

We are being governed by economic irrationality

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Inflation rates are tumbling in Europe, the UK, and the USA.

Despite what mainstream economists in all these places suggested, which was that this would not happen until significant unemployment was created, which desired increase in unemployment required an increase in interest rates to precipitate an economic crisis requiring that redundancies happen, the reality is that the impact on unemployment of those rate increases has, so far and thankfully, been limited and inflation has fallen anyway.

Those who, like me, argued that inflation of the sort that we suffered was always going to be transitory would appear to have been proven right; that is exactly what it was.

However, despite this, the European Central Bank retained its high level of interest rates this week, and no one expects the US Fed to cut its rates next time around, and nor does anybody have any realistic hope that the Bank of England will do likewise.

What we now have is a quite extraordinary economic situation. Although it is now apparent that there never was a reason to increase interest rates, high interest rates are being maintained, nonetheless.

As a result, economies that have survived for over a decade on negative real interest rates are now having to endure positive real interest rates, i.e. base rates of interest that are in excess of the rate of inflation. What we can be sure of is that these positive real interest rates will do three things.

Firstly, they will redistribute income and wealth upward in society.

Second, they will penalise those who borrow, significantly reducing their capacity to spend. That reduction will be suffered most by the young and those on low incomes, who tend to have greater borrowings in proportion to income. The downward economic multiplier effects of that will be significant.

Thirdly, this creates the possibility that although it is now very clear that unemployment

was not needed to reduce inflation we will get a recession and significant unemployment anyway as a consequence of the positive choice of central bankers to perpetuate these high rates of interest.

In that case, it is appropriate to ask what is motivating central bankers in their clearly stated desire to maintain high rates of interest when there is no identifiable economic need for them now if ever there was.

So far, the only explanation that those central bankers can provide is that they fear that there will be inflation in the future, although they cannot say from where it will come. Nor can they explain why high interest rates will be any more appropriate as a tool to deal with the inflation that they fear than it clearly was not with regard to the last round, where rate rises clearly had no impact on the fall in inflation.

We are, therefore, left with a situation where central bankers' self-serving and self-fulfilling paranoia about inflation provides cover for the redistribution of wealth within society while simultaneously creating a recession with cost to the majority without there being any logical explanation for their fear that supposedly motivates the retention of high interest rates in the economies of Europe and the USA.

To put it another way, we are being governed by irrationality, and politicians appear to think themselves helpless in the face of this fact as if the power of democracy is to be sacrificed to the whim of financial ideologues who have lost any sense of rational ideology.

As a recipe to precipitate the collapse of economies and to create a consequent invitation to fascists this approach makes sense. In every other context, it can only be seen as deeply dangerous.