Paying for the Pandemic

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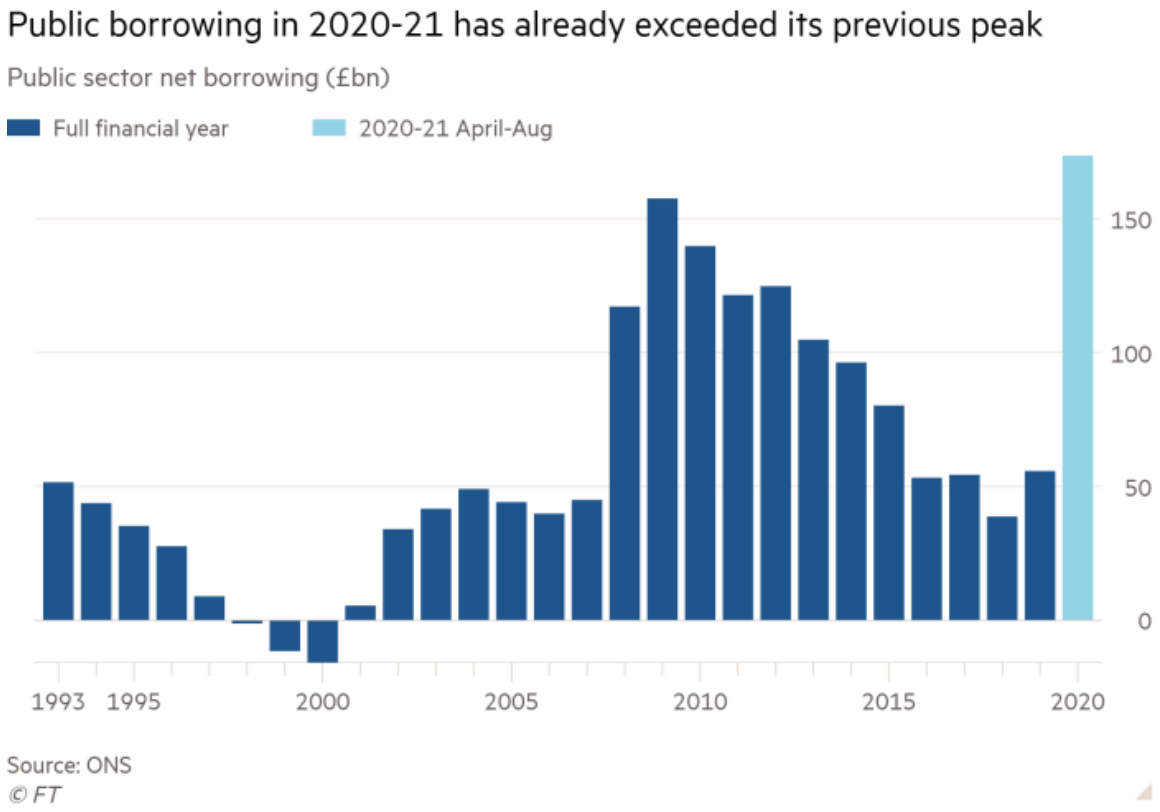
Introduction

This paper argues that the cost of Covid to the UK us unlike any national emergency seen in peacetime. Even with the rapid rollout of the vaccine the UK will face a perfect storm of high unemployment, weak consumer confidence and high debt in the public and private sectors. This paper argues that debt monetisation through quantitative easing and an unprecedented debt write-off by the Bank of England may help release the cash required to stimulate the UK economy and help it recover.

The cost of Covid

The final cost of the Covid pandemic has yet to be totted-up, but the signs so far are that the UK economy will emerge from the pandemic deeply bruised and battered. The Office for National Statistics put it bluntly: “The coronavirus (COVID-19) pandemic has had a substantial impact on the economy and subsequently on public sector borrowing and debt” (ONS, 2021a). The Office for Budget Responsibility (2020) also estimate that public sector borrowing for the 2020/21 financial year could reach £393.5 billion by the end of March 2021. The UK’s National Debt, which reached £1,876.8 billion at the end of 2020 (ONS, 2021a), may easily pass £2 trillion before the pandemic and economic crisis is over.



Even with the rapid rollout of the UK's various vaccines it will not be until towards the end of 2021 that economic recovery can even begin to start. In the meantime, The Claimant Count[1] hit 2.6 million in December 2020, an increase of 113.2%, or 1.4 million, since March 2020 (ONS, 2021b). The economy will be starting its recovery from a position of high unemployment, low consumer confidence, high public, private and corporate debt. The question is, therefore, what action can the UK Government take to both pay for the pandemic while also stimulating the UK economy?

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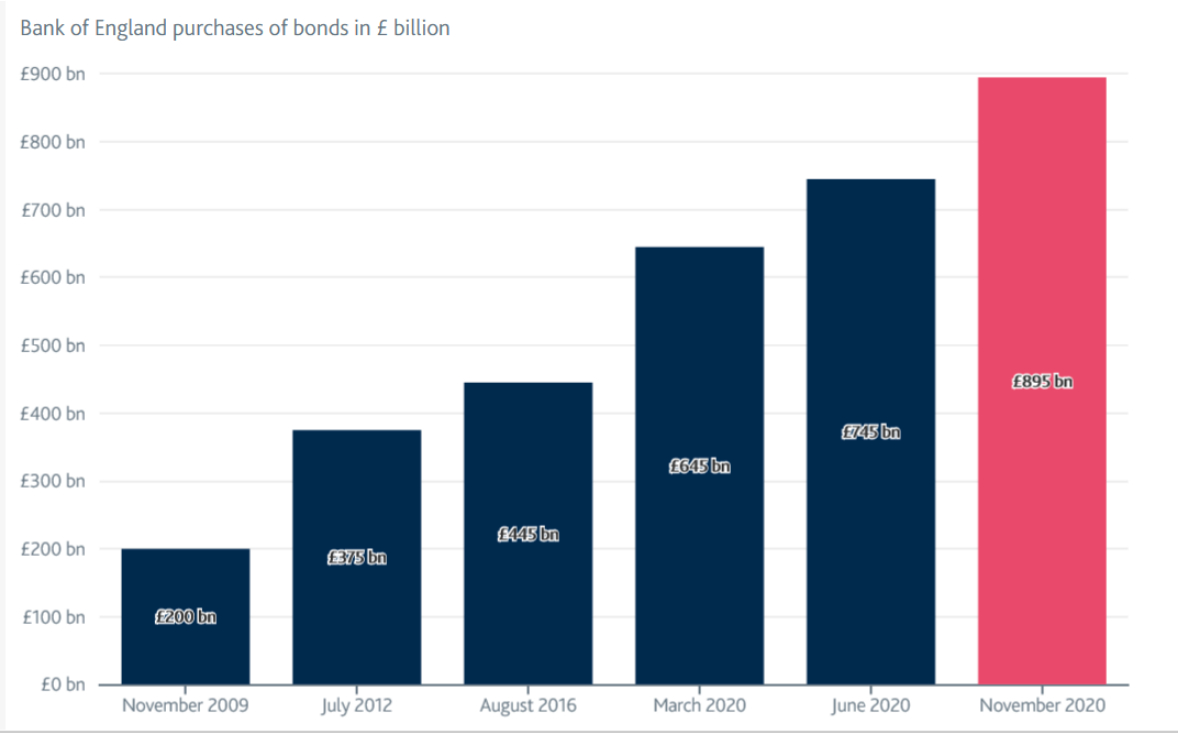
A range of tax rises to pay for the pandemic have been muted including increases on the basic rate of income tax, increasing tax on capital gains, increasing corporation tax, reducing the tax relief on pension contributions, new property taxes, and many more. The risk is that any increase in taxation might smother the flickering flame of any economic recovery by sucking much needed cash out of the economy. The

[1] A measure of how many individuals are claiming out of work benefits such as Job Seeker's Allowance. However, due to Covid some of those claiming support through Universal Credit may be engaged in some form of employment.

reality is that the UK will need additional cash injected to primp-the-pump of economic recovery. So how can the Government deal with its record-breaking debt while injecting fresh money into the economy?

Quantitative Easing 2.0

During the 2007/08 Credit Crunch and Financial Crisis, and since, the Bank of England has engaged in 'Quantitative Easing' (QE). Quantitative Easing is where a central bank, in the UK's case the Bank of England creates digital money which it then uses to buy various assets including UK Government Bonds, i.e. Government debt. Following the most recent round of QE in November 2020 the Bank of England now holds £875 billion in UK Government Bonds and £20 billion of sterling non-financial investment-grade corporate bonds. Thus, the stock of assets held in the Bank of England's 'Asset Purchase Facility' will total £895 billion (Bank of England, 2020).



Source: Bank of England (2020)

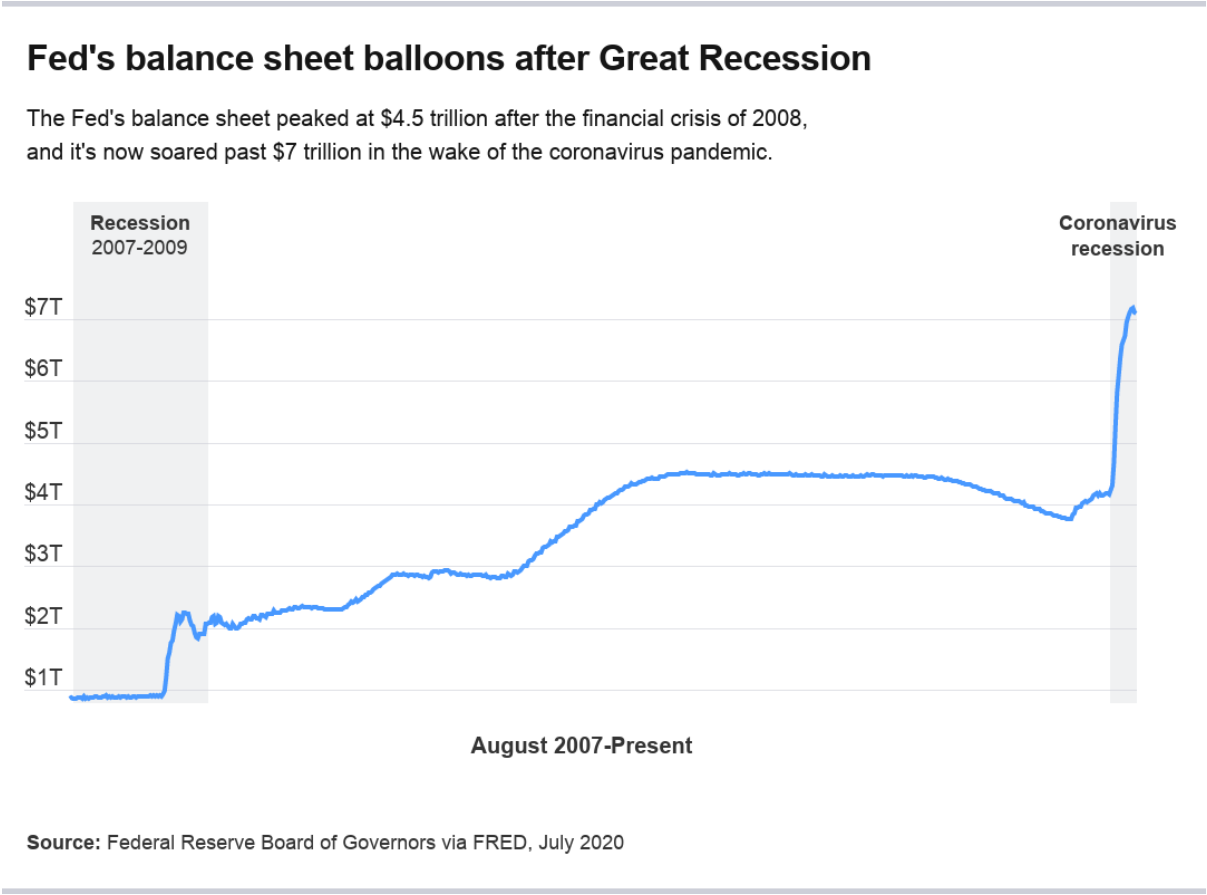
This paper argues that once the Covid Pandemic is clearly on the decline the UK Government should negotiate with the Bank of England to carry out another

unprecedented round of QE. This would involve the Bank of England creating new digital money and buying the majority of the UK's National Debt – known as debt monetisation. The Bank of England could then either keep the debt on their balance sheet indefinitely or write it off. This would allow the UK Government to re-finance any remaining debt at a lower rate of interest and borrow fresh funds to stimulate the UK economy.

Successful Examples

The Bank of Japan has bought up 40% of Japan's national debt and now routinely buys up large amounts of the Japanese Government's debt (The Mainichi, 2020).

The US Federal Reserve holds over $7 trillion of US debt on its balance sheet (Foster, 2020), injecting billions into the US economy through the Coronavirus crisis.



Risks

Despite the apparent advantages debt monetisation is not without risks. Just as printing money in the bank could undermine confidence in a currency the same could occur with Sterling leading to hyperinflation such as has been seen in Venezuela and Zimbabwe in recent years. However, a quick one-off dose of debt monetisation could be just the cure the UK economy required to deal with the effects of Covid.

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