

Funding the Future

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I was asked on the blog yesterday what the government could have done after 2008 to prevent the almost inevitable financial crash that I think is now coming our way.

I talked about [this potential crash in a video yesterday](#), referring to the latest Bank of England [Financial Stability Report](#), which makes it clear that they share my opinion. That was a good question, because what was said after 2008 was that we would not, of course, let this happen again. What seems very clear is that we will.

So what should we have done?

Splitting up banking

As many agreed in 2008, and as I proposed at the time, the most obvious thing that we should have done was to separate plain, straightforward day-to-day banking, on which we all rely for transaction processing, from everything to do with financial speculation. We should, in other words, have recreated the 1932 [Glass-Steagall Act in the USA for use in the UK](#).

The abolition of that Act by Bill Clinton was one reason why the USA fell over in 2008, which was the primary cause of the UK banking failure in that year. If we had enjoyed this separation, then the contagion from the speculative part of banking into the service supplier banking could not have happened in 2008, and it could not happen now.

The UK government promised it would do this, but never did so with any conviction, and the split has always been notional at best. There is now substantial backtracking on it. In fact, none of the essential protections were put in place when total separation was required. You cannot have a Chinese wall between these two activities within one limited liability operation. The two must be totally distinct. That has to happen now.

Publicly owned banking

Second, the government should have built a new publicly owned platform for transactional banking and required all providers of banking services to use it under

license from the government.

If this had happened, then if any private sector bank were to be at risk, the accounts and balances of that bank could have been automatically transferred into state control, and the access of its customers to the banking platform would not have been affected. The model of Network Rail and train operating companies, which have been able to fail without disruption is the basis for this.

This would have forever prevented the ability of the banks to hold the government to ransom, requiring that they be bailed out to keep their banking operations going in the event that they recklessly lost their capital. Instead, this requirement was ignored, and no one is still talking about it.

If it had happened then, firstly, we would now have the potential for a decent banking system, both supplied by the state and by the private sector, independent of the financial risk the private sector operators want to create at present, and secondly, banks could be allowed to fail without risk to the wider community.

Capital controls

Thirdly, and perhaps most importantly, we should have had capital controls.

Capital controls are the rules and tools that a government might use to regulate the flow of money into and out of its economy. They exist to protect a country from the destabilising effects of speculative financial flows, and most especially the hot money flows that can inflate bubbles on the way in and trigger crises on the way out of an economy.

There are several aspects of capital controls that require explanation.

- * First, capital controls are not exotic or radical. They are simply the financial equivalent of border checks. Every nation already regulates goods, people, and data crossing its borders in some way. Regulating capital is no different: it ensures that the financial system serves the public purpose rather than being captured by footloose cross-border speculation.
- * Second, capital controls come in many forms. They can include taxes on short-term inflows, minimum holding periods for financial investments, limits on foreign borrowing and lending by banks, restrictions on offshore lending, and reporting requirements on large cross-border transactions. Some controls are prudential. These are designed to strengthen the banking system. Others are macroeconomic and are designed to support exchange-rate stability or prevent asset bubbles.
- * Third, they work. Countries that have used capital controls judiciously, from Malaysia during the Asian financial crisis to Iceland after the 2008 banking collapse, have often recovered faster and with less social damage than those that did not. These controls gave policymakers room to cut interest rates, stabilise currencies, and support domestic recovery without being punished by speculators.

* Fourth, capital controls are a defence of democracy. Without them, governments are constantly held hostage by the threat that markets might withdraw funds if they disapprove of policy choices. With them, economic policy can be oriented toward public well-being rather than placating global finance. Controls weaken the power of hot money to veto democratic priorities.

* Fifth, capital controls are entirely compatible with a modern, open economy. They do not prevent productive investment, whether inward or outward, real trade, or long-term international cooperation. They ensure that capital entering a country does something useful, whether that be by building capacity, creating jobs, or supporting innovation, rather than fuelling a casino.

* Finally, capital controls express the fundamental principle that money is a public good, and its movement should support the stability and prosperity of the whole economy. In an age of globalised speculation, they are one of the few tools that can restore balance between democratic states and the financial systems that can too often otherwise seek to overwhelm them.

Capital controls are not about shutting the world out. They are about keeping destabilising forces in check so that society, and not speculative finance, sets the terms of economic life.

If we had had such controls, then we could have:

- * Managed interest rates better, particularly since 2021.

- * Reduced hot money flows into the UK, meaning greater stability for our exchange rate and greater opportunity to export for British businesses.

- * Limited the amount of money being lent for antisocial purposes, whether that be to:

- * inflate the housing market, or

- * to back financial speculation by hedge funds or private equity operators, or

- * for mergers and acquisitions.

None of these adds real value to the UK economy, but together they account for most of the lending by most UK banks, indicating how antisocial the nature of their operations is.

A British National Bank

Finally, we should of course have used this opportunity to create a state bank that would have guaranteed access to banking for everyone, but which could also have been used by businesses for the purposes of overnight deposit-taking, eliminating as a result the speculation in UK government bonds associated with the so-called repo market, which has been another cause of financial instability in the UK financial sector.

When businesses have to resort to such desperate measures because they know that the only agency able to guarantee them safety with regard to their money is the government, because the banking sector cannot, the government should accept its responsibility to provide that facility and not let a totally unnecessary activity be undertaken in its place at a cost to society at large.

This bank could also, of course, have delivered the mortgage stability that this country wants, as explained in my **Alternative Budget**, which also explains how this could have been provided with the capital it would require.

Conclusion

I could write more. My point is this: whatever is going to happen could have been avoided.

Tory governments did nothing to prevent it, and must take a huge part of the blame for anything that happens soon, as should Reform, because they would have made things even worse.

Labour cannot escape responsibility either. It has, by now, had the chance to indicate that it would do things differently, and has given no indication that it would in any way whatsoever.

So what do we need? Courageous politicians who understand money and are willing to take these issues on. Do we have them? Time will tell.

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