
How to pay for the coronavirus emergency: the fiscal challenge

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Abstract: The coronavirus emergency presents the British Government with the greatest fiscal challenge since the Second World War. While the course of the emergency will be determined by the nature of the infection and the arrangements for dealing with it, the course of the recovery from the epidemic will be determined by the financing of the emergency, whether this is done by the government, or left to households and firms running up private debt. The quickest recovery will be obtained by maintaining a high level of government borrowing serviced by taxes on wealth and profits. This would reverse some of the regressive features of the epidemic which is exacerbating an unequal distribution of income and wealth.

Keywords: coronavirus costs; fiscal policy; taxation; government debt; debt management; Keynes; Kalecki.

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1 Introduction

‘... a plan conceived in the spirit of social justice, a plan which uses a time of general sacrifice, not as an excuse for postponing desirable reforms, but as an opportunity for moving further than we have moved hitherto towards reducing inequalities.’¹

Eighty years ago, on the outbreak of the Second World War, Keynes wrote a set of articles for *The Times* newspaper outlining how the British Government could pay for the war effort without unduly restricting consumption. The articles were subsequently published as a pamphlet entitled *How to Pay for the War: A Radical Plan for the Chancellor of the Exchequer*.

No apology is needed for recalling Keynes’s pamphlet, in view of the scale of the coronavirus crisis, and its social, economic and financial consequences for the country. The key requirements are the organisation and provision of medical support and, as in war-time, ensuring that the population can maintain their consumption of essentials, without jeopardising the personal isolation required, while maintaining monetary and financial stability both during and after the crisis. At the time of writing his articles, Keynes had before him the experience and mistakes of the British government’s management of Britain’s contribution to the First World War. This was a clear influence on Keynes’s thinking. In particular it had made him sensitive to questions of how such efforts affected the distribution of income and of the sacrifices that were required. The paper also draws on the work of the Polish economist Michał Kalecki, who shares with Keynes the credit for the Keynesian Revolution in economic theory and policy, and whose commentaries on British war finance in the Second World War placed distribution at the centre of the analysis.² While Keynes and Kalecki could look back on the First World War for lessons, an epidemic is not the same as making war. This time, except for what we may learn from China and Italy, we have very little prior experience that can be used to guide economic policy-making. However, there are similarities in the fiscal challenge that the medical emergency poses.

The unprecedented (in our life-times) nature of the crisis, and our response to it, has changed the way in which we conduct our daily business. This makes any prediction highly speculative. At best an informed observer can try to identify the key factors that will determine the course of the crisis and the recovery from it. While the course of the crisis will be determined by rates of infection, medical needs and the government’s management of the crisis, the course of the recovery will depend on how the material and economic cost of the crisis has been financed. We discuss this element of the crisis in the sections of the report on ‘The character of the problem’ and ‘The character of the solution’. A plan to meet the financing requirements of the crisis is presented in the third and fourth sections.³

2 The character of the problem

Keynes correctly argued that the war-time dilemma was how to compress consumption, to conserve resources for military purposes, while maintaining decent minimum standards of consumption for the least well off. The problem now is rather different: consumption is being compressed by the emergency measures shutting down non-essential retail and other business activities where people congregate, the loss of

opportunities to consume, and by the loss of income of many workers, the self-employed and many small and even medium-sized enterprises.

In another respect, however, there is an important similarity between the situation of the country in 1939 and the present situation that has an important bearing on the consequences of the crisis, and how it should be financed. As in 1939, Britain enters the coronavirus crisis with one of the highest levels of income and wealth inequality in Western Europe, similar to that in Italy. However, unlike other countries with comparable levels of inequality (e.g., Switzerland) Britain's inequality is associated with high levels of poverty and deprivation, principally because of the deregulation of its labour market and welfare 'reforms'.

Table 1 Selected inequality and poverty measures taken from IFS (2020)

<i>Measure</i>	<i>Before housing cost</i>	<i>After housing cost</i>
Ratio of 90th to 50th percentiles of income distribution	2.0	2.1
Ratio of 90th to 10th percentiles of income distribution	4.0	5.3
Fraction of households earning less than 60% of 2018–2019 median	0.17	0.22
Fraction of households earning less than 60% of 1996–1997 median	0.08	0.11
Children in households earning less than 60% of 2018–2019 median	2.8 million	4.2 million
Children in households earning less than 60% of 1996–1997 median	1.1 million	2.0 million

Notes: All figures are net of direct taxes, state benefits and tax credits, and are at the household level.

Source: The data are taken from https://www.ifs.org.uk/tools_and_resources/incomes_in_uk

An idea of the extent of pre-crisis inequality and poverty in the UK is provided by the figures in Table 1, which use survey data compiled by the Institute of Fiscal Studies. After housing costs and the effects of taxes and state benefits are taken into account, around a fifth of households in the country live in relative poverty, defined as earning less than 60% of median household income. Over 2 million children live in households suffering poverty. The situation is deteriorating rapidly with the policy response to the crisis that overwhelmingly favours the propertied classes, and the salaried middle class. The material condition of the propertied classes has not been altered by the crisis, and it turns out that the labour process of the majority of the salaried middle classes depends on online skills that may be easily located at home. This is not the case with manual workers, who have borne the brunt of the shut-down of manufacturing and non-essential retail and hospitality activities. In Britain employers may 'furlough' them (cease paying them and have the government pay a basic replacement income), or put them on sick pay. By the beginning of May, over 6 million workers, or almost a quarter of the labour force, were receiving this basic income in place of their normal wages. A lower segment of the population, unemployed or on self-employment contracts, are thrown on the mercies of a welfare system whose reforms over decades have been designed to reduce support and make it more selective and less accessible. Finally, at the bottom is a shadowy stratum of

refugees and illegal migrants, whose precarious legal situation prevents them from ever approaching an official body with a request for assistance.

The rapid deterioration in the economic condition of those on the lowest incomes has two important consequences for the crisis. In the first place, the concentration of people in poverty in urban areas prolongs the struggle to control the spread of the virus because of cramped living conditions, chronic health conditions and poor diets, and the tendency of occupations most exposed to the virus to pay less than average employment income.⁴ In the second place, with meagre and delayed support from the state or their community, those facing poverty will do what they have always done in the face of urgent need. Without the means to satisfy their needs, they will borrow.

A consequent rise in household debt will hold down consumption in poorer households when the crisis is over, and smaller businesses will be crippled with debt repayments. However, with consumption restricted to food and household necessities, there will also be a build-up of liquidity in the banking sector. Limited economic activity is concentrating cash flow among suppliers of food, medical supplies and other basic necessities. Monopolistic practices will further concentrate liquidity in big businesses, in a process which is exacerbated by the apparent success of the government's support for larger firms during the crisis alongside the relative failure of its support package for smaller firms.⁵ This is confirmed by bank balance sheet statistics published by the Bank of England. Sterling money balances held by private sector companies and households rose by £57.4bn in March 2020, the largest increase on record – the previous six-month average had been a modest £9bn. Borrowing from banks rose by £55.3bn, some ten times the previous six-monthly average of £5.1bn.⁶

While the consumption of poorer households will remain depressed after the crisis, the gradual removal of restrictions on commercial activities will lead to a recovery of demand by wealthier households. In particular, we can expect consumption by the salaried middle class to be reinforced by the 'forced savings' accumulated during the crisis. These households will meet the supply of indebted businesses keen to generate the cash flow to repay their debts, which they will achieve in part by raising prices. The consequent problem of profiteering and inflation, as businesses raise their prices to pay off debts incurred during the crisis, will make life even more difficult for those on low incomes.

Normally, a boom in consumption would bring about a recovery in tax revenue, in particular in VAT receipts and corporation tax. However, as we have outlined in the foregoing, the present crisis is aggravating inequalities that were already indefensible prior to 2020. The post-crisis consumption expenditure of the wealthy is likely to be off-set by the muted consumption of low-income working households and the unemployed. If the government reverts to austerity with cuts to the social security system, attempts to reduce health service expenditure back towards whatever levels are deemed 'normal', or the imposition of regressive taxation such as increases in VAT, then the recovery of consumption and tax revenues will be further delayed.

Hence a rapid effort to 'normalise' the government's finances to pre-crisis levels, relative to national income, will abbreviate the consumer boom, slow down the recovery of tax revenues, and could contribute to a recession similar to that which followed the First World War. In addition, the withdrawal of emergency housing and maintenance payments will throw very visibly onto the streets the homeless and the destitute who are currently being sheltered – at least in part – from the worst effects of the virus.

3 The character of the solution

While the casualties of the epidemic are being treated, Government expenditure will rise to pay for medical supplies, NHS staff and welfare payments, while tax revenues will fall off with restricted consumption and incomes. After the pandemic, levels of government expenditure should be maintained to support cash and income flows in the private sector. A fixation on reducing fiscal deficits or government debt, just because the medical need has fallen, will hobble the economic recovery and frustrate the intended reduction in debt. Alleviating the effects of the crisis *and* financial stability in the recovery require public sector deficits and debt to maintain expenditure and income flows. For reasons given below, it would be irresponsible to place the burden of the crisis and the recovery entirely on households and firms.

Part of any budgetary resources freed up by the eventual reduction of expenditure on COVID-19 should obviously go towards clearing the backlog of medical and surgical treatment that has been deemed ‘inessential’ in the crisis. There is already evidence of a rise in non-coronavirus-related deaths that have been attributed to a reduced willingness of sick people to visit doctor’s surgeries or hospital emergency clinics. People in need of care, including cancer patients, should not be forced to wait for treatment in order to provide ‘spare capacity’ in the health service. Another part of the budget can be redirected towards expanding expenditure on housing, social services, care for the elderly and further education, all of which have been suffered severe cuts since 2010. This will help to avoid the worst of the recession and go some way towards alleviating the impact of the crisis on inequality and deprivation.

All of this amounts to a sizable fiscal commitment. The question that inevitably arises is how can this expenditure be financed? In the past, Keynesians have relied on the argument that the economic recovery will provide the resources to pay for fiscal stimulus. This may be correct as a statement of optimism. But it does not provide a plan for financing the recovery. In particular, if economic activity fails to recover and make up for the losses in production and employment income, then the economic recovery will not provide the necessary resources. Such a disappointment is unlikely to strengthen the Keynesian argument.

The obvious way of financing the crisis, that will appeal to fiscal conservatives is by raising taxes. If taxes are to rise, as a matter of basic equity it should be taxes on wealth and excess profits. Such taxes would not adversely affect real investment or household consumption, and could facilitate the continued government expenditure required to prevent recession and make current investment pay in the future. However, the amounts that can be raised by taxation are inevitably limited, and the prospects for a balanced budget at a time when economic activity is in decline are unrealistic. The crisis is an economic crisis not only because business activities have reduced during the emergency, but also because its cost exceeds the money that may be raised in taxation at the time of the crisis without impeding the recovery.

A second, more spontaneous solution is already happening: the expansion of private debt. This is augmented by a third measure, the expansion of public borrowing. The fourth way of financing the crisis is by monetising the government deficit.

If the government did nothing other than restricting people’s movements and providing the health services, the financing of the crisis would involve a huge rise in private debt. With bills to pay and faced with a loss of income and no replacement of that

income from the government, households and firms will turn to borrowing formally from banks, or informally from suppliers or landlords with postponed payments or rents. But this is not the debt that economists talk and write about in economics books, where people borrow in order to invest. Crisis debt, or ‘forced indebtedness’ has no economic purpose other than survival. It has not been incurred in order buy any asset. It drains future cash flow and makes creditors reluctant to lend, precisely because there is no asset to provide a future income out of which the borrowing could be repaid (hence the need for a government guarantee).

Therefore, to maintain their credit standing, borrowers of emergency private debt will seek to repay that debt in the recovery. They will do so by raising prices and holding down their expenditure. The greater the debt incurred by private firms and the self-employed for the purposes of maintaining their payment commitments during the crisis, the greater will be the subsequent debt deflation – holding down expenditure on employees and suppliers in order to pay down outstanding debt – inhibiting the post-crisis recovery in employment. The greater is the reliance on private sector debt arrangements, the greater will be the desire of private sector firms and the self-employed to raise prices in order to recover a large enough cash flow to allow for the repayment of crisis debt.

This is not just a question of the debt facilities that are being guaranteed by the Government through the commercial banking system. Where borrowers are in a position to cover their current costs from income, some of the low interest government-guaranteed loans will inevitably be used to repay more expensive unsecured bank loans, or unsecured credit card debt. But reliance on private debt will permeate the whole economy with formal and informal debt, whether it is postponed rent or mortgage payments, or borrowing from friends and associates, whose only purpose is surviving a period of income deficiency, rather than to secure a future income.

The dangers of inflation, combined with falling real wages, will slow the economic recovery into the kind of stagflation that hit Britain during the late 1970s, with disastrous economic, social and political consequences. Avoiding such an outcome means relying on the government to finance the crisis and the recovery from it. However, the government too has been hit by a drastic fall in its revenues. Thus, financing the crisis means relying on deficit financing on a scale unknown in modern times.⁷

Government borrowing will therefore be necessary to overcome the crisis. The Office of Budget Responsibility estimates that public sector borrowing will increase by £229 billion as a result of the crisis, with public sector net debt rising to over 100% of GDP on a financial year basis.⁸ The Institute for Fiscal Studies has noted that a public sector deficit of £200 billion this year is, ‘well within the bounds of possibility’, and the Institute for Government have made a similar argument.⁹ These deficits can be financed in two ways: monetisation or the issuance of government debt. We will discuss these options in turn.

3.1 Monetising the deficit

At the time of writing, the Bank of England has announced a temporary extension to the Ways and Means facility, which is essentially the government’s overdraft facility at the bank.¹⁰ Government spending financed by the ways and means facility is a way of financing government expenditure by creating bank reserves. An overdraft loan from the bank is an asset for the bank, even if it is a liability for the British Treasury. Since the

Bank of England is owned by the Government, the net debt position of the public sector is zero. However, the extension is only meant to provide a temporary source of short-term liquidity, primarily for the purposes of cash-flow smoothing.

Monetising the public sector deficit would go beyond cash-flow smoothing and leave some larger businesses and middle class households with highly liquid balance sheets, which is already apparent in the banking data cited above. This could be considered an inflationary threat, and the Bank of England has in fact made clear that it opposes monetisation of the deficit. To some degree this is a residual adherence to the monetarist doctrine, according to which an increase in the money supply is inflationary. A more realistic threat is that highly liquid balance sheets alongside a shortage of safe domestic assets would lead to a flight to dollars. The resulting depreciation of sterling, by making imports more expensive, would then bring about the feared inflation.

On the other hand, monetisation of the fiscal deficit is useful to relieve liquidity pressures in the bond market. Moreover, insofar as it facilitates the retirement of private debt, it could even alleviate inflationary pressure. This is because the situation discussed above, in which ‘forced indebtedness’ induces firms to attempt to pay off debts by raising prices, can be mitigated to some degree by increases in cash-flow. If private debt is retired in this way, at the same time as the government issues bonds, then monetisation could facilitate the conversion of private debt into public debt. There is already some evidence that this is happening. In March 2020, households made repayments (after deducting new loans) of household debt of £3.8bn; credit card debt was repaid, net of new credit, of £2.4bn.¹¹ These record repayments reflect the high liquidity of middle class and wealthier households. The condition for alleviating business debt is government expenditure targeted at expanding the cash-flow of over-indebted businesses and poorer households. This means that, for monetisation to work effectively, government expenditure needs to be targeted at those households and firms that have accrued crisis debts, so that as the government expands the money supply, the private sector reduces its borrowing.

3.2 Government borrowing

In comparison to monetisation, the sale of government bonds has the advantages of absorbing the excess liquidity in the banking system built up during the crisis and increasing the stock of safe sterling-denominated assets for intermediaries and institutional investors. Contrary to a popular misapprehension, government debt is not a ‘burden on our children’ or a transfer of income from future generations to the present generation. A domestically held government bond is simply a commitment for future taxpayers to pay future bondholders in the same economy, with any decrease in national income only taking place if the bonds are issued to foreign residents. However, typically less than 30% of government debt is held by foreign investors, and at least some of this will have been bought on the secondary market, repaying the original bondholders.

The sale of government debt in the UK is organised by the Debt Management Office on behalf of the Treasury. Usually, the management of public debt is conducted with a view to minimising the cost of borrowing over the long term while minimising interest rate risk. This leads to a trade-off: shorter maturity gilts offer a lower borrowing cost but have to be regularly rolled over, exposing the government to the risk that interest rates might rise, while longer maturity gilts offer a higher borrowing cost but without any risk

of this increasing in the short term. Longer term bonds also have the advantage that they can mop up excess liquidity in the financial markets. In fact, the Debt Management Office has the general objective of minimising borrowing costs using a broadly even split between bonds of different maturities, and a split between ordinary and index-linked bonds.

The benefit of financing deficits by issuing debt in the present conjuncture, aside from the advantages of absorbing excess liquidity and providing a stock of safe assets, is that interest rates on all maturities of debt are extraordinarily low. In fact, nominal yields on long-dated bonds were around 1% prior to the crisis,¹² and real yields have been negative across the entirety of the maturity spectrum for some time. In real terms, investors are paying the government to borrow, and in this situation the trade-off between funding cost and risk suggests that the Treasury ought to increase the emphasis on longer maturity gilts in their bond portfolio – particularly in a situation where a rapidly rising stock of debt inevitably raises the interest rate risk of short-dated bonds.

The government should therefore in the first instance finance its emergency expenditure through the issuance of long-term debt. As explained in an earlier report by Michell and Toporowski (2019), ‘Can the Bank of England do it?’, the experience of quantitative easing demonstrates that central banks have the capacity to control both short term interest rates and the yields of longer maturity debt, giving them *de facto* control of the yield curve after the last crisis.¹³ Moreover, the flattening of the yield curve after 2008 introduced a number of potential risks, including a reduction in the profits of banks and the solvency of institutional investors, leading to the threat of disintermediation in the first case and a search for yield in riskier assets in the second. A larger stock of safe, long-dated bonds would allow the Bank of England to stabilise the yield curve at a level which ensured financial stability, providing a final benefit to the government of financing the crisis through the issuance of debt.

4 Can the rich pay for the crisis?

In *How to Pay for the War*, Keynes argued that the rich really aren't rich enough to pay for the War, and therefore that some of the burden would have to be taken by workers in the form of deferred payment of incomes or forced saving. This is not the case today. We have the opposite phenomenon of forced saving by the salaried middle class unable to spend their incomes, and the concentration of liquidity in large corporations. As we discuss in the first section of this document, the crisis is exacerbating existing inequalities in the UK. Moreover, the salaried middle classes are the least likely to suffer from recent increases in unemployment, and large corporations have had access to support from the government and the financial markets to assist with managing their liquidity. Most wealthy households and large firms will therefore continue to be in a healthy financial position following the crisis, unlike low-income households and small businesses.

Less obviously, taxes that the wealthy pay towards government expenditure are received back as profits in the companies that they own or interest on the bonds that they hold – sometimes individually, but more often via pension funds. A government bond is simply a commitment for *future* taxpayers to pay *future* bondholders. A shift towards a more progressive tax structure after the crisis would facilitate sustained government expenditure at a high level, because the extra taxation required to pay the interest on any bonds issued to finance the crisis would then fall on those with savings. In this manner,

financing the crisis via the issuance of long-dated debt would not result in a further increase in inequality. The payment of interest on government borrowing through higher rates of taxation on the wealthy merely redistributes income among the wealthy.

More importantly, there is a moral and a political case for requiring better-off members of society to pay for the medical emergency. The rich have by-and-large avoided the worst effects of the crisis, while the poor, living in poorer health even before the epidemic and in conditions that make it impossible to isolate themselves from family members infected by the virus, have lost incomes and livelihoods. Death rates by districts show this very clearly, with deaths from COVID 19 in the poorest districts being at twice the rate of such deaths in the wealthiest districts. This is the moment for the better-off to demonstrate that they are prepared to contribute on a scale that is modest by comparison with the sacrifices expected of the less well-off, including those healthcare and social care employees who have risked their lives and suffered the highest death rates.

5 Details

As discussed above, estimates of the extent of extra government borrowing resulting from the crisis are in the region of £200 billion, and the government has announced that it intends to issue £180 billion of bonds between May and July 2020.¹⁴ However, the Office of Budget Responsibility have been clear that the extra borrowing required to respond to the crisis could be considerably greater than this if the lockdown is longer than three months. The Resolution Foundation have made the same point, estimating that a six month lockdown would imply borrowing in the region of £400 billion.¹⁵

Table 2 presents a table of potential borrowing costs if the government finances its crisis expenditure by issuing long-term debt. If yields on long-dated gilts stay at around 1%, then the additional annual cost for servicing the increased debt can be expected to remain below £5 billion. Even if – as the Resolution Foundation warn against – interest rates rise to over 2%, we can reasonably expect the additional annual borrowing cost to remain somewhere between £5 billion and £15 billion per year.

Table 2 Approximate borrowing costs of the crisis

		<i>Gilt issuance</i>			
		<i>£200 bn</i>	<i>£300 bn</i>	<i>£400 bn</i>	<i>£500 bn</i>
Interest	1%	£2 bn	£3 bn	£4 bn	£5 bn
	2%	£4 bn	£6 bn	£8 bn	£10 bn
	3%	£6 bn	£9 bn	£12 bn	£15 bn

If, therefore, the government were to finance its expenditure over the crisis by issuing 30 year ‘recovery bonds’ – 30 year gilts had a yield of 2% in January 2018, just under 1% in January of this year, and at the time of writing are trading with a market yield of less than 1% – it would face an additional annual borrowing cost which could easily be covered by increases in progressive taxation without the need to cut government spending. Moreover, if the government were to formalise the Bank of England’s efforts to stabilise the yield curve with an extension to its mandate, as suggested by Michell and Toporowski (2019), it could take advantage of the lower yields (and greater market depth) offered by shorter dated gilts without a considerable increase in interest rate risk.

Estimates of the marginal increase in annual revenue offered by different forms of taxation are presented in Table 3, using information from HMRC's 2019 'ready reckoner' tables,¹⁶ the IPPR's 2013 proposals for wealth taxation,¹⁷ and Avinash Persaud's 2017 proposals for reforms to the taxation of financial transactions in the UK.¹⁸ These are, of course, estimates based on economic data from previous years, but in two to three years' time, after nominal GDP has recovered from the crisis, the orders of magnitude to be expected from similar tax increases should be similar to those presented in Table 3. The IPPR note that wealth taxes are relatively unusual today, but did exist in the past in countries like Austria, Germany and the Netherlands, and still exist in Norway and Switzerland. Persaud notes that, aside from the substantial revenues it would generate, reform of the UK's financial transaction tax could improve financial stability, complement efforts to shift the economy away from short-termism, and improve HMRC's knowledge of offshore assets held by UK residents.

Table 3 Revenue estimates from progressive taxation

<i>Tax</i>	<i>Revenue estimate</i>
Increase higher income tax rate by 1p	£1.35 bn
Increase corporation tax by 1 percentage point	£2.8 bn
IPPR net wealth tax (1% on non-pension assets exceeding £500,000)	£6.9 bn
Persaud reforms to financial transaction tax	£4.68 bn

Thus, introducing and reforming wealth taxation in the UK could raise the revenue necessary to cover the annual interest costs of long-dated gilts issued to finance government expenditure over the current crisis. Alternatively, the government could raise a non-trivial sum of money by increasing the higher rate of income tax by two or three pence, and a significant amount by increasing corporation tax from its current rate of 19%, which stood at 28% as recently as 2010. Certain figures in business might object to an increase in corporation tax, but there is little evidence that firms forego profitable opportunities just because 20%, 25%, or even 30% of those profits are taxed away. By comparison, when Keynes wrote his pamphlet, an Excess Profit Tax had been instituted to combat the egregious profiteering that had resulted from the more *laissez-faire* approach to financing the First World War. That Excess Profit Tax had raised the marginal rate of tax on profits to 75%.

Finally, the borrowing costs approximated in Table 2 do not take into account any extensions to the Bank of England's quantitative easing program. In fact, the bank announced an extra £200 billion of quantitative easing in March 2020, which will replace government bonds on private sector balance sheets with reserves that pay the bank rate. Without knowing which gilts the Bank of England will buy – and therefore the yields on those gilts – it is difficult to estimate the flow effect on the public finances of this increase in quantitative easing. However, in 2017–2018 the Bank paid less than £2 billion on the reserves issued to finance the existing amount of quantitative easing, earned £15 billion of interest on the gilts, and transferred a net sum of £9 billion to the Treasury.¹⁹ Whatever savings are made on interest payments resulting from the recent extension to quantitative easing – and we might expect this to be in the low billions – will offset the interest costs given in Table 2.

6 Conclusions

The COVID-19 crisis is aggravating health and other social inequalities in the UK. How long the crisis and those inequalities last depends on the government's management of the medical emergency. In turn, the economic consequences of the emergency and the scale and nature of the economic recovery will depend on the character of fiscal policy and how it is financed. Importantly, the gradual emergence from lockdown and the subsequent recovery will require high levels of government expenditure for a considerable amount of time. Those will also need to be financed in a more equitable way.

Monetary expansion of one form or another will play some role in financing this expenditure. But the government will have to ensure that any monetary stimulus reaches the indebted households and firms that need it most. Inevitably, however, the bulk of the deficit will need to be financed by borrowing from the financial markets, and the most straightforward way to stabilise and strengthen the recovery without exposing the state to unnecessary levels of interest rate risk is through the issuance of long-dated government bonds. The interest costs of the debt issued to finance the fiscal response to the crisis should be paid for by a wealth tax, reinforced where necessary by corporation tax and other progressive forms of taxation. This is completely affordable given the likely sums involved. There is no reason to reinstate the fiscal austerity that has characterised British economic policy since 2010.

It is only possible to bring people together to combat the epidemic – and secure a just recovery in its aftermath – if the effort demanded is seen to be fair. The support given to health service employees and key frontline workers and volunteers shows the widespread willingness to share the burden of the crisis. Governments in all countries affected by the epidemic must respond to this willingness by committing to a fair system of financing the crisis and the recovery. If commitment to an equitable sharing of the fiscal burden is left until after the crisis, the consent of the well off to such a commitment will depend on altruism, and those who sacrifice the least will have the least invested in that altruism.

A healthy society needs a healthy tax system. For decades tax systems have been rendered inefficient by 'supply-side' doctrines that exaggerate the sensitivity of the wealthy and business to taxation, as if the rich were discouraged from enterprise by taxes rather than private income, or entrepreneurs forego profitable business because they have to contribute a fraction of the proceeds towards the social and physical infrastructure that makes such business possible. Moreover, these doctrines have contributed in large part to the levels of inequality and poverty that exist in the UK, that are being exacerbated by the current crisis. The scale of the crisis and the unprecedented solidarity that it has evoked are an opportunity to undo some of this damage by a rational approach to public debt and progressive taxation.

The economy too stands on a knife-edge. A reliance on *laissez-faire* policies in effect involves a reliance on private debt, which will burden business and be repaid through inflation and economic stagnation. Rising government debt is inevitable and must be met after the crisis by more progressive taxation to service that debt. More progressive taxation is vital precisely because taxes on wealth and savings have the least effect on expenditure and income: regressive taxation weakens the economic stimulus from government expenditure.

Politically and economically the period after the crisis is the most dangerous for policy. If there has been too much reliance on private debt, resulting in slow recovery and inflation, siren voices on the right will blame the growth of government debt and demand reductions in government expenditure and cuts in taxes on the rich, ostensibly to prevent economic catastrophe. But there is no need to fear any rise in government debt. As long as that rise in debt is through the issue of long-term bonds that are serviced by taxes raised on wealth, it is simply a financial operation that effects the adjustment in the wealth portfolios of the rich necessary to maintain monetary and financial stability. If financed by a tax on profits, the increase in government borrowing has more or less the same effect, although the process is less direct. If we give way to the urge to reduce public debt or abandon progressive taxation, this will only reinforce slow growth and the rising inequalities that have marred economies in the 21st century. The society that survives the epidemic and grieves the human losses deserves better.

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Notes

- 1 Keynes, *How to Pay for the War*, 1940, p.1.
- 2 See in particular Kalecki's 'The 'mysteries' of the money market' 1940, and 'The debt burden' 1943.
- 3 The section titles are taken from those of Keynes's pamphlet. Financial aspects of this paper draw on Calvert Jump and Toporowski (2020).
- 4 <https://autonomy.work/portfolio/jari/>.
- 5 See e.g., <https://www.cityam.com/the-long-read-the-coronavirus-loan-scheme-risks-failing-the-people-it-was-designed-to-help/>.

- 6 Bank of England ‘Money and credit March 2020’,
<https://www.bankofengland.co.uk/statistics/money-and-credit/2020/march-2020>.
- 7 During the Second World War, the fiscal deficit at its peak reached 27% of GDP.
- 8 <https://obr.uk/coronavirus-reference-scenario/>.
- 9 <https://www.ifs.org.uk/publications/14771> and
<https://www.instituteforgovernment.org.uk/explainers/coronavirus-public-borrowing>.
- 10 <https://www.bankofengland.co.uk/news/2020/april/hmt-and-boe-announce-temporary-extension-to-ways-and-means-facility>.
- 11 Bank of England ‘Money and credit March 2020’,
<https://www.bankofengland.co.uk/statistics/money-and-credit/2020/march-2020>.
- 12 <https://www.dmo.gov.uk/media/16337/drmr2021.pdf>.
- 13 <https://progressiveeconomyforum.com/publications/can-the-bank-of-england-do-it-the-scope-and-operations-of-the-bank-of-englands-monetary-policy/>.
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- 15 <https://www.resolutionfoundation.org/publications/doing-more-of-what-it-takes/>.
- 16 <https://www.gov.uk/government/statistics/direct-effects-of-illustrative-tax-changes>.
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- 18 https://papers.ssrn.com/sol3/papers.cfm?abstract_id=2908464.
- 19 See the OBR explainer at <https://obr.uk/forecasts-in-depth/brief-guides-and-explainers/direct-fiscal-consequences-unconventional-monetary-policies/>.