OUR VIEW

The Economy

By some measures, the UK economy is performing relatively well, with modest growth, a record level of private sector job creation, low interest rates, slowly rising living standards and a reducing deficit. However, these apparent positives need to be considered alongside the seemingly perennial problems of low business investment, poor productivity, a record current account deficit and an overpriced housing market. Our economy remains dangerously reliant on excessive levels of public and private debt.

George Osborne talks repeatedly about borrowing falling, yet in the next three years borrowing on our behalf will rise sharply. It's astonishing that, a full eight years after the financial crisis and after a surge in growth in employment, the UK is still expected to borrow £56 billion in the 2016/17 year, just over £1 billion a week.

Government debt now stands at an eye watering £1,591 billion, 50% up since Osborne took office, more than £50,000 per person in full or part time employment.

The government anticipates spending £772 billion in the 2016/17 year with an incredible 63% (£487 billion) being spent on Welfare (31%), Education (13%) and Health (19%).

It appears that the Conservative government considers it politically impossible to make any meaningful savings in these huge departmental budgets (look at the furore that arose when Osborne attempted to reduce Tax Credits and disability benefits), so as a nation we appear doomed to live beyond our means until some external shock brings this financial incontinence to an end.

The government will spend £39 billion on interest payments alone in 2016/17 and that's with interest rates at an historically low level. This figure is 85% of our total annual spending on the Defence budget. When debt and interest rates spiral upwards in years to come, the interest bill will rise, all at the expense of spending on services.

In reality, we will probably end up borrowing even more as growth may well turn out to be lower than forecast (Osborne's calculations are based on 2% growth in each of the next six years). George Osborne has told the Commons that he plans to deliver a surplus of £10.4 billion in 2019/20. It appears likely that this surplus can only be delivered by one off accounting gimmicks. I would not be at all surprised if the tax changes being mooted (Making tax digital – see above) are part of this plan, with Osborne hoping for a one off acceleration in tax payments to enable him to meet his deficit elimination target before the next election.

Political incompetence

With the Labour party now providing little more than a comedy opposition, the government can more or less do what it likes. Pledges are made and then broken and there is no coherent voice raising complaints. This has led to even more political incompetence, with policy in so many vital areas flawed, muddled, ill thought out and counterproductive.

Unfortunately, the government continues to regularly "back the wrong horse". A few examples include the failure to reach a decision over London airport policy, a failure to deviate from a dangerously reckless energy policy (including the failure to commission new nuclear power stations) an unwavering belief in the failed economics of the absurdly expensive HS2 project and a flawed view of Europe.

At the root of government problems lies a reluctance or inability to identify long term objectives and then to develop a plan for the best way to achieve them. All too often, it seems that policies are decided by the outcome of a search for what looks to be electorally attractive in the short term, rather than what is in the best interest of the country in the long term.

I understand that no less than ninety-six "special advisers" are now on the public payroll. Many of these people appear to be bright, ambitious youngsters, marking time between completing their degrees at Oxbridge and moving into politics. This is exactly the route that David Cameron followed. Clearly most of these individuals have hardly any real world experience, so you are left wondering exactly what they "bring to the table".

Given that so many Ministers are quite clearly incompetent, you could advance an argument that they need all the help they can get. However, it seems unlikely that they are asking the right people for advice.

<u>Economists are clueless</u>

I never cease to be amazed by the tremendous weight that policy makers and the media give to economic forecasts and statistics. There is a never ending supply of "data" spewing forth from (seemingly) august bodies both in the public and private sector which politicians use to justify their actions, prove they were correct or prove that their policies are the right ones. At the moment, there seems to be a daily battle between both sides of the referendum debate with claim and counterclaim.

A cursory examination of the facts shows that economists are both spectacularly bad at accurately forecasting the future, as well as being spectacularly bad at being aware of what is going on in the present. It would be wrong to suggest that economic forecasting is easy, but it would be far more sensible if politicians acknowledged that most economic forecasts are educated guesses and much "data" is not wholly accurate and is often subsequently revised.

The worst thing about bad forecasting isn't that the predictions are often woefully inaccurate; it's that the economists in question are so confident in their predictions.

The Queen famously asked academics at The London School of Economics back in 2008 why none of them saw the financial crisis coming. Four years later, she was told by an economist at the Bank of England that the crisis was a "rare event and therefore difficult to predict". How enlightening.

One example of mind boggling ineptitude caught my attention recently. The Office for National Statistics (the nation's official statisticians) has now decided that its measure of average house prices in the UK is wrong and needs changing. They will publish their full findings later this year, but they believe that they have overstated average house prices by possibly as much as £37,000 by giving too much weighting to very high value homes and also, quite incredibly, they have only taken account of homes bought with mortgages. What astonishing incompetence.

Economists are always changing their minds (because they don't know what is happening or what is going to happen) but few practitioners of this "dismal science" do it quite as regularly as central bankers. I have lost count of the number of times Mark Carney (Governor of the Bank of England) has signalled an interest rate rise, only to change his position a few months later in the face of revised forecasts.

"When the facts change, I change my mind. What do you do Sir?" This quote is attributed to John Maynard Keynes, one of the most influential economists of the 20th century. No doubt many economists could defend their changing views in this way. Perhaps however, they should have been a little bit less certain in their forecasts in the first place.

A fair tax system

Adam Smith, the great political economist and philosopher, laid down four fundamental principles with regard to taxation as far back as the 18th century.

It seems to me that all Chancellors of the Exchequer should be made to recite these principles every day and have them at the forefront of their minds when determining taxation policy.

Smith said tax should be:

i) cheap to collect
ii) people and businesses should know how much and when they have to pay
iii) it should be based on ability to pay for reasons of fairness and efficiency and
iv) paying it should be convenient for taxpayer and tax collector.

A glance at the tax regime in Britain would suggest Mr Smith's simple rules have long been forgotten.

Another banking crisis?

The imbalances in the world economy make me believe that another full scale banking crisis could quite easily occur. Collapsing oil and commodity prices are now seeping into the financial system, just as collapsing house prices did in 2008.

Another sovereign debt crisis could soon arise, this time it would not be centred on the peripheral Euro nations but on commodity exporters. Venezuela and Ecuador already look "bust" and it is quite possible that Saudi Arabia and Russia, two major economies, could head that way too. The banks were happy to make loans to oil exporting nations when oil prices hit over $100 a barrel. These loans look far less secure now.

Central bank policies of maintaining near zero interest rates may be politically expedient, but they also make it almost impossible for banks to earn any kind of profit margin on the difference between deposits and lending. Indeed, negative rates across much of Europe mean that banks holding cash on their balance sheets are actually losing money. Over time, this weakening of the banks will be unsustainable.

What we learnt from the 2008 financial collapse was that the financial system is incredibly complex and interdependent, so losses in one market will inevitably "pop up" somewhere else. The collapse in oil and commodity prices will inevitably result in losses in the banking system. No one at this stage can confidently predict how great these losses will be.

The EU and Eurozone

The Euro is the most ambitious project undertaken in monetary history and the long term future of the European Union is now wholly dependent on its survival. The dire performance of so many of the Eurozone economies, with near zero growth, high unemployment and unsustainable levels of debt, clearly shows the Euro is failing the majority of the nineteen different sovereign economies which have the misfortune to use it. The Euro area today is now a drag on world economic growth.

The survival of the Euro can only be achieved by a move towards complete political union amongst Eurozone members ("ever closer union") and the permanent transfer of wealth from the richer countries (in reality, Germany) to the poorer ones. It is very hard to envisage how the centralised unelected European elite will be able to achieve this without an enormous public backlash at their anti-democratic attempts to effectively eliminate sovereign nations.

The Euro has already led to the surge in support for populist extremist parties from both the right and left. The retro Marxist comedians (also known as the Greek government) believe that there really is such a thing as a free lunch, every day forever (as long as the Germans pick up the tab).

Greece is of course "bust". It cannot be bailed out and it can never repay its debts. Further impositions of austerity will not promote its recovery. It is clear that the only way forward for Greece will be through default or the writing off of a substantial proportion of its debt burden and a devaluation of its currency so that exports can prosper. The European elite are unable to accept that they face the terrible choice of writing endless blank cheques to support Greece and the other struggling economies of the Eurozone, or alternatively they will have to halt the monetary union project.

The origins of the EU that we see today can be traced back to the panicky post war reaction to the horrors of two World Wars. I have no doubt that the eleven founding fathers of the EU, including Winston Churchill, genuinely believed that they could eliminate the European ills of nationalism and warmongering once and for all. They had a vision of a peaceful, united and prosperous Europe and the first of these aims has been realised. However, the flawed structure of the EU will lead to lower relative prosperity in the future and more division.

The Referendum

In June, the people of the UK will get to vote on Britain's future relationship with Europe for the first time in forty one years. Back in 1975, Britons voted 67% in favour of continuing our membership of the EEC or the "Common Market".

In perhaps the most famous of all episodes of Fawlty Towers, aired in October of that year, Basil Fawlty welcomed the Germans to his fictional Torquay hotel by telling them:

"I didn't vote for it myself, quite honestly, but now that we're in, I'm determined to make it work"

The EEC that Basil Fawlty and Britain chose to embrace back then bears very little resemblance to the modern EU of today. The UK economy at that time was in poor shape, with strikes, low productivity and rampant inflation and Britain was known as the "sick man of Europe". Many people believed that easier access to the continental markets would assist our flagging businesses and that this was the only way to halt our economic decline.

At the time Britain joined, we were one of just nine member states. Initially at least, Britain was able to have some influence over the rules to try to create a new economic order based around free trade, deregulation, privatisation and the removal of state aid from failing businesses.

Britain's influence has diminished massively over the years, largely because the EU is now made up of twenty eight member states, with another five on the waiting list. In addition, the UK's decision not to adopt the Euro (for which quite bizarrely we must thank Gordon Brown) has further reduced our influence, but has saved us from economic meltdown. If Britain chooses to remain within the EU it will inevitably become an increasingly minor player in this doomed superstate.

Many people I have spoken to have said that they are finding it hard to make an informed choice for the referendum as they feel there are insufficient facts for them to consider. Although I sympathise with this view to some extent, and to date neither side has come up with many positive messages, I do think that the use of basic common sense enables sensible conclusions to be reached.

David Cameron claims that he has negotiated concessions which mean it makes sense for Britain to remain part of the EU project and that we will be more secure and wealthier in the years to come. He claims that leaving would be a dangerous "leap into the unknown". What an odd claim, given that Britain had been an independent, sovereign trading nation for hundreds of years before joining the EEC and that our security is dependent on our membership of NATO.

So the Remain side are keen for us to continue on the path we have been on over the last forty years, with the continued growth of EU power into more and more areas of our lives and the slow inevitable march towards a country called Europe.

They seem happy to ignore the fact that the EU's share of the world economy is rapidly falling and that this cannot be rectified given the structural problems of the Euro. They also do not acknowledge that globalisation and tariff reductions now mean that there is no need to be a member of an enormous political entity in order to reap economic benefits.

We are now less dependent than ever on our trading partners in Europe. Initially over 60% of our exports went to the EU. By 2012 that figure dropped below 50% and it is now at 45% and diminishing. Given that we are net importers from the EU, we will be in a very strong position to negotiate beneficial trading arrangements going forward. The Remain campaigners claim that trade will grind to a halt but this is clearly nonsense – for example we are the second biggest world export market for German car manufacturers and the biggest export market in the world for Champagne.

It would be utterly self-defeating for the EU to enter into any kind of trade war with the UK. There is no reason why we could not negotiate an EFTA type (European Free Trade Area) agreement and then have the freedom to spend the balance of our net EU contributions (£35 million per day) on our own priorities – research, education, infrastructure etc.

The Remain campaigners claim we will be isolated outside the EU, but in reality we will enjoy the freedom once again to make alliances and negotiate deals appropriate to our interests and expertise. Our historic links to so many countries around the world and the fact that English remains the international language of business mean we are ideally placed to benefit in the decades to come.

There is nothing modern or free market about the EU. It is an old fashioned cartel with an unworkable currency and a stagnating economy. In my mind, the economic arguments are clear, as are the more emotional arguments of regaining sovereignty and becoming a self-governing democracy again with control over our own destiny.

History shows that in most referendums the status quo option tends to triumph and the bookmakers believe this will be the case in June. The government will hope that their "Project Fear" campaign will scare enough voters to vote to remain and they will be aided and abetted by the very same establishment stooges (the BBC, the CBI, the Financial Times etc.) who were campaigning so forcefully for us to join the Euro. They were completely wrong then and they are wrong again now.

Whatever happens in the referendum, the forces of globalisation and the EU's intractable problems will mean that the UK will inevitably separate from this failed entity at some stage. I have no doubt that a sensibly negotiated withdrawal now would be in the long term best interests of the UK.