Britain | The end of an experiment

Liz Truss has lost her chancellor, signature tax cut and authority

The prime minister has not done enough to restore confidence in Britain's finances or her own premiership

Oct 14th 2022

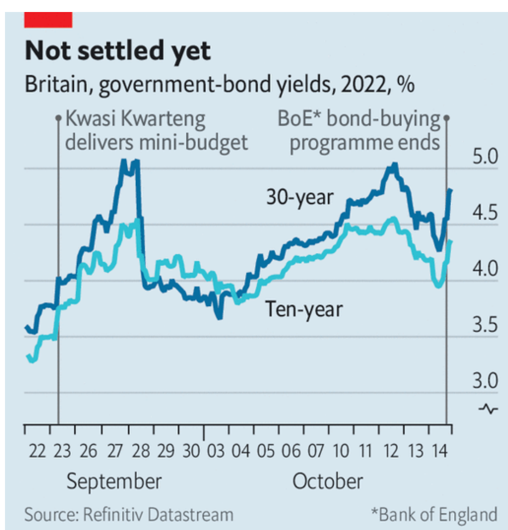
TRUSSONOMICS IS DEAD. Liz Truss started her premiership with a mad dash for growth. She continues to insist that boosting Britain's growth rate is her mission. But whatever remains of her time in office is now focused on a different goal: restoring the faith of the bond markets in Britain.

On October 14th Ms Truss fired Kwasi Kwarteng, the chancellor of the exchequer, and replaced him with Jeremy Hunt, a far more seasoned political operator. Later, at a press conference, she announced that she would reinstate a planned increase in corporation tax. These moves were designed to appease both buyers of British government debt, whose confidence had been shaken by Mr Kwarteng's blow-out budget on September 23rd, and vocal critics from her own party. She has not yet done enough to reassure either group.

Ms Truss's reversal is a humiliation. She had spent the Conservative Party leadership campaign promising to abandon the planned rise in corporation tax. She brushed aside warnings from Rishi Sunak, her rival, that her plans for unfunded tax cuts represented a dangerous "fairy tale" which would stoke inflation. In the end the fiscal statement on September 23rd included cuts worth £45bn ($50bn), an even more lavish giveaway than the one she had dangled during the contest.

That "went further and faster than markets were expecting", she admitted today. Now she says her priority is restoring Britain's credibility with its lenders; she will do "whatever is necessary" to ensure debt is falling as a percentage of GDP over the medium term. As a result, from April companies with profits over £250,000 will see their headline rate of tax rise from 19% to 25%, a level comparable to France and Germany. That will net the exchequer some £19bn a year by 2026-27.

Yet this is insufficient to get the government out of a fiscal hole it has largely dug for itself. Prior to today's statement, Carl Emmerson and Isabel Stockton of the Institute for Fiscal Studies, a think-tank, said borrowing would need to fall by around £62bn in 2026-27 to meet the debt target. Having reversed course on taxes twice (a pledge to abolish the top rate of income tax was abandoned earlier this month), a little over half of Ms Truss's original tax cuts remain. Yet another U-turn would heap further embarrassment on the government: a cut to the Health and Social Care Levy, which means around £15bn in lost tax receipts by 2026-27, has already started going through Parliament.



The Economist

That points to cuts to government spending: Ms Truss said today that "spending will grow less rapidly than face were mostly erased after she began to speak. More ominous was a renewed climb in gilt yields: having fallen to 3.8% on September 30th, the 30-year yield is now nudging 4.8% (see chart).

Investors are meant to wait until October 31st to hear from Mr Hunt how he plans to make the sums add up. To jangle nerves further, an emergency bond-buying programme by the Bank of England, designed to stop fire sales of pension-fund assets that had been set in train by Mr Kwarteng's budget, came to a close soon after Ms Truss had spoken. The bank says that "liability-driven investment" funds, which were at the heart of the mess, have used the programme to improve their resilience to gilt-price volatility. Increased usage of the overnight deposit market, where funds typically park spare cash, suggests that they have indeed started to rebuild their buffers. But with the buyer of last resort now out of the market, bond traders can look forward to a tense session on Monday morning.

Even if the markets settle down, Ms Truss has been fatally undermined. Her authority was shot through as soon as markets rejected Mr Kwarteng's budget. Today's reversal removed what was left. Mr Hunt will wield enormous power over her: she is a "prisoner of the markets", and as a result, "the prisoner of the Treasury", said David Gauke, who preceded Ms Truss as a chief secretary to the Treasury.

Much of her party is determined to get rid of her. Her project of deficit-funded tax cuts and a smaller state always had shallow support in a party that combines a new-found taste for state intervention with an old liking of sound money. Even those Tories who backed her project now have little reason to keep her in place, save for the embarrassment of installing its third leader in a year. The question preoccupying MPs is not "if" but "when": should they move against her now or wait until after the fiscal plan on October 31st?

In a public letter thanking Mr Kwarteng for his 39 days as chancellor, Ms Truss declared that he had "set in train" structural reforms to planning law, as part of her mission of lifting Britain's parlous productivity. In truth, those reforms exist only on paper and face a difficult battle through Parliament. "We share the same vision for our country and the same firm conviction to go for growth," she wrote. Convictions are all she has left. ■

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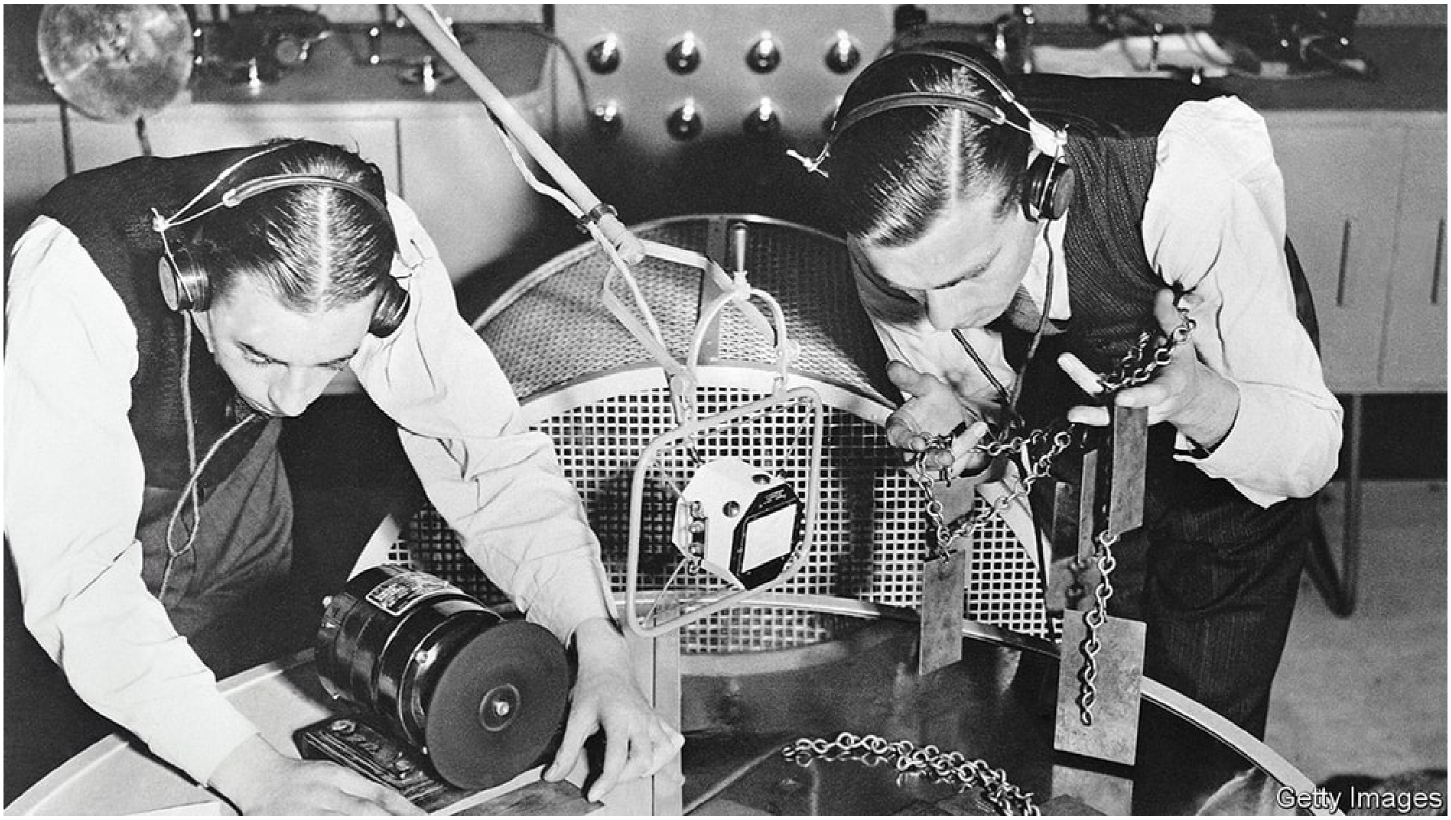

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