

Funding the Future

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I published this video in the Economic Truths series this morning. In it, I suggest that it's an economic truth that every time a government spends, it creates new money to do so. It does not spend what is commonly called taxpayers' money, nor does it spend funds borrowed from the City. It simply asks the Bank of England to make a payment—and that's what that Bank does, extending an overdraft to the government to let it do so.

<https://www.youtube.com/watch?v=6ntd72cTLQU>

The audio version of this video is here:

https://www.podbean.com/player-v2/?i=x7h5b-1688a74-pb&from=pb6admin&share=1&download=1&rtl=0&fonts=Arial&skin=8bbb4e&font-color=auto&logo_link=episode_page&btn-skin=ff6d00

The transcript is:

Governments create money when they spend. This is an economic truth.

I've been talking about other economic truths in a whole series about money, which are linked below. But in those videos, I was talking about the money that is created by our commercial banks when it lends and how that functions within our economy. But the fact is that we have two sources of money in our economy. One is the money created by commercial banks, and the other is the money created by the government.

The fact is that every time the government spends money - and remember, it spends a trillion or so pounds a year - it does not go to the Bank of England and say, "Hey, is there any money in the account? Can I spend it today? Or should I actually hold back for a day or two until some more tax is paid?" That is not what goes on.

Instead, Parliament authorises the Government to spend by the passing of a budget. Once the budget has been passed, the spending is legal and it can therefore take place. And the government then goes along to the Bank of England, which it owns, and says, "We now want to spend this money, which Parliament has approved, therefore please extend the credit to us to let us do so."

And so, the Bank of England, quite literally, marks up an overdraft for the government every morning, as it starts to spend, and lets it go spending on whatever it wishes because it is a bank and it can extend credit because the government has made a promise to repay it, at least technically. Now, that's what happens, therefore. Every time the government spends, it creates new money.

Just like a bank does not lend out depositors' money, the government does not use taxpayers' money to spend. This idea that taxpayers' money is used to pay for government services is wrong. It is complete and utter nonsense. It is untrue, a fiction, a falsehood. I don't mind what else you want to call it. It is simply not correct.

The government creates every single penny that it spends by asking the Bank of England to extend it an overdraft.

Now it is entirely true that every day, tax will come into the government. That is a fact.

And therefore, as a matter of fact, every day, part of that overdraft, or even all of it, will be cleared by the tax receipts received during the course of that day.

But that's not the point. When the government spends, it creates new money, and the receipt of the tax clears the overdraft. It doesn't fund the expenditure.

Now, unless this is understood, you don't understand how government finances work. Because anybody who thinks that the government is funded by taxpayer money is wrong. There is no such thing as taxpayer money. There is simply a bill that a taxpayer owes to the government for the tax that has been demanded by them, again authorised by Parliament, which is what makes it legal. Without an authorisation from Parliament, taxation is most definitely not legal.

So, you have to remember this fact. The government spends money. And then it taxes. The tax that is charged to cancel the overdraft that is created by the government at the Bank of England as a result of its spending, is charged quite deliberately to cancel that overdraft. It literally takes the money created by government spending out of circulation again.

This is, therefore, exactly akin to the way in which a commercial bank works. A commercial bank lends money to somebody, and then the loan it has made is repaid, and the new money that was created by the loan is cancelled, destroyed, it's gone forever.

The government creates a loan with the Bank of England by its spending, and then it taxes, and when the tax comes in, that tax cancels, destroys, in the same process, that money that was created to fund the government spending.

So, the government always creates new money by its spending and tax never funds government spending.

Instead, what tax does is cancel the impact of the money creation by the government. And of course it has to, because If you spent a trillion pounds a year and didn't tax, we would have inflation that would go through the roof.

But the reality is that we don't have inflation that goes through the roof. We never have had in this country. We've had some sort of high inflation every now and again, but nothing very serious. And the truth is that is because we have an extremely effective operating tax system which claws money back from the economy, which is what its job is.

That is the primary role of taxation. Unless you understand this cycle, which is that the government creates money to spend and then taxes it to cancel the impact of that spending, of new money, on inflation you don't get how the government's finances work. It is the most fundamental thing you have to understand.

And it's difficult because it's the other way round, like so many economic truths, from what you usually think, because it's the opposite of what a household does. And this is vital, because understand that and everything else about the government makes sense. And you also understand that most of what is said about the government is complete nonsense.

There is no taxpayer money.

The government does not run like a household. It does not have the sorts of constraints that households have.

And that's because it has its own bank, by the way.

And the government never, ever spends taxpayers' money. Because it can't. Because the taxpayers' money has been used to cancel the government's overdraft at the Bank of England.