Engaging the Powers

What they're really up to…

MR OSBORNE'S EXPERIMENT

By

William Keegan

Searching Finance

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Mr Osborne's Experiment is a critique of the chancellorship of George Osborne in the first few years of the coalition government which came to power in the UK In 2010. Keegan points out a major point of contention at the outset when he refers to the aftermath of the banking crisis of 2007:

> **The banking crisis introduced a collapse of economic demand which needed to be offset by government action, not reinforced by budgetary cuts. A myth was propagated by Chancellor George Osborne and others that it was government deficits that caused the crisis. In fact it was the banking crisis that caused the rise in public sector deficits which was the counterpart of the collapse in demand. (p.2)**

Keegan continues:

> **Policies of austerity were the last thing the British and other European economies needed. As I hope to show in the following pages. That there was an eventual economic recovery does not justify the fiscal policies pursued from the summer of 2010. If the historical pattern of growth had been allowed to continue, output in the UK would have been up to 20% higher in 2013-14 than proved to be the case. (pp.2/3)**

Well, that doesn't leave much doubt as to which side Mr Keegan is on! The papers from the website *Engaging the Powers* (engagingthepowers.org), of which this is one, steer clear of partisan politics, but Keegan is writing not as a politician but as an economist and in his weekly *Observer* column was just as free with his criticisms of the previous Labour government as he is here of the succeeding coalition administration. Keegan would not pretend to be anything other than partisan but his allegiance is to a school of economics, not to a political party; he is a Keynesian.

As a matter of background, it is probably worth making clear at this stage that here is a very longstanding cleavage of opinion between two theoretical or ideological positions: on the one hand there is the 'school of thought' which follows the economist John Maynard Keynes. It was Keynes's ideas which provided the direction of Roosevelt's 'New Deal' in the US before World War II. The same ideas were adopted by the new Labour government of 1945 as it set out to lay the foundations of a welfare sate in the UK. Keynesian economics, though much battered by circumstances, held sway in the UK until the advent of Margaret Thatcher who had quite different ideas. The ideas that Mrs Thatcher put forward have, in fact, dominated every successive UK government since her time, including, with modifications, the period of the New Labour administration. George Osborne simply carried on the Thatcherite tradition. Keegan as a Keynesian, it will be understood from this brief historical sketch, had reservations about New Labour but was quite unequivocally opposed to the thinking of the Thatcherite tradition.

After this introductory salvo, he goes on to acknowledge, nevertheless, that the economic woes with which we were struggling at time he wrote this text could not be entirely attributed to the policies of the Coalition government. There were long standing tensions to do with the depressed level of earnings for significant groups of the UK population.

Keegan continues his introduction by referring to the 'trade off' during the crisis and its aftermath whereby unemployment was eased by the creation of low paid jobs. Thus, the long-held assumption of policymakers that having a job is a way out of poverty is no longer valid. But low pay is partly caused by globalisation - if labour costs in the UK are comparatively high, corporations will decamp somewhere else where they are lower; low pay is also a result of the emasculation of the trade unions.

Keegan continues:

> **My contention is not that the policy of austerity is responsible for everything that has gone wrong in the progress, or lack of it, of real earnings and living standards in recent years, but that it has played a considerable part in aggravating the problem; moreover, the concentration of austerity measures on the public services has caused hardship and misery for 'the voiceless'. (p.4)**

However, the austerity regime of the coalition government has certainly played its part in the difficult conditions which now pertain.

> **As the veteran economist, Robert Neild , wrote shortly after George Osborne's 'emergency budget' of 2010: Confidence, or lack of it, is at the core of the economic crisis. Mr Osborne justified his harsh and urgent budget tightening in June 2010 by the need to maintain confidence and avoid a threat to to our sovereign debt. But that budget policy, together with the uncertainty of the business outlook abroad, has undermined the confidence of our businessmen and has led us into depression. They need to have confidence in the future demand for their products if they are to invest in new buildings and machinery and so generate more employment. But that confidence has been squeezed out of them for the sake of foreign confidence.**

Keegan now refers again to the criticism, levelled repeatedly at the previous Labour government, that it was the profligacy of that government which led to the massively increased debt problem which the incoming coalition government faced.

> **Although much has been made of 'Labour Mess', government debt as a share of GDP was lower in the UK during 2007 than in every G7 country except Canada. What happened was that in the early period of Brown's chancellorship there was if anything an overemphasis on 'prudence'…As a matter of plain fact, on the eve of the 2007-08 financial crisis, public spending as a share of the economy was, at around 39% of GDP, close to the levels recoded during the latter years of Kenneth Clarke's 1993-7 chancellorship. (pp.4/5)**

Keegan ends his introduction with this comment:

> **What cannot be denied is that the British economy was recovering in mid-2010 and then 'flatlined'. It is my belief that George Osborne's initial pronouncements set the recovery back by several years, with the consequences covered in this book.**

George Osborne's strategy

> **Under the Chancellorship of George Osborne, the most important stated aim of economic policy…was to bring down the budget deficit. It had been with this in mind that the Chancellor, indeed the entire Coalition, has repeatedly aimed to justify its policy of 'austerity'. Even when, after three years of what the Shadow Chancellor Ed Balls referred to as 'flatlining', the economy showed signs of recovery in 2013, the Chancellor went out of his way to promise more 'austerity' with the emphasis on day to day spending on public services…(p.39)**

When George Osborne arrived at the Treasury in the summer of 2010, he chose to be a prisoner of the Treasury and the Bank of England because it suited his political strategy and the experiment he was about to conduct…Osborne's political strategy, which his Lib Dem partners were all too ready to go along with, was to blame the economic crisis with which he was faced entirely on his predecessors: 'Labour's Mess', or, in Prime Minister David Cameron's words, 'Labour's failure to mend the roof when the sun was shining'. It mattered not that both Cameron and Osborne had backed Labour's broad approach to public spending at the time. The argument went that profligate public spending was the cause of the crisis, and the resulting deficit must be removed. This would require several years of austerity…(p.40)

Keegan continues:

The entire strategy was based on the argument that budgetary tightening was necessary in order to put the economic house in order and that this would pave the way for a sustained recovery, not the same thing all over again. Yet for all the regulatory efforts by the Bank of England - which hoped it had learned from its previous mistakes - there was a widespread feeling that the bankers did not 'get it'; that the financial sector was still wedded to the bad old ways and that another financial crisis could not be ruled out. (p.41)

The financial crisis

Keegan now points out:

It can hardly be emphasised enough that it was the banks which caused the crisis, not Labour public spending plans which, as noted, had already been supported by the Opposition in the run up to the crisis…The present government (the Coalition of 2010-15) has seldom lost an opportunity to hammer on about 'Labour's Mess'. yet the record demonstrates that, for all the apparent political success the Chancellor and his colleagues have had in making people believe them, the charge simply does not stand up. Thus, Treasury figures show that the key measure, net public sector debt as a percentage of GDP, was actually higher during the last two years of the Major government than in any year under Gordon Brown's Chancellorship…Gordon Brown did indeed 'mend the roof when the sun was shining. with the net debt to GDP ratio falling to 29.7% (compared with 41.9%a and 42.4% in the last two years of the previous Conservative government. (p.48

But the banking crisis occurred on Labour's 'watch'. Maybe, says Keegan, but the responsibility for it, apart, that is of course, from the bankers' own contribution goes further back in time involving a succession of governments.

Where governments were responsible, or should we say irresponsible, was in the way that, seduced by the vogue for 'light touch' regulation, and by the belief in the wisdom and 'efficiency' of financial markets. They allowed the financial markets to run amok…(p.49)

It was a collective failure…But it was not New Labour that originally championed the deregulation of the 1980s. That was the product of the lethal mixture of the ascendency of the free market philosophers, championed by Mrs Thatcher and Ronald Reagan, and the financial pressure groups that stood to gain from what became a free-for-all, leading to a crisis in which the bankers were bailed out at the taxpayers' expense.

Such was the arrogance and sense of entitlement of the bankers and financial 'traders' involved that, after the rescue, they effectively demanded a return to 'business as usual', awarding themselves huge bonuses even when they were recoding sensational losses.

Hamish Preston
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