



How a politicised Treasury got the UK economy so heavily into debt

I am surprised how few have asked the question 'How, with all the bodies charged with expenditure and borrowing control, did the UK get into a position where the government is borrowing £200 billion a year?'

Some of this year's public sector deficit is genuinely cyclical, either as a result of the impact on revenues and expenditure of growth that can reasonably be expected to be made up at some point or as a result of temporary measures to try to stimulate the economy. But our calculation is that only about £60 billion of the current £200 billion can be attributed to these factors. The other £140 billion reflects a structural deficit which will have to be corrected by constraining public spending or through tax rises (and our research for Taxpayers Alliance casts some doubt on whether some of the tax rises mooted, particularly those on businesses and on higher rate taxpayers, will actually reduce the deficit).

How did this structural deficit emerge? The simple answer is that the Treasury has been consistently excessively optimistic about two different factors – the trend rate of economic growth and the tax receipts from a given rate of growth.

The overoptimism about growth is something about which cebr has been warning for 8 years. Despite this, the Treasury have treated our advice, which in the end has turned out to be accurate, as 'not invented here'. They have claimed that their assumptions have been audited by the National Audit Office (NAO), which appears to be true in some sense. I have never felt that the NAO had any competence in the field of economics and its failure to prevent the Treasury from making major and costly errors has damaged the reputation of the organisation as a whole – a warning to those who bite off more than they can chew. At the very least the Treasury should now get a competent set of economic consultants to audit its assumptions.

The overoptimism about tax receipts is a more complex issue. My view is that as the UK's tax regime has become relatively onerous by international standards, in an increasingly global world with scope for tax arbitrage, companies and rich individuals have moved highly taxable activity offshore.

Once the Treasury became overoptimistic about tax receipts, the money burnt a hole in the pockets of the politicians who blew it on spending binges.

But why would an allegedly competent Treasury make such major mistakes in the first place?

Here I am afraid is the key to the story – the politicisation of a once great institution. One can argue that the practice started with Mrs Thatcher, but she at least had the excuse that she was trying to introduce a more up-to-date way of thinking. There is no equivalent excuse for Gordon Brown's appointment of his former political hack Ed Balls as Chief Economic Adviser or for promoting his former private secretary Nicholas MacPherson over the heads of more experienced officials to be permanent secretary. These moves made it clear that Brown wanted to stifle debate.

Forecasting is a matter of judgement and when the judgement becomes overly politicised officials are likely to end up telling the politicians what they want to hear. Now we are all paying for this failure. The next Chancellor will have to get rid of the political appointees and set up a mechanism for depoliticising the Treasury.

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