes everything, but I think it is unlikely.

Second, supply chain disruptions will resolve as the world comes to an accommodation with Covid. I think that may be a very costly accommodation as it becomes apparent just how harmful this disease will be in the long term, with likely significant falls in life expectancy resulting, but again, purely economically that accommodation will be found.

Third, in a stabilised world profit-taking, whether by second-hand car dealers, or banks, or energy suppliers, will be harder to sustain. In most cases prices that are currently being seriously inflated are likely to fall significantly, as supply chains are sorted and a new stability returns. Second-hand car prices will return to normal. Interest rates will decline to near zero again. And fuel prices will go down, significantly, not least as green alternatives kick in. I only see a possible exception in the case of food. There real disruption resulting from sanctions on Russia and disruption in Ukraine will have an impact for longer, but again, consumer patterns may adapt to counter this.

Overall, what this means is that in the medium term I suspect significant price falls are going to be seen in the economy. There will quite likely be deflation. Even the shortage of money in consumer hands, which I think will continue, not least because of the combined callous indifference of central bankers and many governments, will require this. Businesses will ultimately be forced to price their products to what the market can afford or go out of business.

Why raise this issue now? Because what it suggests are three things.

First, if inflation is to be a short term phenomenon what are required are fixes that take the peaks out of the price rises. That is things like cutting duties and indirect taxes, whilst simultaneously helping those in real need. Smoothing the path back to normality is what is required, and large wage increases are very unlikely to become the new normal as yet, even if central bankers think otherwise.

Second, windfall taxes and taxes on those parts of the economy where inflationary pressure is real because there is too much money in well-off consumer's hands are

necessary. So, energy company profits should be taxed more. Banks should also be looked at. But so too should taxes on high income and wealth rise as this where the inflationary pressures are.

Third, we need to invest. When there are falling prices investment falls as people defer spending, presuming goods will be cheaper in the future. There is a strong recessionary element to deflation in that case. So, investment to create jobs is essential and the planning has to happen now.

Is there anything we do not need? There is, of course. That is interest rate rises that can only make all the current scenarios worse.

If only central bankers would stop waging class warfare and did instead actually think about the causes of the inflation we have we might get significantly better policy to manage our current economic crisis. I am not confident that those in charge are capable of that though. And that's the worry, because if we get deflation, which I think much more likely than stagflation, we are in more trouble and won't have prepared for it, yet again.