

Truss's plan to borrow to spend is inexcusable when the...

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I have posted this [thread to Twitter](#) this morning:

Truss apparently has an energy plan. What is more we are to hear about it today. It sounds expensive, because it will subsidise those who do not need support. But it will also, apparently, be funded by borrowing, and that is bizarre (to be polite). A thread....

I will discuss the strengths and weaknesses of whatever plan Truss announces today when we know more details of who it will support. The one thing we do apparently know for sure is that the £130 billion (or more) cost will be paid for with borrowing. That's not necessary.

When it comes to funding its spending there are three choices available to any government. It can tax. It can seek to persuade savers to deposit their money with it, which is usually and incorrectly called borrowing. And it can create new money to pay for the spending.

It seems that Truss is planning to 'borrow' the funds that she needs to deliver this plan. What that in effect means is that she is planning to push up the interest rate the government offers to savers to lure money from institutional funds into government bonds, or gilts.

Let's be clear what those institutional funds are. They are pension funds, banks, insurance companies and others who manage money on behalf of others. The higher interest rate will be required to persuade them to reallocate funds to gilts, as government bonds are called.

The current interest rate on government savings varies depending on what precisely is on offer, but is around 3%. If Truss wants £150 billion more that will increase: 4% is quite likely. That, for the UK government, is very expensive money in terms of recent history.

So, the question is why is Truss going for this very expensive option when there are alternatives?

Tax is one such alternative. The current UK windfall tax is absurd: it will raise £5 billion when excess energy company profits might easily exceed £150 billion as a result of this crisis. But inexplicably Truss is refusing to tax this money.

No doubt Truss could also do a windfall tax on bank profits, which I expect to increase by around £40 billion or more as a result of increasing bank interest rates, which they have done nothing to earn. But again, I am not expecting action there either.

Give or take, there may be £200 billion of such excess profits in the economy soon (which will represent the cost she will be paying out from the government) and right now the tax take on this at ordinary rates will be less than £45 billion.

If the overall rate were increased to, say 60%, that take would rise to £120 billion. Could any company object? Well, of course they would. But my argument is let them: these are windfall gains arising through no entrepreneurial action of their own.

At a time of national crisis the companies should be grateful for the chance to keep 40% of their ill-gotten riches. They won't see it that way. I don't care. My concern is that £120 billion of borrowing could be prevented as a result.

What else could be done? The next alternative is to simply borrow the money required to pay for this energy package from the Bank of England. It can do this.

There is a facility called the Ways and Means Account that could simply let the Bank of England provide the government with an overdraft of the required sum.

And it need not charge interest on the loan either, because the Bank of England is owned by the government anyway, making charging interest on the loan irrelevant.

I know that to do this would be unconventional, to say the least. It would also have contravened EU requirements but I would have thought the government should have noticed we are no longer in the EU, and so can do this.

The advantage is very clear: it is that the pressure to increase interest rates on government borrowing would not then exist, and that means rates will not be forced up in the market more generally.

Right now the last thing we need is an increase in interest rates, forcing people with mortgages to default on their debts. If direct lending from the BoE to the government could prevent that it would be a very good thing.

Then there is the last alternative, which is Bank of England lending to the government disguised as quantitative easing. The net effect of this is the same as the BoE lending

direct to the government. QE is only done to get around the EU rule that such lending should not be done.

In a QE deal the Treasury could issue a £150 billion bond to the financial markets tomorrow, making it clear that the Bank of England will buy it back in a week's time. The financial markets will then get a risk free cut on the arrangement to make them happy.

In effect though, there would be no new net borrowing from the financial markets, excepting a one week period. In effect the BoE lends direct to the government under QE, and pretends it is not, which is a stupid game but one that has been played.

Is direct lending by the BoE to the government better than QE? Of course it is: no bung is given to the finance markets for partaking in a wholly unnecessary arrangement. That's the win.

But let me address the problem in both these schemes involving the BoE creating new money for the government to spend, which is what the BoE lending to the government really involves, however it is disguised.

That new money that the BoE creates as a rule of this lending has to get from the government into the real economy, which is you, me, businesses and everyone else. It moves from the government to the economy via our commercial banks.

In effect, the BoE puts money into a special type of deposit account that only the commercial banks can have with the BoE. There is over £900 billion in those accounts right now. And interest is paid on them at the BoE base rate.

There is no law requiring that interest be paid on these accounts at the BoE base rate. Before 2008 nothing was paid on the balances. But since QE happened and the balances have risen this interest rate has been paid.

This was not a problem when the interest rates were as low as 0.1%. The cost to the government was next to nothing and the issue was ignored.

Now the interest rate is 1.75% and by Christmas it may well be 3%, and by next year 4% is thought possible. The cost is rising rapidly: it could be £40 billion next year, paid on money gifted to the commercial banks.

This is unnecessary and a complete waste of money. To avoid this charge, the new money needed to tackle the crisis should not be injected into the economy via those accounts but via new accounts where the rate paid should be fixed at 0.1%, forever.

This would be legal. And it would be better than a windfall tax on these profits because it would simply stop the banks profiting in the first place.

So, of the four options (tax; inducing savers to deposit funds with the government or borrowing; direct lending by the BoE; and QE) which is the best?

Not taxing windfall profits is inexcusable. There is no other word for it. Truss will not do it because she believes in making the rich richer. That is the only explanation I can offer for her refusal. Anything else she says makes no sense.

Increasing government deposit taking, or borrowing, requires interest rate rises and the effect of this on mortgage holders and on renters, where rents tend to increase in line with mortgage costs, will be as bad as the energy crisis for many households, so it has to be wrong.

Then we come to the Bank of England lending the money to the government either directly or using QE. Direct is best because it is honest, and cheapest. And it is legal. And if the BoE governors would not do it they should be sacked.

If, however, international niceties are to be honoured even though we are not in the EU, QE could be used instead. And if in both the last two cases the interest rate to banks was limited the cost could be minimal.

What is clear is that of all the available options Truss will be taking the worst. The question is, why is she doing that? Could it be that this is the one that maximises the return to energy companies, banks and the wealthy? I have no other explanation.