Funding the Future

It really is time that Labour got its economic act toge...

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The Labour Party issued the following press release yesterday for use by newspapers (and 0thers) this morning:

Britain paying £251 billion "Tory bond blackhole" as collapse in Treasury bond fund revealed

A Treasury fund originally designed to profit from the Bank of England's quantitative easing programme has turned from a **£73.6 billion asset** into a **£177.6 billion liability** in the space of just three years, shock new figures have revealed.

The black hole in the Treasury's bond fund began to appear during Rishi Sunak's term as Chancellor, but dramatically increased in size as a result of the economic crash triggered by last September's 'Kamikaze Budget'.

According to the Treasury's latest statement of its 'group financial position', the fund went from being the biggest asset on its balance sheet in March 2020 to its biggest liability at the end of March 2023, thanks to the **£251 billion decline in its value**.

That is equivalent to 10 per cent of the UK's gross domestic product in 2022, or the entire GDP of Scotland and Wales combined. In spending terms, it would pay for the running costs allocated by central government last year to every school and police force in England, every branch of the armed forces, and the whole of NHS England.

In terms of losses for the taxpayer, it represents a cost of £8,900 for every household in the UK and is 76 times the amount that was lost by a previous Tory government during the exchange rate chaos of Black Wednesday in 1992.

As a result of these losses, the Treasury's calculation of the returns that the taxpayer has made over the total lifetime of the fund has also shifted from a £128 billion net profit at the end of March 2021 to a £58.8 billion net loss at the end of March 2023.

As recently as July 2021, when Rishi Sunak was Chancellor, the Treasury's annual report for 2020/21 dismissed the prospect of the taxpayer facing a net loss over the lifetime of the Treasury's bond fund as a "remote possibility".

The figures were slipped out in the Treasury's annual accounts for 2022/23, one of 108 'transparency' publications issued by the government on 20 July to coincide with the start of the Parliamentary recess and the three by-elections held on that day.

Rachel Reeves MP, Labour's Shadow Chancellor, said:

"Families are already feeling the squeeze from what feels like an endless Tory cost of living crisis. Now they face yet another hit thanks to the Conservatives' catastrophic mistakes in managing this fund. This Tory bond black hole will land working people with another astronomical bill for years to come.

"And it leaves them paying the price for the failings of successive Tory Chancellors: the hubris of George Osborne thinking this fund was a one-way bet, the complacency of Rishi Sunak ignoring the warning signs in the bond market, and the recklessness of Kwasi Kwarteng turning a crisis into a disaster.

"All of them are guilty of putting their short-term political ambitions ahead of the long-term economic interests of the country. That will only change when we have a Labour government in place, determined to rebuild the foundations of economic responsibility, and give Britain the more secure, more resilient economy it needs."

I struggled to find an appropriate technical description for this press release and decided in the end that the word 'drivel' best fitted the bill, because that is what this is, from beginning to end. Even more worrying is the possibility that Reeves does not realise this.

If Reeves really understood what was going on in the accounts of the Treasury and the Bank of England then she would know three things.

The first is that there is no such thing as the fund she refers to. What she would instead acknowledge is that in reality the Bank of England does not, and never has, run the quantitative easing programme. That has always been a Treasury operation. There are two ways to know that. One is that there are letters between the BoE and the Treasury that confirm that all losses on quantitative easing operations would always be borne by the Treasury - meaning that they alone were always accountable for them. Second, the Bank of England does not consolidate its supposed QE operation into its own accounts precisely because it has no liability for them. So, what Reeves should be saying is that throughout its life QE has not been properly accounted for and it is now time that it was, within the accounts of HM Treasury and not within a supposed Bank of England subsidiary. However, since that would shatter the myth that she also promulgates that the Bank of England is independent of government she will not do that.

Second, Reeves should stop pretending that there is any black hole in the government's accounts as a result of it issuing its own bonds. There is not. There are, again, several reasons for saying so.

Of these, perhaps the most important is that the whole of this analysis is based on the logic of mark-to-market accounting. In other words, the report is based on the logic that the Treasury might immediately make the sale of its whole portfolio of bonds, issued by itself, under the quantitative tightening programme. This would undoubtedly give rise to a loss. However, the assumption is absurd. There is no need (literally none at all) for the Treasury or the Bank of England to sell these bonds. Logically they should all be held to redemption, at which point the loss would be vastly reduced. Reeves should have recommended that. But again, that would challenge the logic of Bank of England's independence and so she will not do that.

What Reeves should also be doing is asking why on earth it is that the Treasury is preparing its accounts on the basis of International Financial Reporting Standard accounting standards. As the **IFRS Foundation** **says:**

The objective of general purpose financial reporting1 is to provide financial information about the reporting entity that is useful to existing and potential investors, lenders and other creditors in making decisions relating to providing resources to the entity.Those decisions involve decisions about:

(a) buying, selling or holding equity and debt instruments;

(b) providing or settling loans and other forms of credit; or

(c) exercising rights to vote on, or otherwise influence, management’s actions that affect the use of the entity’s economic resources.

In other words, accounts prepared on this basis are prepared on the assumption that users are going to buy or sell shares in the entity preparing the accounts, or might have doubts about its commercial creditworthiness. This makes the standard wholly unsuitable for use by a government that a) has no shareholders and b) is the ultimate credit-worthy organisation as it is the ultimate creator of all money. Reeves should be saying this and suggesting alternative government accounting be used, but she is not.

My third concern is that Reeves should be saying that this issue has arisen solely and only because of increases in Bank of England interest rates. That is the precise reason why the value of the binds in the QE programme has fallen. There is no more to it than that. To claim anything else is wrong. But she supports those interest rate rises. She should not for reasons I note elsewhere today, but she does, and so she is as much responsible for this situation by saying she would do nothing to change those rates or by removing the Bank of England's power to set them as the government is.

In summary, unless Reeves is willing to both understand an issue and then say how she might address it, I cannot see what she is doing issuing utterly meaningless press releases that do not address any of the issues that she claims to be talking about or even indicate that she understands them.

It really is time that Labour got its economic act together, but this press release suggests it has no clue how to do so.