A Proposition for Building Economic Recovery

Stephen Parsons
November 2011

Introduction

In what follows I give a summary of the country's economic position and I suggest that it provides an opportunity for government to make a positive contribution to economic recovery without jeopardising the public finances.

Britain's Current Economic Position

Gross Domestic Product (GDP) is the most commonly quoted statistic to represent a country's economic performance: a monetary estimate of the value derived from enjoying the fruits of our collective endeavour.

UK GDP in 2010 was £1,458,452million. In 2007 it was £1,405,796million. And taking into account the influence of inflation (general price increases) this means that the level of economic activity has not yet really returned to its state before the financial crisis. And because inflation has not been compensated by wage rises, and in conjunction with negligible savings-account interest rates, consumers' effective purchasing power has been reduced.

And yet, as far as I can see, the UK is a fundamentally sound economic structure; a reasonable financial prospect. Some figures required for an appreciation of the position are deployed in Table One.

Table One: Some Statistics for Economic Appraisal

	% of World Pop'n	% of World Trade	% of World Forex Deals	National Debt / GDP (%)	Tax / GDP (%)	National Debt / Gov't Income (ratio)	Budget Deficit / GDP (%)	Budget Deficit / Gov't Income (%)
UK	0.9	3.9	37.0	67.7	36.6	1.85	-10.2	-27.9
US	4.3	9.2	18.0	68.3	28.3	2.41	-10.3	-36.4
Japan	2.0	6.3	6.0	117.2	27.9	4.20	-9.2	-33.0
"Europe"	4.1	28.5		65.9	39.8	1.66	-6.0	-15.1
Germany	1.3	10.2	2.0	57.6	36.2	1.59	-3.3	-9.1
France	0.9	5.0	3.0	76.5	43.6	1.75	-7.1	-16.3
Italy	0.9	3.9	1.0	99.4	43.3	2.30	-4.5	-10.4
Netherlands	0.3	4.0	0.0		38.0			
Belgium	0.2	3.4	1.0		44.4			
Brazil	2.6	1.1	0.0		33.1			
Russia	2.3	2.1	1.0		36.9			
India	16.0	0.8	1.0		15.8			
China	19.3	6.7	0.0		16.1			

Sources: BIS; IMF; OECD; author's calculations

The International Context

Although only just about one percent of the world's population lives in Britain, our share in the world's trade is four times as large. And that's just on the basis of what's called merchandise trade (goods and services); trade or international exchange of financial instruments also takes place in London to a disproportionate extent (37% of foreign exchange market turnover). Thus Britain is demonstrably embedded in the economic culture of international exchange based on specialisation and relative competitiveness.

The Place of Government

It is of the nature of national state governments that they assume responsibility for management of the public realm and the associated financial obligations this entails. The national debt and the budget deficit are the twin measures by which the government's financial status is usually assessed.

It is conventional to express national debt in proportion to GDP for comparative purposes. And on this basis the UK (67.7%) seems similarly placed to the US (68.3%) and to Europe-as-a-whole (65.9%); and compared with Italy (99.4%) or Japan (117.2%) the UK has significantly lower debts.

However, the national income measured by GDP includes both the public and the private sector, whereas the national debt is only attributed to the public sector; so it would seem more reasonable to assess public sector debt in relation to the income of the public sector. When this is done the comparison alters: UK national debt is 1.85 times the size of government revenue; this is more than for Europe-as-a-whole (1.66) but considerably less than for the US (2.40; higher than Italy's 2.30) and nowhere near Japanese levels (4.20).

No one who's got (or 's ever had) a mortgage is likely to consider a loan of less than twice their annual income as wantonly imprudent; especially as we enjoy the benefits of living in the house all the time we're paying off the loan (just as we enjoy living in the country's infrastructure whilst paying down the national debt).

The same argument applies when assessing the scale of the budget deficit. In relation to GDP the UK's budget deficit (-10.2%) is greater than the general level across Europe (-6.0%) but is roughly equivalent to that of the US (-10.3%) and Japan (-9.2%). When reconsidered in relation to the size of government income the UK deficit (-27.9%) is positioned between European levels (-15.1%) and levels in the US (-36.4%) or Japan (-33.0%). The Chancellor of the Exchequer's present shortfall certainly puts Mr Micawber's misery-inducing income-related deficit (-2.5%) in the shade!

Taken together, these measures of the national debt and the budget deficit make it possible to conclude, on the basis of international relativities, that the level of British national debt does not look threatening but that the priority currently being given to control of the budget deficit is justifiable.

Policy Development

Although the level of public sector debt is not threatening, any further increase would obviously add to recurrent debt service charges and thus increase the budget deficit. This argument may be used to counsel against any government intervention that involves public spending.

However, it really ought to be straightforward to offset a temporary addition to public sector debt that is used to finance housing construction by the sale of the completed properties (whether for private residential ownership or commercial rental). This policy could combat the current condition of economic stagnation without adding to any underlying recurrent budget deficit. And it would increase national residential capital (in contrast with the sale of existing social/council houses). The shortage of housing (sometimes qualified as either appropriate or affordable) is widely proclaimed or generally accepted as a problem in Britain. This should be an opportunity to do something about it.

Conclusion

Britain's economic stagnation justifies government intervention. The size of the national debt is unthreatening. A house-building programme funded by sales would not add to national debt or the size of any recurrent budget deficit. Instead it would constructively address two recognised national problems (economic inactivity and housing shortage). It is a plausible policy proposition.