

# Opinion

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Mariah Careyensis

Ben Macintyre, page 38



## Cameron may drown in his clear blue water

With the collapse of their poll lead, the Tories have reverted to type and adopted a thoroughly bad economic policy

Anatole  
Kaletsky



A few weeks ago it seemed as if Britain — for all its economic problems and the manifest political inadequacy of Gordon Brown — at least had a competent Opposition that would one day form a credible alternative government.

Now the tables have turned. The good news for the world economy is that Mr Brown has become a leader of global stature, filling the policy vacuum created by the clueless dithering of the Bush Administration and the surprising failure of Barack Obama to step into the breach.

The bad news for Britain is that the Tories have chosen this moment to self-destruct, leaving no plausible alternative to Labour, and nobody, apart from the redoubtable Vince Cable, to challenge Mr Brown's delusions of grandeur — or potential economic misjudgments.

Talleyrand's famous remark about the House of Bourbon — that they had "learnt nothing and forgotten nothing" — seems to apply with equal force to David Cameron's Conservatives after their repeated decapitations since 1992.

Last week George Osborne showed that he had learnt nothing, by foolishly identifying the recent weakness of sterling with the alleged weakness of the British economy and the Government's fiscal policy. In fact, the pound's decline is not a

problem but a solution. It follows naturally from the Bank of England's aggressive rate cuts and the monetary freedom that Britain retained by staying out of the euro. This precious freedom is now reflected in the highly competitive exchange rate and ultra-low interest rates that will help to lay the foundations for recovery, just as they did in 1994-95 and 1983-84.

This week, Mr Cameron showed that he had forgotten nothing by suddenly reverting to the policies of John Major — not just the "strong sterling" totem, but the whole package, complete with empty promises of fiscal restraint, warnings about a "Labour tax bombshell" and contempt for Keynesian economics. These were policies that Mr Cameron used to advocate when he worked for Norman Lamont. The leader of the Tory "modernisers" was supposed to have forgotten all this nonsense when he left the side of the former Chancellor on Black Wednesday, but he has now reverted to type.

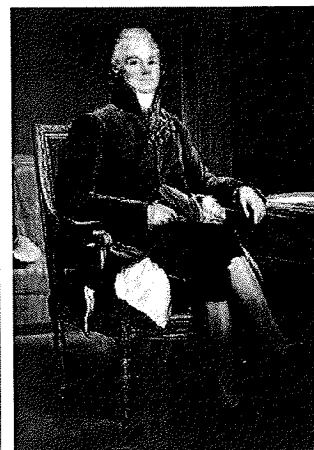
How can we explain this sudden throwback to the economic policies of the 1980s, that may well be remembered as the second-longest suicide note in history, after Labour's 1983 manifesto under Michael Foot?

The political motivations seem fairly straightforward. Mr Cameron's initial approach to the financial crisis was sensible: support emergency efforts to stabilise the economy and the banking system, while calling for important improvements in the detail, such as revision of the bank bailouts terms and abolition of the pernicious "mark to market" accounting that has greatly intensified the boom and the bust of the present financial cycle.

But frustratingly for the Tories, their leaders' voices were drowned out, first by the hubbub of the financial crisis and then by the unexpected chorus of adulation for Mr Brown. With the polls moving in Labour's favour, it seems that patience suddenly snapped on the unrepentant Tory Right and Mr Cameron felt obliged to placate it. By attacking almost every aspect of Mr Brown's economic policy and promising to do the opposite, he has certainly created "clear blue water between the Tories and Labour".

Unfortunately for the Tories, their policies are thoroughly bad economics. "Unfunded" tax cuts and unbalanced budgets sound dangerous, especially when the country has a hangover from a decade of excessive borrowing and spending by homeowners. It seems sensible that, after such a binge, consumers should be encouraged to save. And it is obvious that any tax cuts or new public investments announced by the Chancellor next week must be paid for by future tax increases. But such analogies between household and government budgets are totally misleading, as any textbook of Keynesian economics explains.

The essential message can be summarised in three sentences: if an entire nation decides to cut spending and increase saving at the same time, the result is not an increase in saving but an increase in unemployment. This means that households can only increase their savings or reduce their debts if someone else spends and borrows more to keep the economy afloat — and in a recession that normally has to be government. And finally a government that spends and borrows in a recession can usually



Should the Tories heed Talleyrand's words on the House of Bourbon?

repay much of this borrowing without raising tax rates, because recovery automatically yields higher revenues and reduces spending on the unemployed.

By flatly rejecting this message, the Tories have put themselves at loggerheads with almost every government and central bank in the world, as well as Britain's business lobbies. But surely the same was true of Margaret Thatcher in 1981? After all, 364 economists famously wrote to *The Times* denouncing her public spending cuts and higher taxes — yet the economy started recovering almost immediately after the notoriously deflationary 1981 Budget.

But conditions today are different from 1981 or any part of the Thatcher era. Keynesian economics

was at best ineffective and at worst dangerous from the 1950s until the early 1990s for two reasons: high inflation and the national obsession with stabilising or "defending" the value of the pound, either against the dollar, the mark or, before that, gold.

For the moment, the intensity of the global financial crisis has removed both these constraints. Inflation is no longer a threat because of the collapse in oil, commodity and house prices, soon to be followed by falling wages as unemployment rises. The currency constraint has been removed by Britain's decision to stay outside the euro, while worries about a long-term loss of confidence in sterling are implausible as the US, the EU and Japan face economic problems very similar to Britain's.

The only real constraint on a policy of fiscal expansion, is the possibility that paper money in general may lose its value — not just in Britain, but also in America, Europe and around the world.

At present investors and savers seem to trust nothing except bits of paper signed by governments, be they dollar bills, bonds or banks with government guarantees. At some point the world's savers, investors and bankers will presumably decide that assets of real economic value, such as houses, oil wells or shares in commercial enterprises are better stores of wealth than paper signed by governments. But when this happens the financial crisis will, ipso facto, be over, and inflation not deflation will again be the main threat.

That will be the time to hear from advocates of fiscal prudence — but until then the right policy will be to borrow and spend.