

NOTES OF COMPASS COFFEE MORNING – 22ND MARCH 2025

‘IT’S THE ECONOMY, STUPID’ – IS REEVES RIGHT, IS THERE NO ALTERNATIVE?

Speakers:

- Polly Toynbee – Guardian columnist, author, most recently (with David Walker) of *The only way is up*
- Stewart Lansley – economist, visiting fellow, University of Bristol, Compass Associate, and Council Member, the Progressive Economy Forum – author of *The Richer, The Poorer* and of a new Compass report *Paying for a decade of national renewal*

STEWART LANSLEY

A question to the audience: every year The Economist compiles a list of the best performing economies in the world. In 2024, the best was Spain. Where was the UK? Answer: 31st.

This gives us an indication of the state of the economy Labour inherited. There is no question that it’s in a mess – we’ve had slow growth, nearly static living standards, the public finances are in a worse state than at any time since the war, and public services are crumbling.

What lies behind the dire state of the economy Labour has inherited

There are two reasons for this:

- a series of rolling shocks over the last 20 years that all countries have faced – the 2008 financial crash, the pandemic and climate change
- in the case of the UK – many of the problems we face are essentially self-inflicted by bad economic policy
 - austerity – applied more heavily in the UK than in any other country since 2010
 - an over-privatised economy – the market has been pushed into areas e.g. social care, housing (the housing market is almost completely privatised now) where the market shouldn’t be, and that has impacted on the way the economy runs.

Two other important factors

- the economy and the political system have a bias to inequality – much of the policy base of this country makes inequality worse
- an inbuilt tendency to contraction – it’s not surprising that Britain has had a static economy for the past 15 years, because if you look at the way the economy runs, there is a built-in tendency not to grow

The underlying reasons for this lie in the full-blooded adoption of neo-liberal doctrines – the counter-revolution against post-war social democracy – and in Britain we have built an aggressive and predatory model of capitalism. This has entailed a massive transfer of power over the last 30 years away from labour, workers, the state, regulators and democratic institutions towards 3 groups:

- corporate boardrooms
- the finance sector
- the hugely grown billionaire class.

These people are having a much greater impact on the way society and economies work than was the case before the neoliberal agenda.

The way the corporate sector has seized this power was not what the neoliberal evangelists were supposed to do, which was build a stronger and more efficient economy in which everybody would be better off. Instead, they have essentially used it for self-enrichment. We need to understand the distinction between wealth creation (Starmer's no. 1 priority, as it was for Blair and Thatcher) and wealth extraction or wealth appropriation. Wealth creation is when we invest to make the economy stronger, to build the size of the cake from which everyone potentially benefits. Wealth extraction is when the powerful simply grab a share of the cake, which doesn't make the cake bigger, but simply redistributes it upwards.

Over the last 30 years, there has been a shift from wealth creation to wealth extraction. The mechanism by which this happens is that big corporations have been turned into cash cows for their owners, dividends have been rising at 10 times the rate of wages over the last 30 years, and some companies have been turned into private fiefdoms – e.g. the global technology companies. A critical factor is that far from this very competitive economy that was supposed to happen from all these processes, what we've had is anti-competitiveness – Britain, the US and the world at large have moved towards what is essentially a semi-monopoly situation. Looking at Britain, nearly all the most important markets, from energy supply to supermarkets, food, banking, construction – are controlled by a handful of firms, for example 80% of housing is built by the top 4 firms. This gives immense power, and we have very weak regulations for preventing it.

If we look at the effect of these things – which are happening globally as well as in the UK, although the UK is to some extent an extreme example of it – who has gained from global growth over the last 25 years: the top 1% globally have gained 35% of that growth, the bottom 50% have gained 2%. So that is the reason why we've had large surges in inequality.

What is Labour's strategy?

So this was the backdrop against which Labour came to power, and one would hope that their primary goal would be to try and correct for the broken economy that they have inherited, and to rebuild the social resilience that has been lost. Labour have inherited a terrible economy, it is not an easy task, there are no simple solutions. So we have to accept we're not going to get transformative changes overnight. But we can say that, if there is no or limited progress over the next 5 years, the repercussions could be very serious – it could certainly play into the hands of the populist right – but it would also raise big questions about Labour's purpose and strategy. So let's look at Labour's strategy.

They have been trying to lower expectations, by repeating a refrain that 'there is no money left', so progress will entirely depend upon growth. The main element of their growth strategy is boosting investment: they've taken steps to boost public investment through the National Wealth Fund, but their proposal is very modest, and linked very much to the private sector. Their aim is to use a bit of public money to persuade the private sector to come in, so success will depend on whether the private sector comes on board or not.

We know the history – e.g. the Private Finance Initiative – which built lots of hospitals and schools, but did so on contracts which completely overpaid the private sector, and we're still paying the price today. So that is quite a questionable strategy. And if we look at predictions of growth, which have already been downgraded by independent forecasters and are likely to be again, then even if you take the most optimistic measure, these estimate a growth in the size of the economy by 7% by the end of Labour's term. That's not going to deliver very much when we're trying to rebuild living

standards and the public sector, *and* it's optimistic. Growth will help, but the effect will be marginal.

Is there a better option than Labour's plan?

The fiscal rules

Firstly, there is much debate about whether the fiscal rules, which are constraining investment, are correct. Labour has adopted very tight fiscal rules, partly as they want to look economically sensible, but also because of fears that the market will increase interest rates. But what's happened is that Germany and the whole of Europe have announced in the last week that they are going to relax their own fiscal rules, which have been very tight over the last 20 years – and they are going for a pretty bold reflationary strategy. And that's putting pressure on Britain to do something similar.

And it's interesting that mainstream economists – e.g. Andy Haldane, who was Chief Economist at the Bank of England until 2 years ago, along with several other mainstream (not left wing) economists, have argued that it is too tight, and we really need to get investment going at a much faster rate. And essentially, the fiscal rules are self-defeating. Very tight fiscal rules play into the bias to contraction that we have at the moment.

Learning from Keynes and the post-war Labour government

The debate about fiscal rules resurrects the work of probably the greatest economist of the 20th century, John Maynard Keynes, who was the architect of the post-war economic order, who would certainly be advocating relaxation of the fiscal rules. Keynes was asked to give a lecture on the BBC in 1942, which was the low-point of the war, in order to build up morale in Britain. He argued that we can afford reconstruction - whatever we can do, we can afford it. What he meant was that if we maximise the resources that we have, then we can do a lot – and that's what happened. The Attlee government inherited a terrible economic situation, hence calling it a fiscal Dunkirk, but they mobilised resources.

The question is – although the circumstances are very different today – there are important lessons we can learn from Keynes about how we can manage our resources more effectively for social good.

Wealth

The first area in which we can do more is wealth. Controversial. The level of wealth has been rising at twice the size of the economy over the past 30 years, it is now worth 6 times the economy, compared with 3 times in 1970. That's a huge surge. Nearly all this wealth has been captured at the top – indeed the share of wealth held by the bottom 50% of the population has fallen since 1970 from 9% to 7%. Most of this wealth is unearned, it's not the product of historic rates of investment and improvements in infrastructure. It's due to other factors, like extraction and asset inflation.

But the problem is that it is barely taxed. We tax this great bundle of wealth – 14 trillion – at an average of only 4% a year, whereas incomes are taxed at 35% a year. It doesn't make any sense. The tax system has failed to catch up with the increasing power of wealth in the economy. But taxing wealth is not just about raising more revenue. When wealth is transferred, it has an

incredibly negative effect on the economy. When it's not being used, it has a passive effect e.g. it is held in property and financial assets, and then when it gets transferred, most of it is spent on things that make the economy worse. The level of this transfer of wealth is due to double in the next 25 years – it's going to explode hugely. So to improve the economy, we need to tax wealth more heavily.

We could be deploying these passive resources into productive use in getting the economy going. Of course there is a big political question of how we persuade people to let us tax their wealth.

Arising out of the issue of this huge hike in wealth is the 'paradox of wealth' which applies to rich countries: the wealthier we get, the less able we are to meet social and individual basic needs – food, affordable housing, social care etc. The reason for the paradox is that the combination of very high inequality and a highly marketised economy leads to resources being redistributed from basic needs to the demands of the rich. And that is precisely what has happened over the last 30 years.

Take the housing market – over the last 15 years – nearly all housing built is at the luxury end. E.g. Thames, central London – 90% has been bought by global rich and left empty. All that land and construction has been wasted from the perspective of abating housing need. Another example - private jets – Britain is the second biggest user of private jets outside the US. It has the highest rate of emission in the whole of Europe.

London is the tax haven capital of the world – there is a huge industry of perhaps as many as 250K people working in tax avoidance, lobbying, PR – to protect the wealth pools of the global rich. The reason this happens – the power transfer that has taken place from the state/labour to big business - means we have lost social control over how resources are distributed.

What is needed

This is long-term, and requires some big shake-ups. And if we're going to use resources more for the common good, we need to fire on 3 cylinders:

- we need a more equal society – this will mean that resources are spent on basic needs
- we need much higher levels of social ownership, so that resources are in the hands of society; and
- we need much tougher regulations over extractive capital, which is at the root of this huge misallocation of resources.

POLLY TOYNBEE

Some responses to Stewart's excellent thoughts.

Chronicling the baseline – documenting what Labour has inherited

Our book, which came out a week after the election is designed to be a 'baseline' for Labour. It is an auditing of what Labour inherited on election day, in every department, so that everyone remembers how hard it was, and the threadbare state public services have been left in..

So when we look in 2 or 3 years time and people say 'what did Labour do for us' we can say e.g. the NHS improved by this much, schools by that much etc - especially early years which a lot of

investment is going into. Our previous book of this kind, 'The Verdict' in 2010, evaluated what Labour had achieved. Not everything was done well, but we wanted to chronicle each of the social programmes. We were both involved in 'New Deal for Communities' for instance, in danger of disappearing altogether, along with other successes – 3500 Sure Starts have disappeared mostly, or are very thin if still there. We wanted to hold on to that and say 'this is what happens if you invest this much, put effort in'. We're still getting data on Sure Start – last month, the IFS which has been monitoring Sure Start's effects, came up with an analysis of the latest GCSE results, and found that those who had been through Sure Start did better. They also found earlier that those children went to hospital much less.

So it is important to hold onto the knowledge that things *do* work – but when the Tories get in, they always throw stuff away. Osborne's first austerity budget in 2010 was a real shocker. It cut through everything, all of doctor and nurse training, so a whole cohort is missing from those years. And we wanted to keep recording this so no-one can ever say 'oh these social programmes never work' as many of them did. And Iraq you might put on the other side of the balance sheet, but it's really about people remembering social programmes.

Labour's plans – upcoming cuts

What we'll get next week in the Spring Statement will be big cuts in public services in the unprotected departments – ie those other than health, education and defence. That means huge cuts in departments already cut to the bone – the Justice Dept is in an appalling situation – and crucially, benefit cuts.

The impact of disability benefit cuts

The cuts to disability benefits are appalling, absolutely dreadful. I did an interview with a woman I'd talked to 13 years ago (at a time when IDS was cutting benefits), who got back in touch. She has 3 severely disabled children. She herself is now in a wheelchair with rheumatoid arthritis, but has been working in the NHS as an administrator. She now has 2 older sons (one aged 20 is at college, and has just learned to cross the road for the first time) – they will lose all their PIP – as won't get it until after age of 22. Youngest one is 16 in wheelchair at school – she thinks she will lose hers, as you have to get 4 points for any one incapacity – she has 13 points in all, but they are in 2's and 3's for different things. It's the detail of how these systems work – and when you look at the details, it seems particularly monstrous. It is estimated that another 100K people will be projected into poverty by these disability benefits, because they are in families with someone with a disability, and that is a terrible thing for Labour to be doing.

Borrowing

I'm a passionate supporter of Labour, and have been waiting 14 long years for them. And I think a lot of the front bench are really good, and are pretty horrified by it too. But somehow they've been persuaded by the Treasury. Rachel Reeves herself is a Keynesian – her book about women economists contains huge praise for the Keynesian economists. But the Treasury has persuaded them as it always does with Chancellors – it frightens the life out of them – it says, look what happened to Liz Truss – it's going to happen to you if you don't watch out. And actually quite a lot of the Guardian economic writers say it might be so, and indeed it might be – our borrowing is 100%, it's costing 100bn a year to pay the interest, so borrowing doesn't look a very good option at the moment. And of course if the Treasury and others go round telling markets 'you're going to freak out' then they will freak out. But it probably is quite risky/scary to borrow more at this stage,

when every country is borrowing more, and gilts are at more of a premium, and goodness knows what's coming down the line in terms of what we'll hear shortly, in a couple of weeks, about exactly what the tariffs will be, and that again will send interest rates up. So it's a scary time to be borrowing more. And I don't think that's the answer at this moment.

Tax

But there is no reason not to tax more, if you could persuade people, if you could say 'look this is a crisis, it's like Keynes in '42, who wrote a book called 'How to pay for the war' – this *is* a war – we need defence – the threat from Russia is very real. Keir Starmer has done immensely well with Europe, around Ukraine – I think he could turn round and say 'defence requires that we all put our hands in our pockets – it does require more tax – and so does the state of the economy – which is worse than we thought and may yet get worse – and so we will ask you all to pay more. And of course the broadest shoulders should bear most, as our tax system mostly does.

But there are an awful lot of things you could do to make sure that happens. Why do the better off get 40% tax relief on their pensions, when ordinary tax payers only get 20%. Why don't people pay NI on unearned income – landlords, shareholders. There are ways of raising money that I think could be quite popular e.g. VAT on private schools is v popular. The Winter Fuel Allowance policy was right in principle, if Reeves had only lifted the threshold a bit – 50% public opinion thought it was right – 'why give me a winter fuel allowance'. There are things you can do, but you have to do them in the right way, it was unfortunate that she didn't make that one change, but it was actually fairly popular – not true that v unpopular.

And other things – Compass, IFS etc have listed – there are some peculiar tax reliefs – a secret welfare state for the better off. There is money there. But it still does mean appealing to the whole population, not just the rich – who need to make some sacrifices – when country is in real trouble, which it is. How do you persuade people.

The impact of the right wing media

We are a very tax phobic country. You can see why cabinet take fright. Outside every cabinet minister's office there is a desk where all the daily newspapers are laid out. They are all shouting at them every day – they're after you're inheritance – Inheritance Tax is hugely hated – people are persuaded they'll lose their homes – whereas only around 5% of estates pay IHT.

80% of our media controlled by *very* right wing media – not European type Christian democrats but very right wing media barons – and the public have been told for many years that tax is a terrible thing. Roy Jenkins: 'tax is the price we pay for civilisation' – most decent people think that – many more people think that than the government fears. But the great cacophony of noise that comes out of the media even when you suggest a small thing like the IHT change for farmers – nobody expected that to blow up – IFS and Resolution foundation have been talking for ages about the injustice of family farms getting this huge bonus on IHT – so the reaction came as a shock.

Making the arguments

Governing is really difficult – we can sit about thinking of what to do – the problem is how to persuade people beyond our bubble. I don't know the answer. It's very important to keep your eye on the enemy – read the Mail and Telegraph. Everything seems to us to be common sense and rational, but we have to find ways of making that argument. Margaret Thatcher used to say 'you

can always spend the pound in your pocket better than the state will' – to which we have to say – what do you value most in life – health, family health, education, safety, security, parks, leisure centres – you can't buy these with the pound in your pocket – you can only buy them with a pound of tax. We're making progress – witness the rebellion against the Tories at last election – around e.g. the state of the NHS – and people would pay more tax for NHS and maybe social care. But a hypothecated tax only takes you so far – only for popular things – the argument has to be bigger than that. Looking at the good cabinet ministers being sent out to defend the disability cuts – it makes you weep – eg. Steven Timms, Torsten Bell. And Rachel herself is definitely a Keynesian. Governing is hard against wall of sound that comes at you all the time.

Q & A SESSION

Q Would Labour bring in a Wealth Tax?

Polly

- Naming the tax is important – so people don't feel their homes are under threat
- Surely a windfall tax of wealth over £10m would be acceptable
- Council tax reform – Buckingham Palace paying the same as a semi in Blackpool – 70% winners, 30% losers but it's the losers that control the media – start modestly then raise
- Add NI to unearned income
- Defence could be a lever to achieve a tax increase
- The Government have chosen benefits to cut, as it's cash straight away – more predictable.

Stewart

- The debate around this is changing – polls by Fairness Foundation – people more receptive when more explanation given
- Spain has introduced a Wealth Tax
- Shame Labour didn't open up debate during election, but worried it would backfire
- Pressure on public finances will force the debate onto the agenda

Q Would a Wealth Tax cause millionaires to leave the country?

Stewart

- Ultimately, an international settlement is needed – under discussion – not much hope for e.g. a minimum Corporation Tax while Trump is around
- Biggest tax havens are British protectorates – could require transparency of business accounts – 2 have done this.
- Wealthy people often live here as they like it – 10K figure has not basis – some might leave, but it probably doesn't matter
- 2% on wealth over 10m – would be 50K for someone with 20m – not that much for them
- Oligarch spending not positive for the economy

Polly

- Problem of Trump threatening tariffs if we try and tax US Big Tech fairly

Q What can we do to change the public attitude to paying tax?

Polly

- Government needs to be better at shaping a narrative
- Rather like Blair/Brown – doing good by stealth – sounding tough
- They should talk up the positives – what we get for our tax, what works.

Q Would it be better to link tax increases to specific spending

Stewart

- Would be good if people had great awareness of good their money does, but also...
- Problem of perception of tax system as unfair e.g. IHT targets medium rich rather than very rich, and bottom 20% payer higher rate of tax than those at the top
- Need restructuring so system becomes more progressive, and eliminates loopholes
- Once have a fairer system, easier to increase the level
- There will be objections, just have to ride that.

Q Would a tax on wealth over 10m raise enough – wouldn't the level need to be brought down, causing people to worry they will be affected?

Stewart

- 2% tax on those with over 10m would raise around 20bn – similar to what raised by increasing employers NI – and wouldn't affect them too much.
- Most of the wealth of the rich is unearned – economic case for some of the increases in wealth to benefit society
- Not just justice and equality – bad economic effects of wealth accumulation.

Q Where is climate action in all of this

Polly

- Optimistic about direction
- Kemi Badenoch unsuccessful in making it a wedge issue – the public care about climate
- Ed Miliband doing good work – energy security appealing across the political spectrum

Q How can we influence Labour and government circles to counteract Treasury orthodoxy?

Stewart

- Treasury is hugely powerful, probably as much as the PM
- Operates according narrow set of principles which mirror the neoliberal agenda – low tax, disciplined spending, weak regulation, power to markets.
- Need to get new values into Treasury e.g. egalitarianism
- May need to split the Treasury – e.g separate Dept for Resource Management – to ensure the country's wealth is spent on good growth.

Q Is Doughnut Economics (Kate Raworth) relevant here

Stewart

- Yes that's part of it
- Need better allocation of available resources – land, labour, capital
- Currently controlled by markets and private corporations
- Large number of resources spent on low value activity
- Poorest 30% have little impact on this.

Q Doesn't this imply a frightening amount of government control over the population

Stewart

- No – as the State wouldn't do this – in a more equal society, the market would deliver more high social value activity.
- Need more social ownership – State now owns only 10% assets compared with 1/3 post war
- Public finances are ruinous due to debt being much higher than value of assets

Polly

- Strong impulse, even among many Tory voters, to bring wrongly nationalised industries back into public ownership, because they are such a disaster.
- Tricky to do it with e.g. 16bn debt on water companies – needs to be done without costing taxpayer more.

Q Why is Brexit not mentioned

Polly

- Debate in Westminster Hall – European Movement involved – not consequential, but good that it's happening
- Shouldn't set about rejoining at the moment – better not to say we're going to tear up Brexit
- But defence likely to be a catalyst for closer ties
- Possibly over time single market and customs union rules will be more flexible
- Different ways of being close likely to evolve.

Q How to change the economy being dominated by a few companies

Stewart

- Over last 20-30 years – merger and takeover boom – concentration of activity among a few giant companies
- Contrary to neo-liberal pro-market agenda – this is anti-market – it distorts and rigs markets
- Competition and Markets Authority has tended to follow Treasury line that shouldn't interfere too much or increase regulation
- Recent development: sacking of previous CEO of the CMA, replacement by former director of Amazon UK – even less rigorous attitude to regulation.

Q How can you get rid of the triple lock in a just way – not needed by all

Polly

- Agrees it needs to go – older people now less likely to be poor than younger
- Multiplier effect
- Instead, should raise Pension Credit, which should have been done alongside winter fuel allowance change
- Politically problematic as all parties have pledged to keep it.

Q Why is Labour being so timid, given the size of its majority

Stewart

- Roots in the election campaign – nerves about perceived ability to manage the economy – didn't make arguments for a bolder approach – now boxed in
- Problematic, as will need to be bolder to make decent progress this parliament

Polly

- Good reason for Labour's fear of markets
- Instinct of city people and head of companies is that Labour not to be trusted
- Conflate their own personal pockets with the good of the economy
- Labour only wins if it's ahead in the polls on managing the economy
- Always go too far in trying to reassure people cf Blair/Brown vowing to stick to Tory spending plans for first 2 years
- But....will lose the next election if spending doesn't increase by then.

Q Will Labour lose its timidity and get more radical in the time its got left?

Polly

Yes – because of commitment to reduce child poverty

Stewart

Not sure. They need to, but don't know if they will. If they do, it will be because circumstances force them to.

Q Can QE be a solution to the problem of funding the public sector

Stewart

Currently doing the opposite – Quantitative Squeezing – Bank of England is selling bonds – adding to pressure towards contraction – they should slow down

QE in the past – problem was that a lot of money went into asset price increases

QE a blunt instrument – monetary policy not the answer – other methods of stimulating the economy are better.