Twitter Thread by Richard Murphy



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I am bemused by those who demand that we repay the UK government's debt. It makes me wonder, do they know what it is? And how do they think it can be repaid? And do they appreciate the consequences? A thread is coming on.....bear with me, because I think you need to know this.

First, what is the UK government's debt? I've immersed myself in this issue and can confidently say the Office for National Statistics's figures are wrong, most especially because they claim that the UK government is in debt by owing money to itself. That's not possible.

Whatever the Office for National Statistics like to claim, money you owe yourself is not debt, and so quantitative easing cancels about £800 billion of UK national debt right now. There are other mistakes in their numbers, but I'll just stick with this one for the moment.

So, if the ONS claim the national debt is around £2.1 trillion at present, it isn't. Allowing for the UK government owning around £800 billion of its own debt the figure reduces to maybe £1.3 trillion, give or take a bit. But that, I hasten to add, is not the end of the story.

It's important to understand that the ONS includes some things few would think of as debt in their figures. For example, around £200 billion (£0.2 trillion) of National Savings balances are included in the national debt. Whoever knew Premium Bond holders were such a burden?

Come to that, in reality the remaining gilts are, when all is said and done, just savings accounts. They are simply the safest place for long term savers like pension funds, life assurance companies and foreign governments to place their money.

The question that has to be asked then is why when the government spends more than £60bn a year subsidising pension, ISA and other saving (as it does) is it so desperate that this money be saved anywhere but with the government itself? That simply makes no sense.

So all who claim they are desperate to repay the national debt should really be asked, why are you so keen to stop people saving in the safest way they can? Because that's what they are really demanding should happen. And there's no evidence people want to stop saving that way.

And remember, government-backed saving is so popular that right now people will buy government gilts, or bonds, due to be repaid in 40 years time with a negative interest rate, which means they will get back less than they actually save now. And people still buy it.

In that case there is another question for those complaining about debt, which is why are they so obsessed about the debt when the cost of interest on it as at a record low, and still falling, and in absolute terms costs less a year than it did before the 2008 crash?

On gilts and national savings, which together make up most of the 'debt', the questions to debt obsessives is then, why don't they want people to save with the government when that's what they really very badly want to do? Why deny people what the savings market wants?

The other issue to understand about the national debt is what happens to the figure that replaces QE when QE cancels government debt because the government can't owe itself? That replacement figure is what are called central bank reserve account balances, or CBRAs, for short.

Central bank reserve accounts have around £800 billion held on them right now, and that number is growing. That figures not the same as the QE balance, but there is a relationship between the two. And that's for good reason.

When the government buys back its own debt when doing QE it creates new money within the Bank of England to do this. There's nothing mysterious about it doing so. All banks create new money by lending, and the BoE makes a loan to a subsidiary company to create this money.

Then that subsidiary company uses the money it's had created for it to buy back the government's own debt. And to record that fact the payment made has to go through the central bank reserve accounts that the UK's commercial banks maintain with the Bank of England

It's important to note that CBRAs are only available to commercial banks. That's because they are the accounts used to move money between commercial banks and the government. There is nothing mysterious about this. They just are what they are: a collection of bank accounts.

And remember, all that bank accounts do is record debts. All money in the modern world is debt. It's nothing else. And so all that a bank account does is record who has agreed to owe who else money. It's hard to get this essential point, but vital to do so.

So, when the government agrees with someone to buy the gilts, or government bonds, that they own then a payment must follow. And since all payments from the government go into the rest of the economy via the commercial banks then the CBRAs have to go up to record this payment.

Now here's the hard bit. For most people it's mind-blowing. When the commercial banks now pay their customers the money the government owes them the balances in the CBRAs do not change. The balances between the commercial banks and their customers do but the CBRAs are not altered

People want to think that it’s money from the government that’s used to pay the banks’ customers. Of course, in a sense it is. But the CBRA remains untouched by the transaction. And this needs explanation.

That explanation is easy. When the government pays a commercial bank the money due for the gilts that payment does not benefit the bank. It benefits the bank’s customer. So the double entry in the commercial bank is to debit the CBRA and to credit the bank customer’s account.

The bank is in this sense a genuine intermediary. And all they are doing is some accounting. There are no piles of notes that change hands, let alone gold or any other such tangible thing. Money is debt. So all the bank is doing is recording changes in debts owing.

As a result of this transaction the Bank of England now owes the commercial bank more money. And the commercial bank owes its customer as a result. But when the customer then spends that money the CBRA does not change. The Bank of England still owes the commercial bank money

The promise to pay the Bank of England makes to the commercial bank is reflected in that bank's CBRA. The promise to pay that the commercial bank makes to its customer is reflected in that customer's account. There are two promises to pay and two accounts. They're not related.

Understand those last few tweets and you understand modern banking, and very few people do. Sadly, almost none of our politicians seem to do so.

But what does this mean for the national debt? If we now have, as a result of QE, the government owning its own bonds and the Bank of England owing commercial banks a roughly similar amount instead, is the government still in debt for the value of the debts QE has cancelled?

The answer, at one level, has to be that yes, it is. If all money is debt and the Bank of England, which is owned by the government, is in debt to the commercial banks then surely it follows that the government is in debt? Superficially that seems to be true.

But then think about this a bit more. What is that sum now owing on the Central Bank Reserve Accounts that in reality now makes up about £800 billion of the supposed national debt? It is simply money. And what is more, it’s money made by the Bank of England.

So, that money is something very like Bank notes in some ways. After all, they are what we also call money. And they are also created by the Bank of England. And, just for the record, as my forthcoming research has shown, they are not included in the national debt.

There is a good reason to not include this government created money - what is called ‘base money’ - in the national debt. That’s because base money, which is banknotes and central bank reserve account balances, is what the Bank of England call ‘the ultimate means of settlement’

In other words, base money is the means of payment when all else fails, which is why commercial banks now need so much of it to make sure that they can function and always pay each other and why cash is also the ultimate backstop for payment in the economy when or if trust fails

And if something is the 'ultimate means of settlement' then how can it be repaid, except by using itself? After all, this is money. That is the only available description of it that there is. That's what the Bank of England says it creates when doing QE.

So, what those demanding that the UK national debt be repaid are really saying is that this Bank of England money that keeps our economy functioning must be repaid. But what does that mean? Indeed, what is repayment of any of the supposed national debt going to mean?

First of all, let’s make clear that the government bonds that have been repurchased by the government using QE can’t be repaid. There is simple reason for that. They have, in effect, already been repaid. They have been cancelled in all but name. They need not be discussed again.

Then let’s consider National Savings savings accounts, like Premium Bonds, which form part of the national debt. Can I presume that no one is suggesting that these accounts must actually be closed? If so, let’s live with this £200bn of savings some call debt.

Now let’s consider the remaining gilts, or bonds in issue. Many of these are used, just like National Savings accounts, to provide a safe place for money to be saved. Can I presume that no one wants to take away safe savings accounts? Why would you? So let’s keep that part.

Another pile of gilts are owned by banks and others as a result of regulation that requires that they have access to ultra-safe money. The object is to present another bank crash. Can I presume no one wants another bank crash? So let’s keep those gilts in issue.

A significant chunk of gilts - around £400bn or so - are owned by foreign governments. That’s because they want to own sterling, and this is how they do it. They see gilts as being as good as money. There is good reason for that. Gilts really are the next best thing to money.

My guess is that we don’t want to force foreign governments to sell their UK government bond holdings because that might create a currency crisis which won’t help the UK. I doubt anyone wants one of them. So let’s leave those gilts well alone too in that case.

Who else owns gilts? Banks do. They use them to underpin what is called the repo market. This is not the place to explain that market in detail. But in essence it is used to guarantee the safety of money deposited in UK banks by very large companies, usually overnight.

Most UK savers who have what they think to be ‘money in the bank’ enjoy a government guarantee to make sure it is repaid. In that case I guess they won’t want to deny large companies the chance to also have a guarantee on their savings. So these gilts are also needed.

So what's left to the gilt markets that might be repaid after we take all these factors into account? Not a lot to be candid. So why the obsession about repaying these gilts? It is really hard to fathom.

In fact, the only thing to say about the desire to force gilt repayment is that it is wholly destructive. It would undermine the pensions, savings, life assurance, foreign exchange and banking sectors. There are left wingers who might want this. But why anyone else? I'm baffled.

I am also baffled by the desire to force gilt repayment when there seems some desire on the part of the financial markets to own more of them. I have no clue why so many who describe themselves as market fundamentalists are so anxious to deny markets what they want.

There appears to be a self-destruct instinct in those commentators who want the national debt repaid because their beloved City could barely function without it. Do they not realise? Do they not know? Are they lying? Or do they just hate the state so much that they don't care?

Whatever the reason that people want gilts repaid is, let's move on to the £800bn on central bank reserve accounts that they also want cleared. How could that be repaid? And what will the consequences of an attempt to make this repayment be?

Remember, that this debt is just balances on bank accounts. But these are a peculiar type of bank account. They are, like all bank account balances, debt. But unlike all others, the balances on central bank reserve accounts are deliberately created to function as money.

That's because whilst these balances are technically repayable to any bank on demand, repayment on demand by the Bank of England to one bank means that the sum due to it by another bank increases. That's because electronic money has to be redeposited. That's double entry at work.

To reiterate: this redepositing has to happen. Unlike cash, central bank reserve account balances can't be lost down the back of sofas. So if a bank draws on its own central bank reserve account it inevitably does so to make payment to another bank's central bank reserve account.

That's because this is the way post-2008 that banks deal with each other. They don't trust each other not to fail. So they always demand immediate payment. And if there's a shortage of liquidity to make these payments - as in March 2020 - QE creates more of it, instantly.

So, and to be blunt, it is these balances that are keeping the banking system functioning right now. And as was proved early in 2020, we really do need hundreds of billions of pounds in such accounts, effectively created by the Bank of England via QE, to let banking function.

So why would anyone who does not want a banking crisis want these balances repaid when they play such an enormous role in the functioning of the UK economy, and the City of London? I am utterly baffled to know why. They either want a financial crisis, or don't understand banking.

But let’s despite the absurdity of that wish assume that they got their way and it was decided to reduce these balances. This thought experiment is really important. Stick with me, please.

The central bank reserve accounts are debt that can only be cleared by repaying the debt. The commercial banks can’t do that. The debt is base money, and not the commercial money that they create. They can’t get rid of base money by themselves. Only the government can.

How can the government get rid of base money, which is what the balances on central bank reserve accounts represent? There is only one way, but three mechanisms. The way is to take money out of the economy. The mechanisms are tax increases, bond sales and austerity.

The first two mechanisms mean people pay more money to the government. That additional money payment would have to go to the government through the central bank reserve accounts - that’s the only available transmission mechanism. And so the balances on them would reduce.

The third mechanism - austerity - means cutting government spending. If done whilst keeping tax and bond sales (or flows to government savings accounts) constant this reduces the flow of government money into the economy and so reduces the central bank reserve account balances

Let’s ignore that this would mean banks having fewer funds available to them, and all that means. Let’s instead consider what a tax increase means. What a tax increase does is take money out of the economy - the reduction in the central bank reserve account balances shows that.

That clears the debt on the central bank reserve accounts, so those demanding this happen get their way. But there’s now less money in the real economy we all live in. And that reduction means there is reduced spending power in that economy. And that means demand falls.

Falling demand always has the same outcomes. It means a decline in growth. That in turn means lower sales in businesses. And lower profits. And that then means reduced employment, which in turn means less tax is paid. Which means money does not flow to government the way it did.

A government wanting to reduce the balances on the central bank reserve accounts faces a dilemma in that case. Tax increase are not neutral. Tax increases can reduce economic activity. And that can reduce revenues. But, it has to be stressed, that depends on the tax increased.

So, for example, taxes on wealth do not reduce demand as much as taxes on the incomes or spending of the lowest paid. That’s because the wealthy pay taxes out of savings. Low earners have to cut their spend or take on precarious borrowing to pay. Not all taxes are equal then.

But, whatever happens, increasing taxes usually suppresses economic activity. Sometimes that’s desirable. However, few see that as being at all likely over the next few years. So why increase taxes then, when the outcome will be bad for the whole economy? I can’t answer that.

So what about extra bond sales then? This means selling the bonds the government reacquired when doing QE back into the financial markets. Think of it as QE in reverse. It's discussed often. And it works, in one way. It would reduce the central bank reserve accounts.

There is one problem with reversing QE though. It could be called 'the glaringly obvious'. This is that increasing bonds in issue to clear the central bank reserve accounts does not clear the national debt. It just shifts debt from being due as money, to being due as a bond.

Understanding that QE just simply shifts debt around is no bad thing, because it's true. But given that money (which is what the central bank reserve accounts are) is not the same thing as savings (which is what gilts or bonds are) that does not mean that QE does nothing.

QE had a purpose. It was to reduce interest rates, which has been good news for households in debt. And it reduced the cost of business borrowing too, which means many businesses that might have gone bust of late will not be doing so. That's pretty good news too.

QE had other benefits. As already noted, QE basically created the central bank reserve accounts that have provided the liquidity that banks have needed to keep paying each other without risk of a bank collapse. Staving off a banking crisis is some achievement. QE did that.

Not that I'm saying there are no downsides to QE. There are. Because the funds injected into the banking system were effectively unregulated much simply went into speculation. Stock markets have skyrocketed. The City has won more than anyone else from QE. No one sought that.

There has also been a real downside to this upside for the City from QE. QE has undoubtedly created greater inequality in the UK, and elsewhere come to that. Much of that has been disguised. Governments have been able to claim their economies have recovered. But at a real cost.

This cost of QE has been suffered by those who have been let behind by QE. Reversing QE will not change that, any more than it will reduce the national debt. The redistribution upward has happened. It can't be undone now by shuffling the new wealth distribution around a bit.

So, new bond sales created by reversing QE will not address the problems within the economy, and nor will it reduce the national debt. And tax increases will be really harmful. So we're back to austerity as the only option. And that policy that has failed for the last decade.

Austerity seeks to reduce the flows from government to the rest of the economy through the central bank reserve accounts whilst hoping that tax revenues and the inward flow of funds to the government do not stall. It always was a naive assumption. It still is.

The government is the biggest spender in the UK economy. It's also the biggest employer. And the biggest supplier of savings accounts. The assumption that somehow it can change its behaviour in one way - cutting spend, for example - and leave everything else as it was, is absurd.

Austerity cuts the flow of government created money into the economy. The impact is much the same as a tax cut. Demand in the economy is reduced. So employment falls, and so does tax revenue. But austerity is like a very targeted tax cut. And it hits the least well off hardest.

That the least well off should be hit hardest by austerity should be obvious. The biggest parts of government spend are on the sick, the elderly, those with disabilities, those on low incomes and the young. Of course they're the least well off. Austerity inevitably harms them all

Austerity can reduce balances on the central bank reserve accounts. That is indisputable. But the fall in the central bank reserve accounts is not as big as the cuts made because of falling tax revenues and savings inflows to government. And is the cost a price worth paying? No.

So let me summarise this long thread. It's claimed that we need to reduce the national debt. But first of all we need to state it correctly in numerical terms. And then we need to understand what makes it up.

Roughly half the national debt is made up of gilts or government bonds when those gilts that the government already owns are taken out of account. And these bonds are just savings accounts, in effect.

But these savings have a massively important role in the economy because the holders of these accounts know that the government can never fail to repay these accounts. That's because the government can always create the money to repay. That repayment is guaranteed then.

And in the world post-2008 the ability to repay is fundamental. The trust that existed before then has gone. We know banks crash now. Those demanding gilts be repaid ignore this. They are living in a fantasy past.

In the real present gilts underpin the smooth operation of banking, pensions, many savings products and foreign exchange markets. Since each of these is pretty darned important to the UK suggesting that bonds be repaid is akin to economic madness.

And it's also mad to say that cancelling National Savings is a good idea, and yet around £200 billion of national debt is in this form.

But the craziest demand of all is that we get rid of the money that now underpins the smooth operation of our entire economy, whether by tax increases or austerity, given that bond sales don't work for this purpose. But then, nor do tax increases or austerity either.

So, what do we do? If repaying the national debt is undesirable, what next? There are four simple things to say here.

First, celebrate the fact that something that is a legacy from the gold standard era of money - which the national debt is - has morphed into something so multi-facetedly useful in the modern money era. Thank goodness that we have it.

Second, stop thinking this 'debt' needs to be repaid. The whole reason it exists is that people absolutely trust that the government can always repay it but quite emphatically do not want them to do so. Its virtue is that it continues to offer safe

savings opportunities.

Third, stop all talk of ‘our grandchildren having to repay this debt’. That’s utter nonsense. They too will need it to make the economy work. And the lucky ones will own some of it, because the national debt is private wealth. The real issue is, how can some more have some of it?

And last, stop worrying about the size of the national debt and instead ask whether we are using it wisely. The question is not whether the national debt is a problem, because of itself it is not. The question is whether or not the policies that change it are the best available.

If austerity is not wise - and it is not - and many tax increases might be destructive right now - what spending and tax policies do we really need to deliver national prosperity? That is the real big issue for current debate.

So now let’s come to my last point. Debate on debt repayment exists for a reason. It’s not that deep down anyone really wants to repay the so-called national debt. But those promoting debt repayment do so to stop us thinking about what the state can really do for us.

The state could promote full employment if there was no debt obsession. It could also reduce inequality. It could consider a basic income. It could deliver a Green New Deal. All of these, and more, are possible. The state could care, in a word.

But those promoting debt repayment try to stop these things that would benefit most people in the country happening by promoting a false, and deeply harmful obsession with the so called national debt. I hate to say it, but that’s because they don’t want the state to care.

The national debt is really no such thing. It’s actually savings and money. The real job is to spend those sums wisely. Let’s move on and talk about that, and so show that we do care.

But that’s for another day. The end.