

## **Cameron is right to warn of another recession, but wrong to blame the world**

*When governments cut their deficits when the private sector is still shell-shocked by slump, the situation only gets worse*

By Robert Skidelsky

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Ministers are up to their old game of blaming everyone but themselves for Britain's economic woes. First, they said they were "clearing up the mess" left by Labour. When recovery stalled in 2010, it was because of the Greek crisis. Now David Cameron warns of a new recession even before it has happened—because Europe is not doing its job of recovering properly.

Cameron is right to warn that the world is on the brink of a third recession. But he is wrong to say that this makes it even more necessary for Britain to stick to its "long-term economic plan" of deficit and debt reduction. Because it is these deficit and debt-reduction policies, implemented throughout the European Union, that have been causing the "red lights" of recession to start flashing.

Cameron and George Osborne cannot get it into their heads that if governments start cutting their deficits when the private sector is still shell-shocked by the slump, the policy will not produce growth but deepen the slump and slow down the "natural" forces of recovery. But this is exactly what the coalition government has been doing since it took office in 2010, and what Angela Merkel has forced on members of the eurozone.

The reason is obvious to common sense but escapes the refined logic of treasuries and central banks. The amount of activity in an economy depends on the total of spending. Spending creates incomes: incomes create jobs.

Spending is made up of private sector spending and government spending. If, for one reason or another, the private sector – businesses and

households – reduces its spending, then total spending can only be kept up by the government increasing its own spending. If the government simultaneously reduces its own spending, then the amount of activity in the economy is bound to fall. If we take Britain and the eurozone together this is exactly what has been happening since 2010. Government spending has been cut, and this has dragged down total spending. It is a matter of simple arithmetic.

But, it will be said, Britain did start growing again in 2013, so that proves the government's long-term economic plan was right. Wrong. The resumption of growth had nothing to do with fiscal "austerity". It was mainly caused by quantitative easing (QE) – pumping money into the economy – which a country with its own money-creating central bank can do, but which the European Central Bank currently lacks a mandate for. Hence Britain is recovering, the eurozone is still stagnating. However, QE has produced a lopsided British recovery. The new money has gone mainly to owners of assets, who use it to buy up securities and real estate, reproducing the bubble economy that caused the crash in the first place.

Secondly, the vaunted reduction in headline unemployment – from 8% to 6% – has been largely at the expense of an increase in underemployment. Underemployment – people working less than they want to, at jobs below their capacity – is a much better gauge of economic activity today than headline unemployment. The fact that so much of the "extra" employment created since 2010 has been minimum wage, zero hour and part time

explains the failure of government revenues to recover, and the deficit to shrink, according to plan.

The budget figures are worsening almost by the hour. This year's deficit is expected to come in at £108bn rather than the £100bn forecast in October. This means that £50bn, not £38bn will need to be cut to get the deficit to zero by 2018. And all this assumes a healthy annual growth rate over the period, which Cameron has warned is highly unlikely.

The truth is that the budget problem will not be solved without growth, but fiscal austerity undermines not just growth but also – by forcing more and more workers into low-wage, low-productivity jobs – the growth potential of the economy.

Cameron is right to warn of squalls ahead, but he should look to his own policies before blaming the world.