

Funding the Future

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As the [Guardian noted](#) last night:

The UK government's long-term borrowing costs have reached the highest level since 1998 amid investor concerns over Britain's sluggish growth prospects and stubbornly high inflation.

The yield – in effect the interest rate – on UK 30-year government debt rose by as much as four basis points to 5.22% on Tuesday, above the peak reached after Liz Truss's mini-budget in 2022 caused turmoil in financial markets, to hit the highest level in 27 years.

This move was not predicted by the Bank of England.

I did not expect it.

But then, I did not really expect Trump's election, however bad the Democrat campaign was.

I also did not expect that Trump [would try to impose his madness on the world](#), that tariffs would occur, that a trade war would commence, or that he would seek to actively engage in the affairs of many other nations. It seems likely that all of those things are going to happen now. We are in another place.

But that does not explain why UK interest rates are so high. There is another explanation for that, and it is all down to the Bank of England policy.

Remember that this year, the UK [is expected to run a deficit](#) of around £140 billion. That is what, in net terms, it supposedly has to fund, presuming that the government will not borrow directly from the Bank of England, which it could.

But that is not all that is influencing the UK government interest rate. The Bank of England's quantitative tightening policy is also progressing at a rapid pace, selling vast quantities of UK government bonds back into financial markets for no financial gain for the people of the UK. In fact, the process is realising considerable losses for the UK government, wholly unnecessarily, but that is not putting a halt to it. Dogma comes

before any such concerns at the Bank of England.

The latest data we have on these sales comes from the Bank of England itself and [is for the quarter to September 2024](#):

Table A: Summary of stocks in the APF in 2024 Q3 ^(a) (£ millions)

Week ending	Gilts ^(b)
2024 Q2 ^(c)	695,024
3 July 2024	693,214
10 July 2024	693,214
17 July 2024	692,312
24 July 2024	691,329
31 July 2024	690,419
7 August 2024	689,501
14 August 2024	688,592
21 August 2024	687,649
28 August 2024	687,649
4 September 2024	687,649
11 September 2024	659,940
18 September 2024	659,015
25 September 2024	659,015

Source: Bank of England.

(a) The outstanding amount in each facility is reported on a settlement date basis.
(b) The overall stock of APF gilt purchases for monetary policy purposes, net of sales and redemptions, valued at initial purchase price.
(c) 2024 Q2 measured as the amount outstanding as of 26 June 2024.

In three months, the Bank of England sold £36 billion of government bonds. The aim was to drain money from the private sector economy to constrain growth. Simultaneously, the aim was to support high interest rates, which the Bank thinks necessary to control inflation. As a result, we experienced no growth and did get high interest rates. The policy was, in its own terms, very successful. It caused all the harm that it was designed to deliver.

And now, look at the reactions, which flow something like this:

"Panic, interest rates are rising."

"Panic, that means government costs will increase. How will it balance its books?"

"Panic, there is no growth. Tax revenues will fall. How will the government balance its books?"

"The government must cut its spending, even if that cuts growth and makes revenues worse, and may push interest rates higher as a result."

"Panic, the government must increase taxes as it cannot find spending to cut further."

"Panic, that means interest rates must remain high as the government is going to borrow more."

"Panic....this process will repeat, time after time, after time."

Of course, the process will not repeat, but under Rachel Reeves, it will.

This cycle could be broken in four ways.

First, the Bank of England could be told to stop quantitative tightening. The massive harm that policy is causing would come to an end. In particular, it is likely that interest rates would fall quickly.

Second, the government could say it will, if need be, use quantitative easing to fund its investment programmes for the time being, taking all the pressure off markets to provide funding in a way that would guarantee growth whilst reducing costs. Alternatively, it could just borrow from the Bank of England for a few months whilst markets stabilise. When the country is under threat of a coup from an external power, that would be a quite fair thing to do

Third, the government could borrow from the public at a cost much less than 5 per cent. National Savings and Investments could deliver much more than it does at around four per cent. Most of its products are paying at around 3.5% at present. It makes sense to do this, and why shouldn't savers benefit?

Fourth, the government does not need to balance its books. That constraint is solely of Rachel Reeves' own creation, and when times change, so should she.

There is no reason to panic, in other words. Options are available. Our problem is that the people in charge of our economy do not want to use them.