Funding the Future

The interest rate paid on government debt is not the bi...

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As the Guardian has noted this morning:

Fears of a long recession and the likelihood of higher public spending to cope with the cost of living crisis have sent the interest rate on Britain's debts soaring towards its biggest monthly rise in almost 40 years.

Ten-year UK government bond yields, which are a proxy for the effective interest rate on public borrowing, hit 2.78% to register the biggest monthly rise since September 1986.

Heaping pressure on the incoming prime minister to address the Treasury's worsening financial outlook, some analysts predicted the yield would increase before the end of the year to at least 3%.

I think there is a massive lack of perspective in this report.

Inflation is over 10%. It may not stay that way. It probably won't. With luck interest rates will fall as well. But, right now these interest rates are massively negative. In reality the interest cost is not in any way making up for the fall in the value of the capital saved in government bonds. The rate is, actually, therefore, at a real massive low point.

Now turn that on its head. This means that this year something like £200 billion of government (valued as it was before this inflation hit) might be taken off the real value of government debt. It is falling massively in real terms as a consequence.

The debt botherers should, of course, be very happy abut that. I am not. Firstly, this means that opportunities for people to save with the government are, in real terms being reduced.

Second, it means that the money supply is being reduced when it needs to increases.

Third, it means that a massive opportunity to do QE at a time when bond values are low (they move inversely to interest rates) is being missed.

And fourth, if interest rates are in real terms negative this is still the moment to borrow.

But instead the fuss is about the cost, wholly missing the issues that really need to be discussed and fuelling the austerity agenda instead.