

## Labour without the pain

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This morning's video repeats a theme that first aired here yesterday because there is, overall, little overlap between this blog's readers and my YouTube viewers. In the video I argue that Labour claims it has a “black hole” of £22 billion to fill in the government's finances, but they should stop making a fuss. Doing so would be easy. There are at least six – and maybe more – ways to do it.

[https://www.youtube.com/watch?v=eo-cgUtD9Lw?si=mm7UpD4\\_\\_p7zbTPM](https://www.youtube.com/watch?v=eo-cgUtD9Lw?si=mm7UpD4__p7zbTPM)

The audio version is here:

[https://www.podbean.com/player-v2/?i=g8rnb-16b9f6b-pb&from=pb6admin&share=1&download=1&rtl=0&font=Arial&skin=c73a3a&font-color=auto&logo\\_link=episode\\_page&btn-skin=ff6d00](https://www.podbean.com/player-v2/?i=g8rnb-16b9f6b-pb&from=pb6admin&share=1&download=1&rtl=0&font=Arial&skin=c73a3a&font-color=auto&logo_link=episode_page&btn-skin=ff6d00)

The transcript is:

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There are at least six ways for Rachel Reeves to fill her so-called economic “black hole”.

She says that there is a £22 billion black hole in the UK government budget. I have to dispute that because, technically, it is impossible for the UK government to have a black hole in its budget.

There's good reason for saying that. When the UK government spends, the Bank of England creates money to enable it to do so. It does not wait for tax revenues to come

in. It does not have to borrow. It simply, so long as it has passed a legal budget, tells the Bank of England to make a payment on its behalf, and they have no choice but make that payment because they are legally required to do so. As a result, there is always the possibility that the Bank of England can extend an overdraft to the government to cover its so-called deficit. And, as a consequence, there can never be a black hole. It is a technical impossibility.

It's also a technical impossibility for there to be a black hole because, as history has proven, if the government spends new money into the economy, it can tax it back. It is the actual process of spending that creates the capacity to pay the tax. In fact, you couldn't pay tax unless the government had created the money to make that payment of tax in the first instance because it would not exist. Therefore, spending always has to come before taxation.

But if the government decides not to tax back everything that it spends, and it can if it so wishes, it can instead offer those who are left with some of the new money that it has created the opportunity to save with it. That savings opportunity comes in the form of government bonds, or gilts as they're called in the UK, or by way of depositing funds with National Savings and Investments, which is the government's own savings bank. In either of those cases, the money not taxed back can be lured back into the government's coffers because it has the ability to offer any interest rate it likes to make sure that that happens.

And as a consequence, the chance that there will ever be a black hole as a consequence of government spending is, for all practical purposes, precisely zero, because the government can always recover the money it spends. In that case, it is a ludicrous claim that there is a black hole, but Rachel Reeves is making it, nonetheless.

We can ask questions about her financial literacy for actually making the claim. But, instead, let me put forward six ways in which she could fill that supposed black hole that she claims exists.

The first I've already mentioned. It is that the Bank of England could offer an overdraft to the government. It did this in March 2020 when the Covid crisis started. It said then that the government could have an overdraft of £20 billion, which was terribly generous of it given that the government owns it. And in practice it used to offer a facility much bigger than that to the government on something called the Ways and Means Account, which was, broadly speaking, taken out of use in 2006. That overdraft facility would, of course, fill the black hole.

Alternatively, the government could issue a new bond for £22 billion pounds and it could say this bond is only going to be available on the market for a week, after which it's going to buy it back again via the Bank of England.

This is, of course, quantitative easing. And, announcing it in advance, the City would

happily go along with the arrangement, and there is ample capacity for new quantitative easing in the UK economy at present, and therefore, this would work. The black hole could be filled that way, straightforwardly, simply, and with no fuss and no upset to any market, anywhere.

The third option is even easier. You could just issue that bond and not buy it back. And the City of London would buy it. There is no doubt about that. In other words, this black hole can be filled.

What's the fourth option? The fourth option is a quite straightforward one. And that is, to tell the Bank of England to stop its quantitative tightening program.

Quantitative tightening is simply the reverse of quantitative easing. QE involves the government, via the Bank of England, buying its own bonds back from the financial market. It did £895 billion worth of such purchases between 2009 and 2021. Quantitative tightening involves selling those bonds back into the financial market.

That process is underway at present at the Bank of England. They have sold £200 billion of the bonds that they bought between 2009 and 2021 back to the financial markets, and the only reason they have done so is to keep interest rates high.

That has worked. Interest rates have remained high. But we do not need high interest rates in the UK economy anymore. Therefore, it could end the quantitative tightening process, and if it did so, then the capacity to sell new bonds to cover the government's deficit would exist.

For example, the Bank of England sold £33 billion of old bonds into financial markets between April and June 2024. Therefore selling £22 billion worth of new bonds if the Bank of England stopped the sale of old bonds would be incredibly easy. In other words, the deficit can be covered again.

What's the fifth way of dealing with this? Well, I've already mentioned that we don't need high interest rates, so Rachel Reeves needs to have a quiet word in the ear of Andrew Bailey, the Governor of the Bank of England and say, "Come on, time to drop those rates. Get on with it now."

Frankly, rates are two per cent too high at present. Inflation is running at around 2 per cent. We know that's going to continue. A three per cent base rate would be more than enough to provide a positive net interest rate, which is what the Bank of England's goal is. Therefore, drop that rate by 2 per cent and the government would save more than £22 billion pounds a year in interest cost. Deficit solved.

And finally, there is, of course, the option of raising tax. Tax need not go up on, what Keir Starmer likes to call, working people, but which in fact includes anyone, whether they work or not, because everyone, from children to pensioners, do actually pay tax in

various different ways. So, what taxes could be chosen which would not penalise those on lower incomes? There are some obvious cases.

First of all, capital gains tax could be equalised with income tax when it comes to tax rates. At present, most capital gains are charged at half the income tax rate, and that is ludicrous. It is a straightforward bung to the already wealthy, who are the only people who make capital gains. If those rates were equalised, we could raise over £12 billion a year in extra tax revenue. And that, I suggest, should be done.

We could, as an alternative, cut the higher-rate tax relief on pension contributions because that is a £14 billion a year bung to the already wealthy who are saving in pensions and who get double the rate of tax relief on their pension saving that people on lower rates of tax get, which is totally and utterly unfair and unjustifiable and does not reflect the tax rate that they will pay when their pension is eventually paid out to them in retirement, when almost certainly they will be lower rate taxpayers.

What else could we do? We could add VAT onto the payment for financial services. There is no such VAT charge at present. Financial services supplied to the wealthy, because nobody else buys advice on financial services, is currently exempt for the purposes of VAT. Add VAT at 20 percent and more than £8 billion a year could be raised in additional tax revenues.

I have already suggested enough tax increases here to cover the £22 billion deficit, but if you want some extra reliefs that you could look at and remove, add in the end of business property relief and agricultural property relief in inheritance tax, which simply reinforce the concentration of wealth in society for no overall net economic gain, and that would add another £5 billion as well.

In other words, Rachel Reeves has plenty of ways of using taxation on the wealthy alone to increase the revenues that she can enjoy and, therefore, clear her deficit.

So, why are she and Keir Starmer talking about the need for pain? I simply don't know. Either that's because they are economically illiterate, and we have to consider that possibility, or it is because they want for some reason to impose pain via austerity, which means that we will have a reduced quality.

of government services.

We don't need to suffer those things. We could have all the services we need. Not only could Rachel Reeves cover the £22 billion deficit that she claims the Tories have left for her, but she and Labour could have a vastly more ambitious programme for themselves in office to solve the problems in the NHS, in education, in social care, and in so many other areas in society.

They could do that. The capacity to deliver exists. But they aren't willing to do it. I don't

know why. It is quite absurd that she doesn't know that these possibilities are there. But they do exist. And I will talk about them. Because it is vital that there is public awareness of the fact that this austerity and this pain is unnecessary, and Labour shouldn't be doing this.