class

Centre for Labour and Social Studies

austerity illusions and debt delusions

"Austerity has failed. It turned a nascent recovery into stagnation. That imposes huge and unnecessary costs, not just in the short run, but also in the long term: the costs of investments unmade, of businesses not started, of skills atrophied, and of hopes destroyed.

What is being done here in the UK and also in much of the eurozone is worse than a crime, it is a blunder."

Martin Wolf[1]

class
Centre for Labour and Social Studies

Foreword

By Steve Hart

If you tell a lie big enough and keep on repeating it, people will eventually come to believe it – clearly this is something David Cameron agrees with. The lies justifying the Coalition Government's austerity policies are among the biggest. They've caused untold harm and misery to the overwhelming majority of us, while the richest have prospered. Yet still they continue.

Einstein famously said that "insanity is doing the same thing over and over again and expecting a different result". This certainly applies to austerity – an idea which keeps coming round despite being proven to be disastrous again and again.

Austerity was the solution to the massive problems left by the neo-liberal experiment. It was clear that austerity wasn't going to work and Britain's trade unions quickly identified that the Coalition Government's austerity policies would be disastrous. Our campaigns were often lonely as the media regularly spoke of cuts as if they were unavoidable. But today, with worrying economic statistics constantly making the news there is wide recognition that austerity has failed.

However, the figures don't even tell the worst part of the story. Economic statistics translate all too easily into fear, uncertainty, unemployment, poorer living standards and the piece by piece dismantling of our welfare state. One of the strongest symbols of the failure of austerity has been the shocking appearance of food banks in Britain. Last year Trussell Trust food banks fed 346,992 people nationwide. Of those 126,889 were children[2]. Oxfam have reported that the number of those reliant on food handouts on a regular basis is actually over 500,000[3]. Not something you expect to be part of everyday life in the seventh richest country in the world.

This is not the only harsh reality of austerity. Public sector workers have seen their jobs disappear – 300,000 between 2010 and 2012 – with predictions of another 600,000 to go by 2017[4]. Every job a decent income, every job providing a service to the public, every job a person's livelihood.

Nye Bevan said, "the NHS will survive as long as there are people prepared to fight for it" and clearly, it remains the utmost priority to defend jobs and services for the interests of society as a whole.

This struggle to make ends meet isn't a problem for everyone. Since 1980 income and wealth have been massively redistributed towards the super-rich and away from working class and middle class people. In the UK the living standards debate is a constant reminder that austerity and current government policies act in the interest of the richest 1% of society. Millionaires enjoy tax cuts, while millions fall victim to tax increases and service cuts.

Ever-growing numbers of people are receiving low wages. This is directly linked to the weakening of workers' bargaining power through the decline of unions. Between 1979 and 2010, both trade union membership and collective bargaining coverage more than halved[5]. Such decline led to a fall in wages and higher levels of inequality, as well as the dramatic growth of top pay, deeply destabilising the economy.

If Britain is to build a fairer economy, we must move away from austerity, and austerity-lite, and create a new settlement for working people. This is why it is so important that we win the battle of ideas. For three decades, organisations sidelining trade union values and the post-war settlement have dominated the debate. We cannot let this continue. We are cranking up the ideas machine and as the Coalition Government shows no signs of giving up on austerity, the appetite for a progressive alternative has never been stronger.

The billions of austerity cuts still to come may choke off the fragile recovery currently based on a dangerous 'housing bubble'. They must be halted. A programme of investment to produce growth, to reduce the output gap, is the central priority of economic policy. Growth will reduce the deficit, and in the long-run, when appropriate, will reduce debt.

An Investment bank, with a new interventionist industrial strategy, to boost public and private investment; a substantial house-building programme; and policies to reduce inequality and to boost wages – such as increasing the minimum wage, introducing the living wage, and boosting collective bargaining – will not only be good for working people, but will increase spending power and grow the economy. In the long-run, a more equal economy is a more stable economy.

This pamphlet has been produced to expose the Coalition Government's lies and prove that there are alternative routes back to jobs, higher living standards and economic recovery. Austerity hasn't worked and it won't work. Austerity-lite is not much better. There can be no compromise with a failed idea.

Myth: Britain's economy is out of depression

Reality:

George Osborne might be crowing about slight recovery. Yet the reality is that Britain remains in long-running depression - longer than any experienced since Victorian times. 66 months from the start of the recession, the British economy is still 3% smaller than it was in 2008[6].

66
months since the recession started, the British economy is still

3%
smaller than it was in 2008

No other recession in the last century depressed the Gross Domestic Product (GDP—the economic measure of growth) for longer than 48 months[7]. Even the depression of the 1930s, although slightly deeper, was shorter by a year— and we have a long way to go before we get back to that 2008 GDP figure.

Recession: a period when output is falling or receding

Depression: a period when output is depressed below its previous peak

It will have taken
84
months for the economy to come out of depression

2x
as long as it did in the deeper depression of the 1930s

For all the talk of recovery, Britain remains deep in a depression, with the best estimates that it will remain there for another 18 months. At this point the economy will have taken 84 months to come out of depression - nearly twice as long as it took to come out of the deeper depression of the 1930s[8].

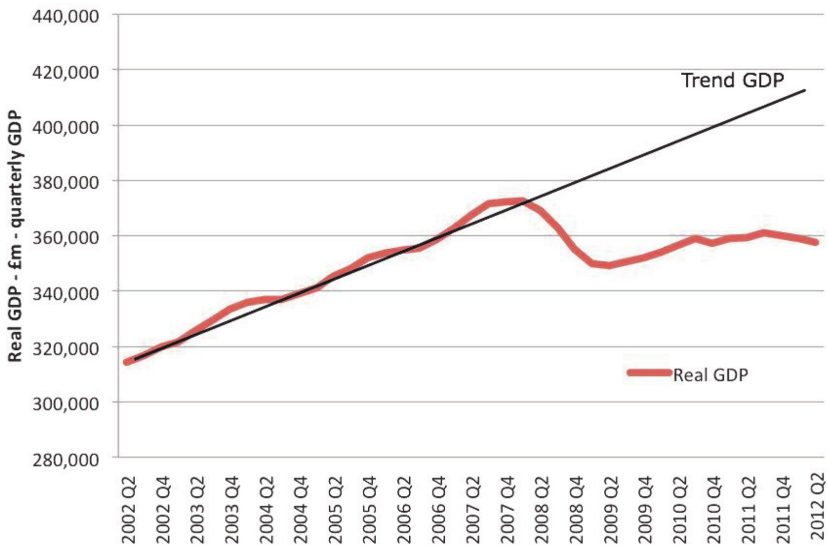
Myth: Austerity saved the economy

Reality:

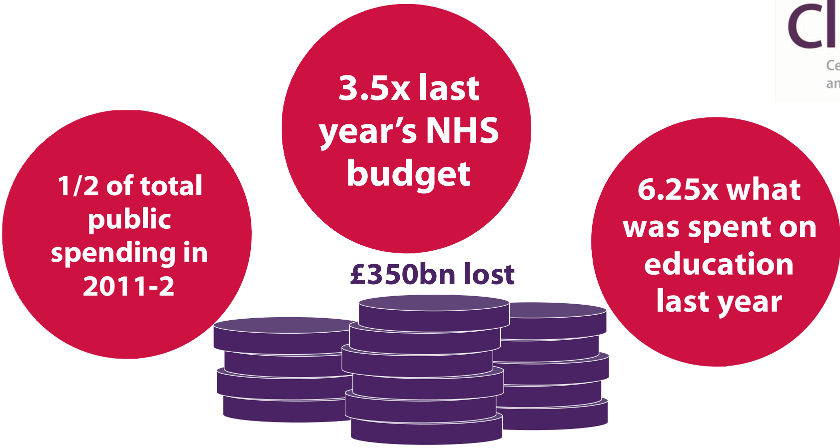
Coalition austerity policies sucked money out of the economy and prevented earlier recovery. Further austerity will only ensure this recovery is stunted. An 84 month depression is bad – it means no growth at all for that period. But economies almost always grow because of improvements in productivity; an expanding labour supply; the effects of investment spending and also the effects of technological innovation.

In Britain, the long-term trend growth rate is about 2.75%[9]. The graph below illustrates this. The straight rising line is the trend growth of Gross Domestic Product which is

Output gap — Trend GDP and Real GDP



Source: www.economicshelp.org ONS-1HYQ



expected. The red line is actual growth. From 2002 to 2008, the economy grew steadily in line with trend growth. Since 2008, first because of the bank crash, then because of the failed austerity policies, the economy got smaller, then bounced along the bottom, instead of following trend growth.

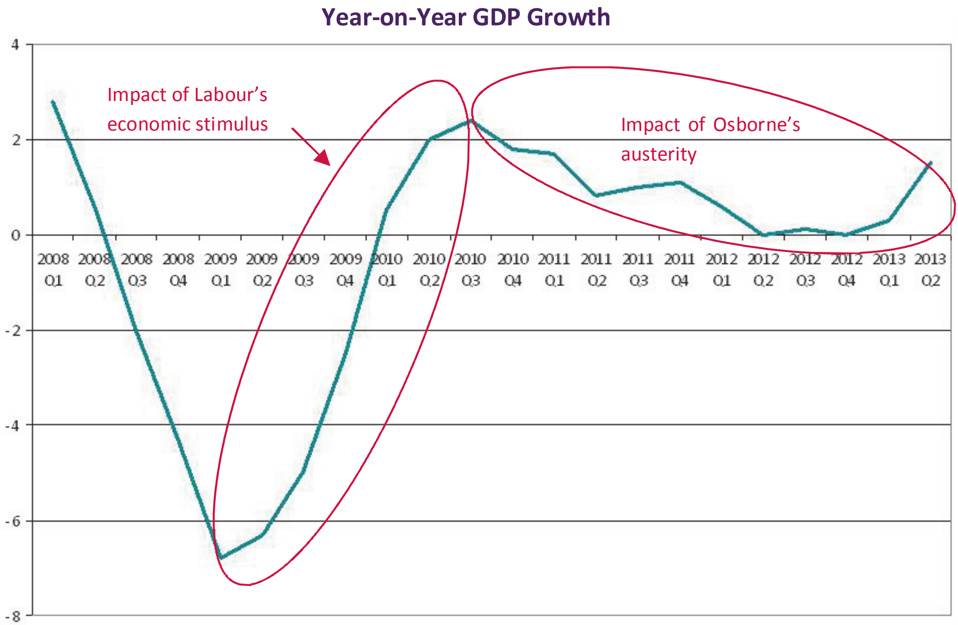
The area between the two lines represents the amount lost to Britain – lost forever. So far, we have lost £350 billion[10] - money stolen from us by the policies of this Government. An amount equal to half of all public spending in 2011-12; 3.5 times what was spent on the NHS last year; and 6.25 times what was spent on education[11].

Myth: Labour wrecked the economy

Reality:

Since 2010 Labour have been branded the Party of reckless spending and many now blame the last government for the depression. The reality is that after the 2008 crash, the Labour government had to ditch the old neo-liberal deregulation approach and bring in policies of economic stimulus alongside effective nationalisation of the banks.

This was probably decisive in starting a global year of stimulus and Keynesian policies which reversed the neo-liberal orthodoxy of the previous 30 years. If further proof is needed of the failure of austerity and the cuts agenda, examination of the economy since 2008 is very convincing.



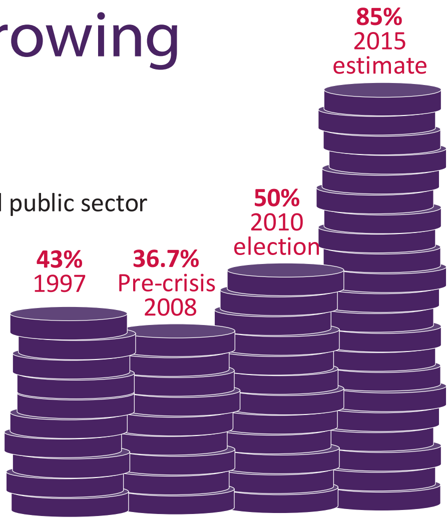
Source: TUC Touchstone blog – Richard Exell see http://touchstoneblog.org.uk/2013/09/dont-do-that-george

Above we see the catastrophic plunge in GDP in 2008 caused by the banking crash. But then we see the instant impact of stimulus. So clear is the cause and effect here, that economists now call it the ‘Brownian recovery’. The line goes up and up, until George Osborne’s June Emergency budget with its massive cuts programme kicks in. Austerity then causes a steady fall in growth until the most recent quarter. **It couldn’t be clearer that stimulus causes recovery, austerity causes recession**.

Myth: Austerity has reduced the UK's debt and borrowing

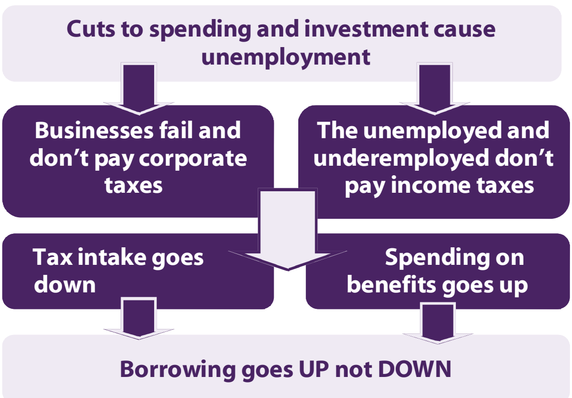
Reality:

Many have argued that debt had to be cut and public sector borrowing reduced. But this is not true. The government started the crisis with nearly the lowest public debt to GDP ratio in its history. The debt ratio fell from 43% in 1997 to 36.7% under pre-crisis Labour[12].



Public Debt to GDP Ratio

Under the impact of the crisis and the banking rescue, it rose to just over 50% at the time of the election[13]. Both of these figures are historically, and internationally low. In fact they are close to the lowest in 300 years! Debt was not - and is not a problem. Despite this the Coalition set out to cut the debt. In this they have also failed - the Office of Budget Responsibility predicts that debt will rise to **85% of GDP by 2015**[14] - austerity policies have in fact increased the public debt.



Not only has the debt not been reduced but public sector borrowing has also gone up. Predictions for public sector borrowing between 2011-16 have risen from an expected £322bn to a massive £539.4bn[15].

Myth: Coalition policies kick-started the recovery

Reality:

Recovery is in spite of Coalition policies not because of them. It takes remarkable economic mismanagement to stop a recovery for so long – the economy is beginning to recover in part because it has been in depression for such a long period of time. Some consumption must return – the new car postponed for so long must be replaced, the house needs to be decorated – and a dip into savings must be made.

The monetary policies of the Bank of England – the massive Quantitative Easing, which happened in spite of the government rather than because of it, were a necessary part of any recovery plan and have prevented the economy from getting even worse. The international situation is also easing – those countries which rejected austerity are in recovery and are buying our exports.

Those countries which rejected austerity are in recovery and are buying our exports

But a big component of recovery has come from the Coalition itself. In spite of all the rhetoric, Osborne has adopted Plan B-lite with a little investment and a little more government expenditure than planned. This combined with stimulating a potentially dangerous 'Housing Bubble' have produced an upturn – time will tell whether it is sustainable. With many of the cuts to public expenditure still in the pipeline - fragile and weak recovery could be choked off very quickly.

> Weak recovery is no substitute for a rounded alternative strategy— one that rejects failed austerity and grows the economy and living standards through investment and expansionary fiscal policies.

Myth: Strict austerity brings faster recovery

Reality:

International Growth since 2008

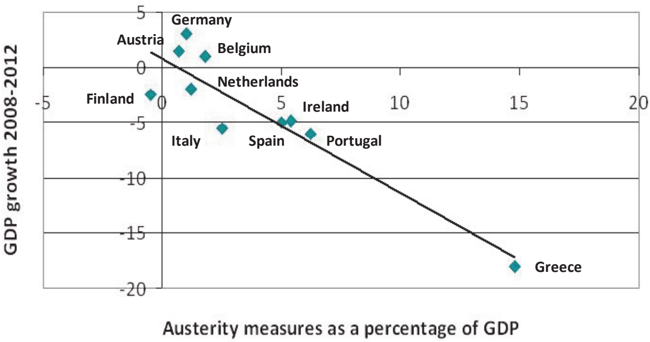
Britain	- 3%
Germany	2%
US	5%
Australia	13 %
China	50 % +

Simple international comparison shows that Britain has done spectacularly badly under austerity. At his first press conference, the new Governor of the Bank of England, Mark Carney took time to downplay the recovery pointing out that the UK economy is still lagging behind other countries, producing 3% less than it did five years ago, while Germany has grown by 2%, the US by 5%, Australia by 13% and China by more than 50%[16].

The US, which pursued economic stimulus instead of austerity to a much greater extent than the UK, is 8% ahead. A further dramatic demonstration of the failure of Coalition austerity. Even the International Monetary Fund, until recently a cheerleader for austerity, has gradually realised the error of many of its ways.

This graph shows the link between austerity and growth in 10 Eurozone countries. The relationship is very clear. Greece, Portugal, Ireland, Spain, and Italy have the highest level of austerity. They also have the lowest level of growth. **Austerity is the enemy of growth**.

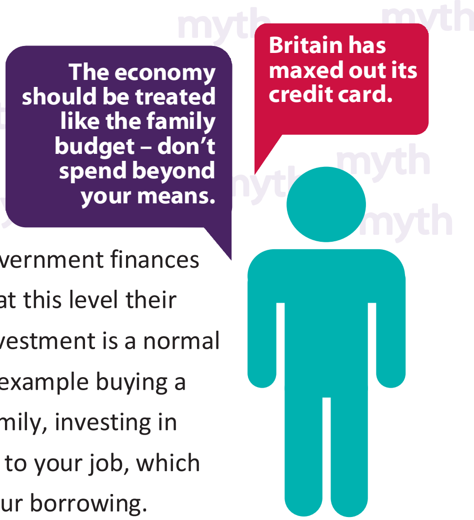
Austerity and Growth



Source: IMF Fiscal Monitor, October 2012

Myth: The national economy can be run like a household

Reality:



The Coalition has repeatedly used the metaphor of sticking to a 'household budget' to justify drastic cuts. But this is not only a misleading comparison, it is also dangerous. Government finances are not at all like household finances, but even at this level their analogy doesn't work because borrowing for investment is a normal and sensible thing to do at the family level. For example buying a house to invest in the future of your growing family, investing in repairing your car to make sure you can still get to your job, which pays your income and enables you to pay off your borrowing.

What seems appropriate at the personal domestic level is quite wrong at national level. Take the 'maxed-out credit card' – while family borrowing is very important as shown above, we all like to live within our means. But if we all cut our personal debt at once, the economy would go into catastrophic depression. This is because what you or I spend, keeps others in work, and what they earn and spend keeps more people in work. If we all cut spending at once, economic disaster arrives like a flash.

> **"We cannot all be austere at once – all that does is shrink the economy for everyone" Mark Blyth[17]**

Falling real wages amounts to cutting wages. If everyone has lower wages, they have less money in their pockets to spend. When less people spend, the economy shrinks. This applies to savings too. If we all save at once, there is no consumption and no spending to stimulate investment so the economy goes into a downward spiral.

Myth: Austerity will stimulate private sector investment

Reality:

Investment has fallen by £68bn from the 2008 peak

The government said that public services had to be cut, to make room for private sector investment. The private sector, they said was 'crowded out' by the public sector. Instead, the reality was that austerity led to an investment strike by the private sector. This was because Coalition policies took money out of peoples pockets and choked off consumer spending.

Investment has fallen by £68bn from the 2008 peak[18]. Far from investment expanding as a result of austerity— it has collapsed.

Myth: We will all benefit from the recovery

Reality:

1 in 5

people earn less than a living wage

Osborne's recovery will not be felt by everyone. Living standards for most are continuing to fall, while one in five earn less than a living wage[19]. Working people are on average almost £1,500 worse off a year since the Coalition took office[20], and yet they prioritise tax cuts for millionaires. This recovery will be felt by the few, not the many.

Sources and References

The following footnotes refer to sources and reports quoted in the text:

1. **Martin Wolf** (2013), *How Austerity has Failed*, The New York Review of Books
2. **Trussell Trust** see http://www.trusselltrust.org/foodbank-projects
3. **Oxfam** see http://www.oxfam.org.uk/uk-poverty-blog/blog/2013/07/foodbank-referrals-from-the-dwp
4. **Institute of Fiscal Studies** (2013) http://www.ifs.org.uk/budgets/gb2013/GB2013_Ch6.pdf
5. **Stewart Lansley** (2011), *The Cost of Inequality*.
6. **NIESR** (2013) see http://niesr.ac.uk/publications/september-2013-gdp-estimates#.UjhoUErwK7w
7. **NIESR** (2013) see http://niesr.ac.uk/publications/september-2013-gdp-estimates#.UjhoUErwK7w
8. **NIESR** (2013) see http://niesr.ac.uk/publications/september-2013-gdp-estimates#.UjhoUErwK7w
9. As quoted by **Mark Carney** in a speech on 28th August 2013.
10. **Mick Burke** (2013) http://socialisteconomicbulletin.blogspot.co.uk/2013_07_01_archive.html
11. See http://www.nhsconfed.org/priorities/political-engagement/Pages/NHS-statistics.aspx and http://www.theguardian.com/news/datablog/interactive/2012/dec/04/public-spending-uk-2011-12-interactive
12. **IPPR** see http://www.ippr.org/publications/55/1821/debts-and-deficits-how-much-is-labour-to-blame
13. **IPPR** see http://www.ippr.org/publications/55/1821/debts-and-deficits-how-much-is-labour-to-blame
14. **OBR Budget Report** (March 2013)
15. **Martin Wolf** (2013), *How Austerity has Failed*, The New York Review of Books
16. **Mark Carney** speech 28th August 2013.
17. **Mark Blyth** (2013), *Austerity: The History of a Dangerous Idea*
18. **Mick Burke** (2013) http://socialisteconomicbulletin.blogspot.co.uk/2013_07_01_archive.html
19. **Resolution Foundation** (2013) http://www.resolutionfoundation.org/blog/2013/jul/05/politics-low-pay-are-changing-time-around-tories-w/
20. **Left Foot Forward** (2013) http://www.leftfootforward.org/2013/09/todays-inflation-figures-most-people-getting-poorer-very-quickly/

Class

The Centre for Labour and Social Studies (Class) is a new thinktank established in 2012 to act as a centre for left debate and discussion. Originating in the labour movement, Class works with a broad coalition of supporters, academics and experts to develop and advance alternative policies for today.

Through high quality, intellectually compelling publications and events Class seeks to shape ideas that can inspire the trade union movement, cement a broad alliance of social forces and influence policy development to ensure the political agenda is on the side of working people.

Who is involved?

Class was set up by Unite the Union, the GMB and the Institute of Employment Rights and has the support of a growing number of trade unions including ASLEF, CWU, GFTU, MU, NUM, NUT, PCS, TSSA and UCATT.

More information

www.classonline.org.uk
@classthinktank

class

Centre for Labour
and Social Studies

128 Theobalds Road, London, WC1X 8TN
Email: info@classonline.org.uk
Phone: 020 7611 2569
Website: www.classonline.org.uk