In the run-up to the General Election, we keep being told that Labour over-spending created the economic mess of 2008.

This is simply untrue. The banks, not Government spending, made the economy crash. The crash happened all over the Western world, and was a direct consequence of banking recklessness and incompetence on a global scale. Governments had made this possible by radically weakening banking rules.

Yet the Tory-Lib Dem Coalition and most of the media continue with the absurd claim about overspending, and support it with more myths. They use these to justify their policy of austerity.

In this booklet, we identify these myths, show why they are untrue, why austerity has - far from "sorting out the mess" - made recovery slower and more painful, and what can and should be done instead.

A briefing note for Radical Independence Edinburgh
April 2015
The story they tell us about austerity

By May 2015, we will have been subjected to 7 years of increasing cuts to public services and social security, inflicting misery and poverty on millions of people. This is what is called *austerity*, and we are told that, painful as it is, it's unavoidable.

What the Coalition Government, in power since May 2010, tell us is that the public finances are badly in the red, because the previous Labour Government overspent.

They also tell us that, as a result, the national debt is dangerously large and we're going to get hammered with repayments and interest if we don't get it down.

The first priority, they say, is to make sure Government spending is within its income. Get the deficit down. The only way to do that is to cut spending, and they've got to be really tough cuts.

Sounds familiar? Maybe even sounds like good common sense?

The trouble is, none of it is true. Public finances *are* in the red, but not for the reasons we're told - and the rest of it is pure myth. *All of it. Respected economists, conservative-leaning think-tanks, Financial Times columnists - virtually all agree that the rest of those statements are plain wrong*. Nobel Prize-winning economist Paul Krugman calls it a "bogus narrative".

We call it a Big Lie.

The public *deficit* and the *national debt*: what are they and what's the difference? Newspapers often confuse the two.

The public *deficit* is the gap between the Government's income in a year and what it spends that year.

It covers the difference by borrowing money. It already owes money from the previous year, and the year before that, and so on: the total of all this money owed is called the *national debt*. 
**Why it's not true: five myths**

**Myth no. 1: "It was Labour overspending"**
Labour did spend more than it got in taxes - but all Governments do this, in most years. The difference (the deficit) from 2002 to 2008 was similar to or less than in previous Tory years: there was actually a **surplus** for 3 years up to 2002.

![Deficit as % of GDP](image)
The deficit went up as high as 7.2% of GDP in the Tory years; in 2007-8, before the crash, it was 2.7%. (GDP is a measure of the total size of the economy - it's usual to compare the public deficit and debt with this.)

**Myth no.2: "The national debt is dangerously high"**
By 2008, before the big economic crash, the national debt was at 36% of GDP. In 1998 the figure was 40%, in 1988 35%. Here's a graph of the debt since 1900:

![Government net debt as % of GDP, 1900-2015](image)
So the debt was not dangerously high, it was at a normal level.
Myth no. 3: "We're going to get hammered with interest payments"
Interest rates are at their lowest ever. Even lower than inflation, so effectively it costs the Government nothing to borrow.

Myth no. 4: "Cutting spending is the only way to fix things"
This is the most damaging myth of all because it's not only untrue, it's being actively used to justify destroying public services. We'll explain why in the next part of this leaflet.

So is the Government in the red or not?
Yes it is - it's still true that the public finances are in difficulty. But the reason is not that spending was specially high compared with tax income before 2008.

The reason is that tax income dropped suddenly and drastically, at the end of 2008.
Why? Because the economy nosedived. Just like that. Businesses went broke, thousands of people lost their jobs. The tax take nosedived with it.

Where the blame belongs: casino banks
Why this sudden disaster? Successive Tory and Labour Governments since the 1980s had loosened the rules for banks. This deregulation freed their managements to take risks with other people’s money in ways which would not have been possible before. So all the big banks used billions of pounds to play the financial markets, and they lost their bets. They went broke - or would have done if the Government hadn't bailed them out. We'll explain later why this hit the rest of the economy so badly.

But the lesson is that the first priority is to get the economy back on track. Get people working, businesses prospering, the tax take back to where it was. We can deal with the deficit later.

There's another big myth: that the Coalition's "tough" policies have been "fixing the problem". Nothing could be further from the truth - but we'll deal with this in Myth no. 5 shortly. First, we'll discuss why cuts are such a bad idea economically.
Why cutting spending doesn't work

For you and me, if our income goes down we have to cut our spending. It makes sense.

But the Government isn't like you and me. It is the biggest employer in the country, by far. When it cuts spending, it cuts jobs.

It's the biggest customer for business in the country, by far. When it cuts spending, it ruins businesses, and more jobs go.

When it cuts benefits, people spend less in the shops. Shops suffer, suppliers suffer, and more jobs are lost.

When jobs are lost, when businesses go under, everyone pays less in income tax, less in VAT, less in business taxes. That means the Government's own income goes down further. It's a vicious spiral.

So austerity is self-defeating.

To get public finances into good shape, the Government needs to increase its income. Not by increasing taxes, but by getting the economy going. More jobs, prospering businesses, mean healthy tax income.

The best way for it to get the economy going is to keep its own spending UP. To provide good quality public services. To pay benefits at a decent level. To invest in housing, hospitals, schools, training, transport. Then money will flow through to shops and businesses, there'll be more jobs, and more income tax, VAT and so on comes back through. A virtuous spiral.

Yes, this means the Government will run a deficit for a while. But that's not a problem. Currently the Government can borrow at interest rates less than inflation. That means it costs virtually nothing to borrow, and has done so since 2008 and before.
**Myth no. 5: "It's been tough, but worth it: we're fixing the problem"**

The overwhelming effect of Coalition policies since 2010 has been to **slow down** economic recovery. They didn't fix the problem, they made it worse by cutting spending when they should have maintained or increased it.

The official figures show this without any shadow of a doubt. The Coalition failed comprehensively to meet its own targets about reducing borrowing. Not because they failed to cut, but because the economy stagnated.

In fact, for a very short time, in 2009, the economy did show signs of recovery - because Labour (still in power at that point) initially did keep spending up. But by 2010 they had changed tack, and in May of that year the Tory-LibDem Coalition took over and intensified the cuts Labour had started to make.

That quickly stifled recovery, scared business and put things into reverse. Business failed to recover. Government blamed banks for not lending. Banks argued that business did not want to borrow. Both were right. Both banks and business were scared by government policies.

Yes, by 2015 the economy is, at last, growing again. It would have recovered anyway - economies do come back from recession. Usually much more quickly.

Yes, there are more jobs. But many of those are low pay and insecure. Wages and salaries today are still 10% lower, in real terms, than in 2008. Investment is low, and productivity has failed to improve at all for 7 whole years. This is not getting back to economic health: it's a superficial patching-up.

As for "fixing the problem" of the banks: there's been a bit of tinkering with regulations, and they have put more capital aside to meet problems with loans, but nothing fundamental has changed. The same kind of crash could easily happen again. All the more so, because personal debt is climbing again: credit card bills and mortgages are shooting up while earnings are only just limping back to where they were 7 years ago.
So why do the big Westminster parties support austerity?

To understand that, we have to go back a way, and see why the economic crash happened. Both Tory and Labour parties are implicated in it.

A really big part of the story is about wages and salaries. Since about 1980, wages and salaries (earnings) have been held down. The economy has grown by 83% since then. Earnings have grown by 46%. The difference has gone into corporate profits. Some was invested back into businesses, improving productivity. That's a good thing. But much more went into banks.

Banks, when they make a loan, effectively "create" money. Until the 1980s, their ability to do this was quite strictly limited by Government regulation, but then these regulations were largely removed. So not only was there an increasing flow of money from business seeking investments, but banks themselves were creating ever more money chasing after profitable investment. Bank lending became riskier, often to borrowers who had little or no hope of repaying. Banks and others moved hugely into trading in loans and other forms of risk, bundled in complex packages, yielding enormous profits.

Blinded in their pursuit of profit, few understood what they were doing. When some of these loans started going bad, the bubble burst. Suddenly, the banks went broke - or would have done if Governments in major countries, including the UK Government, had not bailed them out using our money.

But the damage was already done. For a few weeks in Autumn 2008, the banking system virtually seized up. Ordinary businesses who relied on credit to do day-to-day business found they couldn't pay wages, or order supplies. The whole economy suddenly shrank, by 7%. That's why Government income went down. That's why it's had such a large annual deficit.

There's another huge irony in this story. Businesses that make things and provide services rely on us, the public, to buy them. With our
earnings. But we didn't have enough in our pay packets to buy their increased production.

How to solve this problem? Easy - encourage us to borrow the money. More and more of it, often at high rates of interest. In effect, instead of employers paying us enough to buy the goods we produce, we have been lent the money. It should have been no surprise that there were problems repaying it. But that logic was lost in the tangled forest of bundled loans and financial instruments. By 2007, household debt stood at £1.5 trillion, one and a half times today's national debt, and four times what it was in 1980.

**How and why were wages and salaries held down over 35 years?**

That's very clear: the central cause was the policy of the Conservative Government from 1979 to 1997. This was consistently to reduce employment protection, and reduce the power of the unions - already on the wane because of industrial change. Top incomes, though, didn't suffer. Those of the top 10% increased comfortably over this period.

All this was under the banner of *freeing the market*. Allow businesses to work without restraints, we were told, and they will prosper. The benefits will come through to all of us. That they didn't - that wages and salaries for 90% of us were being held down - was ignored.

The mania for removing regulations extended to the banking system. Previously, banks hadn't been allowed to create and gamble money so freely. When these regulations were lifted, they went on a spree.

When the Labour Government came to power in 1997, they didn't reverse any of this. Labour had become a free market party too. Indeed, they welcomed the taxes on those bumper bank profits and bonuses. Tories in Parliament continued to call for more deregulation right up to the crash of 2008.

Neither Tories nor Labour like delving into the causes of the crisis. You hear nothing from them about their previous enthusiasm for "freeing up" the banks. Like Governments in many other Western countries, they have become prisoners of a "free market", or "neo-liberal" ideology.
The cuts: now and future

Up to 2015, the Coalition Government cut an average of 9.5% off its budget for all departments providing public services. Up to 2020, if re-elected, the Tories plan to make even bigger cuts. By then, spending per person will have been cut by 29%.

You might think that, when the economy recovers, they plan to restore these cuts, taking us back to where we were in 2008 or so. You'd be wrong. The Coalition parties want to keep these cuts, and make them permanent.

Why? Because that's their politics. They would like the state to be smaller. Fewer public services, more scope for private companies. Lower benefits, made harder to get - so that wages don't have to be increased. A "free labour market" means employers can use zero-hours contracts and exploitative conditions of work. A penal benefits regime is needed to force people into such work, even if they are sick or disabled.

The Coalition parties argue that we can't afford the level of benefits we have. What's cruel about their policy is that all their benefit cuts don't save much, in relation to the scale of the Government's budget. In fact, at the same time as they have been cutting entitlements and shaving percentages off benefits, their own policies have been forcing more people on to benefits and tax credits.

The only conclusion we can draw is that cutting benefits is not about saving money. It's about forcing people into poorly paid, insecure work.

Labour and LibDems say their cuts will be less severe, if elected, but are wedded to the austerity programme, too. The SNP, Greens and Plaid Cymru are clearly opposed. The SNP is in favour of a modest increase in public spending.
Where do the cuts fall?

The Government has promised not to cut the NHS or schools spending (in England), or overseas aid. And they have promised to increase pensions, at least as much as inflation (more, in practice). That sounds good, as far as it goes. But since their overall targets for spending cuts are so severe it means that all other public services will get cut, by 2020, on average, by 45%, compared with 2013.

And social security benefits? Well, they continue to get more cuts and restrictions and the regime progressively more severe.

Cuts to Local Government are particularly deep. Less gets spent on things like home care and residential care for the elderly. This not only reduces the quality of life for sick or disabled older people, but many get stuck in hospital for the lack of suitable accommodation or support at home creating great pressures for the NHS. The NHS budget hasn't been increased to cope with these demands, so effectively it's suffered a hidden cut.

Scotland's budget

Scotland's budget has been fixed by a formula ever since 1979, called the Barnett Formula after the Treasury minister who devised it. This has partially protected Scotland - the cuts here have not been quite so deep, though deep enough. But as bigger slices of tax-raising powers are handed over to Scotland, they get removed from the Barnett Formula calculations.

How this will affect Scotland's overall budget is far from clear. It will have to be sorted out through negotiation between the Scottish Government and Westminster. This is likely to be tough.

Social security benefits don't fall within the Barnett Formula. Scottish people get penalised just the same as everyone else in the UK. Like those in the rest of the UK, for the past two years Scottish claimants have faced increasingly stringent requirements to get benefits: more than 80,000 have had their benefits cut for over 4 weeks for things like being late for an appointment.
Austerity is not only unnecessary, it's destructive. The only reason for it is political - an ideological programme to strip away public services.

*Here's what we should do instead:*

**Increase public spending**
Restore those cuts. Put more into the NHS. Decent benefits. Put more into all those things that build for the future: early years support for young families, education, training. Make good social care a reality. This will not only do good in itself, but boost the whole economy.

**Invest**
Build houses, hospitals, schools, public transport and IT infrastructure. Invest massively in green energy. Encourage research and development in a big way. Invest in training - apprenticeships and other kinds of support. This will help the economy immediately, and more importantly build for the future.

**Better wages and working conditions**
Increase the minimum wage. Outlaw zero hours and other exploitative contracts. Increase enforcement of legislation about working conditions. Repeal legislation hobbling union activity. *Better earnings mean a healthier economy.* Credit card debts don't.

**Reform banking regulation**
Split high street banking from speculative investment banking. Then the speculating banks can go broke if they're reckless, and we don't have to bail them out.

Let's remember, when politicians start preaching about "the deficit": getting life back into the economy is what we need, first and foremost.

The scare story about the terrible threat of debt is a total fabrication. A lie built out of myths.

There's no need to fall for it.
This booklet has been produced by the RIC Edinburgh Economics Group.

RIC is the Radical Independence Campaign, formed in the run-up to the referendum for Scottish Independence of September 2014.

The referendum rejected independence, but the work of RIC has continued: the word "Radical" in the title is just as significant as the word "Independence". What gives RIC its drive is the widespread feeling that the politics of Westminster have, for decades, ignored the increasing inequalities between rich and poor across the whole United Kingdom. All the main parties seem to believe that the existing economic system, and its relationship with the state, is basically sound.

RIC completely disagrees. We believe that radical change is needed. One possible route to achieving that change was to disengage Scotland entirely from the UK state and its inbred establishment. This did not happen in 2014. All the ills and injustices of the regime remain, and Scotland remains subject to them.

One of those injustices is the policy of austerity, consisting of savage cuts to spending on public services and to benefits. It's supposed to get public finances back on a sound footing and get the economy on track.

In fact, it does neither. The real reasons for the policy are quite different. This booklet sets out the facts.