{ ECONOMIC GROWTH }

JEREMY WARNER

The risks of relying on government expenditure and credit-fuelled private consumption

Even unbalanced growth, Eddie George, former governor of the Bank of England, once famously said, is better than no growth at all. His remark set the scene for nearly a decade of credit-fuelled, consumption-led growth.

When the coalition government came to power in 2010, it forswore these bad old habits and promised that, in future, growth would be based on much worthier and sustainable sources – business investment, net trade and the 'march of the makers'. Unsustainable, debt-funded, government consumption would also be reined in.

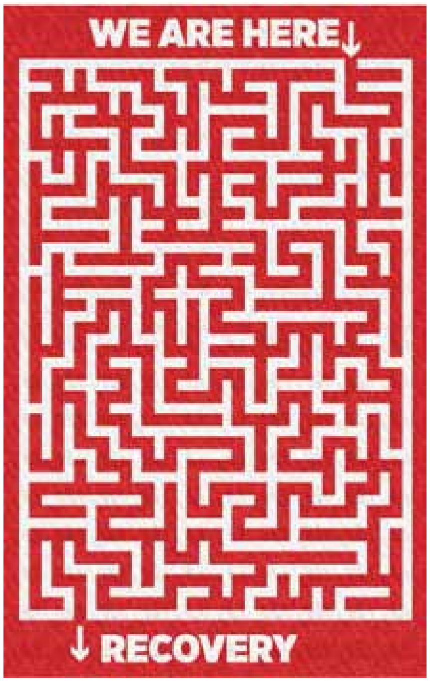
As the government celebrates the recent outpouring of relatively upbeat economic news, and claims on the back of it final vindication for its economic strategy, it is worth noting that none of these noble ambitions have been met. To the extent that growth is returning, it looks much like the old sort – still-growing government consumption, a fast-reviving housing market, and credit-fuelled private consumption.

Notably absent as drivers of growth are net trade and business investment. The experiment with austerity has been all but abandoned, a series of off-balance sheet initiatives to boost the housing market have been announced, and the government has adjusted the Bank of England's remit to allow interest rates to be kept low into the indefinite future. Saving has been disincentivised and borrowing to spend is once more being encouraged.

In short, the economic revival that is finally getting under way has virtually nothing to do with the economic strategy originally adopted by the coalition government. Indeed, it is only really since that strategy was quietly ditched that things have started to pick up. With the UK general election now less than two years away, George Osborne, the chancellor, was desperate for some growth – even the wrong sort of growth will do.

Lingering structural deficiencies in the public finances and the wider economy have been swept under the carpet for another day. The Juncker curse (named after the Luxembourg premier who articulated it) has struck again: "We know as leaders what needs to be done, we just don't know how to get re-elected after doing it."

With the UK general election now less than two years away, George Osborne, the chancellor, was desperate for some growth – even the wrong sort of growth will do



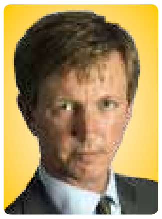
Of course, a rather more charitable version of what's happening is that it is first necessary to get the recovering drunk out of bed with some 'hair of the dog that bit him treatment' before the rebalancing to a more sustainable form of growth can take place.

It's what Lord King, recently retired governor of the Bank of England, has called "the paradox of policy" – that initially at least, debt must be fought with more debt, that a crisis caused by too much confidence, too much borrowing and lending and too much spending, must be countered with more borrowing and lending, more spending and a revival in risk taking.

Even in the eurozone, the point has begun to be recognised. With some periphery economies experiencing depression-like conditions, ruthlessly imposed austerity programmes are being eased, the European Central Bank has broken with tradition to indulge in 'forward guidance' on interest rates, and so on.

To put all this in perspective, there doesn't appear to be any immediate danger of another, no-holds-barred outbreak of reckless banking and hell-for-leather credit expansion. We are still a very long way from the conditions that occurred in the run-up to the financial crisis. Government deficits are also being steadily reduced.

Yet, as we have seen, unbalanced growth eventually becomes addictive, and in the end, it is always profoundly destabilising. The challenge for policy is no longer the life support of central bank money printing, but the sort of difficult supply side and fiscal reform that might give Britain and Europe a more sustainable future. Democratically elected politicians don't tend to be very good at this sort of thing.



Jeremy Warner is assistant editor of *The Daily Telegraph* and one of Britain's leading business and economics commentators