Funding the Future

The choice is clear: do we want more austerity, or an i...

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Financial Times columnist Stephen Bush has an article out this morning with the headline:

Austerity denial and the mystery of Britain's shrunken state

In it, is suggest that the apparent paradox of a British state that costs more but does less is real.

His suggestion is that since 2010, austerity has removed many services that once helped people before they reached a crisis, including youth provision, employment support, tax credits and assistance for poorer students. The state has consequently become increasingly concentrated on the sick, the retired and those already facing acute hardship.

Public spending has, however, still risen as a share of GDP, but that does not mean the state has become more generous. Weak economic growth has reduced the denominator against which spending is measured, while healthcare, debt interest and the costs of an ageing population have risen. The composition of spending matters as much as its total: more is now spent dealing with the consequences of social and economic failure, while less is spent preventing them.

This, he says, leaves Britain facing an uncomfortable choice. It can accept its present diminished state; rebuild public services and require a much broader section of the population to pay more tax; or shift more healthcare and age-related costs into private insurance, charges and co-payments.

His central claim is that no painless solution exists for the predicament we face. Politicians cannot promise better services, lower taxes and unchanged methods of funding at the same time. The difficulty is not simply the amount the state spends, but what it spends on, why those costs are rising and who is expected to pay.

Insofar as it goes, that sounds reasonable, but I stress the first part of this sentence, which is "insofar as it goes". Like so many journalists who know on which side their bread is buttered, Bush picks a big theme, creates a good headline, and then fails to explain the underpinning problem that he is addressing.

In this case, Bush fails to explain what economists call Baumol’s cost disease. This explains why services such as healthcare, education, social care and the arts tend to become more expensive over time, even when their productivity does not improve. The reason should be obvious, but like many things that should be, it is hiding in plain sight.

The reality the so-called disease highlights is that, over time, the manufacturing sector in an economy can become more productive because technology lets each worker produce more. Wages can therefore rise without prices rising by the same amount. So far, so good.

The problem is that many services cannot increase productivity so easily. A teacher still needs time to teach a class, a carer needs time to care, and a string quartet still needs four musicians and almost exactly the same time to perform, or the result might be truly terrible. But, and this is the crucial point, if we still want those services, the workers engaged in them must nevertheless receive wages comparable with those available elsewhere, or they will leave. The cost of providing their services does, therefore, inevitably rise even though their output per hour has changed little.

The crucial point is that in this case rising costs do not necessarily indicate inefficiency. They may instead reflect the inherently labour-intensive nature of valuable services.

There is, in fact, a deep paradox here. As productivity increases elsewhere, society can afford to devote more resources to health, education, care and culture. What is more, as we are sated with material goods, those services might be exactly what we, the government and our well-being require. The only problem is, in relative terms, they become more expensive over time, just as the need for them grows. Baumol’s law therefore explains why spending on these services will normally rise as a share of national income.

Our governments have, since 2010, attempted to cut out what they saw as the more peripheral of these expensive activities, which were precisely those that held the whole system together because they sought to prevent breakdown. We now know the consequence: we have broken down. That is the outcome of austerity.

So the choice that Stpehn Bush presents is not true, because it is incomplete. He did not explain why austerity has delivered us a crisis. And, like so many who write about economics, he treats money, and where to find it, as the issue.

He is wrong in the first instance because he thinks tax funds public spending. It does not.

He is wrong in the second instance because he thinks that the money available to the government is constrained. It is not, but resources are.

As a result, he focuses on funding when that is not the real issue. The issue is the failure of society to meet need. If it did that, there would be no funding issue.

The problem is that we are not doing what is required, have large-scale unemployment as a result, are refusing to mobilise those resources to meet the need that they could be used to address, and then wonder why, firstly, the economy is in the doldrums; secondly, why people feel alienated from a failing government; and thirdly, why nothing works anymore.

The answer is that all of this is by choice. The headline makes that clear: there is continuing denial that austerity is the policy, and that we are living in an economy that is suffering the consequences.

Politicians of most parties say that they want ot live in an economy that is growing, delivers well-being and full employment, and meets needs, but they refuse to take any of the actions required to deliver this outcome.

What are those actions? They are not hard to list:

* Determine what is needed.

* Identify the available, largely underused resources that might be used to meet these needs.

* Match the two to deliver the greatest effect when meeting needs within existing resource constraints.

* Deliver the services in question

* Watch the multiplier effects work to deliver additional taxation, and save costs.

* Explain what the investment process in this activity is, and that it will be continuing.

* Explain that deficits increase private well-being

* And that so-called national debt is just a savings facility for the wealth that this programme will create.

In other words, get the story and the actions right, and the outcomes will work.

In other words, we could have real prosperity as measured by meeting need. But whilst we fixate on finance, that is not possible.

We, and especially our politicians, have to decide: do we want to comply with arbitrary, meaningless economic rules, or create well-being for everyone? Stephen Bush's approach is all about appeasing finance. I want well-being.

Bush wants to constrain the delivery of that well-being by imposing arbitrary financial rules to ensure that happens.

I show that without those self-imposed constraints, we can have what we want.

So, why are we siding against what people want and need? That is the question.