

# Funding the Future

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Politicians claim countries must be run like households, and that's completely wrong. In fact, most often, the exact opposite is true.

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And this is the transcript:

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The household analogy is the curse of the political explanation of the economy. Let me explain what I mean.

Politicians - and Rachel Reeves is a master of this - like to explain the way in which the nation's economics work by comparing them with a household. And there is simply no such comparison to be made.

A government is quite literally nothing like a household when it comes to economic understanding. The politician who uses the household analogy, as Rachel Reeves does when she talks about her mother balancing the household budget every month by checking the bank statement, is making a false comparison that is, to be candid, completely and deliberately misleading. So, I want to explain what the household analogy is, and why it's so inappropriate.

The first and most obvious point to make is that governments are not like households, and there are a number of reasons why. The first and most obvious one is that the government owns its own bank. Not only does it own its own bank, that bank is actually the creator of all the money in the economy.

The problem that the politician who likes to talk about the constraints upon the government because there is no money is referring to the idea there is no money left in the economy, the credit card is maxed out, the overdraft limit has been reached, and everything else. But that isn't true when you own your own bank.

When you own your own bank, you simply tell them to up the limit.

Or, as is the case with the UK government and the Bank of England - and has been the case, by the way, since the 1860s - if Parliament passes a Bill that says the government will spend, then the Bank of England is legally required to make the payment whether or not the government has any money in its bank account or not. It simply increases its overdraft.

You haven't got such a facility. Rachel Reeves' mother didn't have such a facility. But Rachel Reeves, as Chancellor of the Exchequer, has got such a facility. This is the difference between a government and a household.

One has a bank. One does not have a bank. One uses the currency that is created for the nation as a whole. That is the household. The other creates the currency for the nation as a whole. That is the government.

And what is more, the household might have to balance its books - because it eventually could run out of money if it doesn't, or it could go bankrupt - but the government can't. Because the government actually has to make the money for everyone else to use.

In other words, it has to run a deficit. And this is what politicians, it seems, do not understand. Unless the government runs a deficit via the Bank of England, then the Bank of England is not injecting new cash into the economy. And without new cash injected into the economy, two things can't happen.

One, inflation cannot be controlled because inflation demands more money, and if you do not inject more money into the economy to manage the fact that we think that overall a low rate of inflation is good for the economy, there is not enough money to meet the needs of society.

And secondly, growth requires that there be more money in use. And if the government doesn't supply it, it has to come through extending private sector debt. And we know that private-sector debt is much more vulnerable to failure than public-sector debt. In other words, the government has to run a deficit, whereas a household does not.

I hope by now you're already getting the idea that these things are different. But this isn't the only way in which they're different. There's another major difference. A household can dispense with expenditure, and it has no further consequence for the household.

So, for example, if I suddenly find that I'm very tight and I need to reduce my spending, I can cut out all holidays. It has no further consequence, bar the fact that I'm going to spend a week or two sitting around at home, rather than going to sun myself or whatever else I wish to do, wherever I want. That's it. We cut the cost, we don't have to worry about the consequence for someone else. That's what a household economy can do.

But a government can't behave in that way. If the government decides to cut its expenditure, somebody else's income falls. So, if the government decides to cut, for example, payments on the winter fuel allowance, the money available to pensioners to spend decreases. As a result, there is a reduction in the growth in the economy for which the government is responsible.

That's not the case if the household cuts its spending. Its income doesn't fall as a consequence of cutting its spending. But when you are the government, your income falls if you cut your spending. And the two are directly related. And that's clear from economic theory. And yet, it doesn't seem as though any minister actually understands this fact, because they keep on talking about the fact that we need to cut our cloth to suit our availability of resources, or whatever it is.

It's all nonsense. In fact, they are so inept about this point that they don't seem to understand that government spending actually increases growth automatically. Now, that, again, is not true of a household. If I overspend, I don't increase my income.

But if the government spends more - just as if it cut its income, there's less in the economy - if it spends more, there's more in the economy. These two are directly related.

It's not surprising. The formulas that are used to calculate gross domestic product, our measure of national income, actually reflect the fact that government spending is a part of national income. And if the government increases its spending, and there are resources available for it to spend money on, then that will increase our overall level of growth. That is not true of the household. It is true of government.

There's also another big difference, and that's when it comes to debt, if a household borrows money, it does have to repay it. That's the way it works. It goes to a bank and says, 'Can I have a loan?' And the bank says, 'Yes.' And then the household is obliged to make the repayment over time. If it doesn't, it could go bankrupt.

The government is in a totally different situation. It borrows money, and it, first of all,

borrows by and large on much longer time periods than the household does. Households, except for mortgages, tend to borrow money for only a few years at most, whereas governments can borrow for periods of up to 70 years in the UK at present. And secondly, when the government gets to the end of the loan period it doesn't have to repay the debt. What it does is simply issue a new debt to replace the one that it wishes to replace. It rolls the debt over, in other words.

This is how the national debt has continued since the 1690s, when it first began. And over that period, there's never been any serious attempt to repay the national debt, thank goodness, because otherwise, we wouldn't have a big enough money supply to sustain the modern economy. Instead, that debt has been allowed to roll over whenever it comes due for repayment. And the sum has simply increased.

There's another misunderstanding with regard to this debt as well. If someone, let's suppose, dies owing money, then in the household, that reduces the value of that person's estate. Very clearly, they have a liability that is due to someone. That's fine.

But in the case of the national economy, when the government owes money, somebody else owns it. And most of the ownership of UK debt is within the UK economy. Not all, but the part that is not owned within the UK is balanced by the fact that people in the UK own the debt of other countries. So, overall, the situation balances out. Broadly speaking, the total value of government debt owing by the UK government is matched by government debt owned by people. And when we look at this equation, what we see is there is no burden for future generations as a consequence of the government creating debt, because there's an asset to match it.

The lucky children in our society will in fact inherit a part of the national debt because their parents own it, or their grandparents own it. They will get an asset. This idea that the national debt is a burden on every child now alive is completely wrong. It will, in a sense, be a burden on some because they will not inherit the asset to match that debt. But, even then, they're never going to repay that debt. It's just going to be rolled over. So, this idea that household debt and government debt are the same thing is completely absurd.

There's also an intergenerational dimension to this, of course. Because there is a transfer between generations as a consequence. It isn't the case that future generations are going to repay our debt. The real issue is, will sufficient people inherit our debt? So, the government has a responsibility with regard to debt on an intergenerational basis, but the responsibility is to control excessive ownership of that debt through the management of excessive wealth. And I think that's a point that, again, is very little understood. This is not an issue for households, but it very definitely is for the government.

So, what we're coming up with is this absurd idea that there is somehow a similarity between households and governments when there's no similarity at all.

In fact, let's also look at the situation of what happens when things hit bad times. In a household, in a bad time, there will be a serious attempt by the householders to cut their spending, to balance their budget, which is what we have also seen governments try to do. That's what we call austerity. But actually, in bad times, the government has a duty to increase its spending.

Why? Because the private sector isn't spending and households are reducing their spending, and therefore there's a recession. And the only way to stop that recession is for someone to act counter-cyclically, as it is said. In other words, for somebody to start spending, even though the economic messages being sent out are that we are in a downturn. And the only agency capable of doing that is the government. So, the government has to behave in the exact opposite of the way in which the household does.

And by and large, that's true of pretty much everything I've said about this household analogy. If the household thinks it's a good idea to do something, pretty much you can say the government should do the opposite. Because they are the opposite of each other. The household is the microcosm of society. The government is the macrocosm of society. Its job is to manage the overall scene and to compensate for what goes wrong at the household level. It must take the opposite action to ensure that, overall, there is balance within the economy for which it is responsible.

When we have governments who believe they must behave like households, we get exaggerated downturns, we get exaggerated booms, we get credit cycles which don't work because there's too much credit at one point and too little at another, we get interest rate cycles which are destructive, and we get serious economic downturns, unemployment, and so on.

We don't need any of that, if only the government understands its job is to act as a government and not as a household. Would someone like to tell Rachel Reeves? Because it's really important that she begins to understand this right now.