

Funding the Future

Article URL

Published: January 12, 2026, 5:41 pm

The [Guardian has reported](#) this morning that:

The Bank of England may be forced to bring forward the date of its first interest rate cut after three leading forecasters issued a surprise update suggesting the inflation rate will halve to 2% by April.

The Oxford Economics consultancy and analysts at Investec and Deutsche Bank have reassessed their outlook for inflation in 2024 and concluded that the consumer prices index (CPI), which dropped to 3.9% in November last year, will fall below 2% within four months.

I am far from surprised. As all those (limited number) of commentators, like me, who were quite certain, based on the evidence, that inflation would be transitory have always said, this was inevitable. Inflation rates always revert to the mean quite quickly after the type of inflation shocks we had in late 2021 and early 2022. After all, why wouldn't they? When the shock passed (as shocks always do) and given that inflation measures a rate of change over a twelve month period, predicting that rates would fall back to 2 per cent or less in a couple of years at most was one of easiest forecasts to make.

There was never a need for interest rate rises.

What is more, those rate rises have made no difference to the inflation outcome, as yet, because of the extended (minimum two-year) time period that they need to work.

No action by any politician has produced this fall in inflation.

The Bank of England deserves not one iota of credit for it happening.

This fall in inflation is all down to one thing, which is the simple passage of time.

And the only thing that would be required to return the economy to some sort of stability, presuming the Bank of England had not so grossly misunderstood what was happening when the comprehension of inflation is the sole economic task asked of it, would be to allow wages to now catch up with price rises, restoring purchasing power to

the economy as a result.

What I do hope you noted in that last paragraph was the massive caveat. Note that I said 'presuming the Bank of England had not so grossly misunderstood what was happening'. The trouble was, they did grossly misunderstand inflation, in the most spectacular fashion. As a result, they did three things:

- * They massively increased interest rates, forcing them to levels that are way above the level that the economy can sustain when the long-term trend has been towards net zero rates. This has been an act of gross irresponsibility. It has also led to a serious short-term upward redistribution of wealth in society.
 - * They have tried to force wage rates down, in the process trying to reinforce the redistribution of income and wealth in society, at most obvious cost to the young, those on lower wages and those who have the temerity to have to borrow to buy a home because their family cannot buy one for them.
 - * They have brought considerable pressure to bear on government spending, seeking to deliver austerity as a result. In this, they have been aided and abetted by the ONS methods of accounting for the national debt and government interest costs, both of which considerably overstate the consequences of borrowing.
- The result of this action on the part of the Bank of England is that we now face vastly greater economic risk in the UK than we ever did from the inflation that they thought they were tackling.

The biggest risk that we now face is deflation, from which there follows recession and even depression. This requires explanation.

We face the risk of deflation in the UK economy because, to some degree, the Bank of England is right: raising interest rates does eventually (but maybe not yet) reduce demand for goods and services in the economy. This is the result of more and more people being crushed by the burden of debt that falls upon them, which then reduces aggregate demand and so the prices for goods and services fall as a consequence. There is now a very strong likelihood that this will happen over the next couple of years as the impact of new high-interest-rate mortgages really hits the economy. We will, however, already have very low inflation rates by then, and so the chance is that we will tip over into deflation.

There will be those who think that deflation is a good idea, but they will do so from the position of economic ignorance. The fact that prices might go back to where they were in 2021 is not necessarily good news. That is because deflation has a host of unwelcome consequences, of which some are as follows:

- * Falling prices, whilst some business costs such as wages are fixed, give rise to an immediate downturn in business confidence and a simultaneous increase in the number of business failures as profitability disappears almost in an instant.
- * Failing businesses will inevitably put downward pressure on wages because unemployment will rise.

* Declining income for households with debt will create enormous problems. Their loan obligations will be of a fixed value in pound terms, but their incomes might actually decrease in those same terms, i.e. their debt burdens might rise, even if interest rates fall. The longer deflation lasts, the bigger this risk is.

* Interest rates might tumble, but so will borrowing for three reasons. The first is that businesses and households will not borrow to buy capital items, because they will believe that those items will be cheaper next year. Expenditure will be deferred. This fuels a recession. Second, banks will understand that the capacity to repay debt will fall within the economy and will impose strict credit limits. In a consumer credit-driven economy, this will again increase the risk of recession. Third, people will also be reluctant to borrow when they know that the real cost of repayment will exceed the apparent cost of the items that they acquire.

Put these factors together and a very ugly economic situation results.

Presuming that government revenues also fall, and presuming that we still have a government dedicated to balancing its books, as both our major political parties are, you then get the government trying to cut spending at a time when the need for greater activity on its part will be essential, and that too could fuel recession.

This situation is entirely foreseeable now.

What do we need to prevent this now? I suggest three immediate things:

* Very rapid cuts in interest rates.

* An automatic right for mortgage holders to break long-term deals signed in the last eighteen months because that is all they were inappropriately offered.

* Significant plans by the government to boost its spending to counter the coming recession. These would have to relate to a Green New Deal and do nothing to promote asset price inflation when those prices are the one thing in the economy that can fall to advantage, albeit hopefully in a controlled fashion.

This is the economic need now.

What is the chance that any politician will deliver this? Close to zero, I suspect. Buckle down for a bumpy ride. Things look as though they might get much worse, very soon.