Can't Pay? Won't Pay!

Debt, the Myth of Austerity and the Failure of Green Investment.

Molly Scott Cato

Green House is a think tank founded in 2011. It aims to lead the development of green thinking in the UK.

Politics, they say, is the art of the possible. But the possible is not fixed. What we believe is possible depends on our knowledge and beliefs about the world. Ideas can change the world, and Green House is about challenging the ideas that have created the world we live in now, and offering positive alternatives.

The problems we face are systemic, and so the changes we need to make are complex and interconnected. Many of the critical analyses and policy prescriptions that will be part of the new paradigm are already out there. Our aim is to communicate them more clearly, and more widely.

We will publish a series of reports and briefings on different subjects. We do not intend to have a party line, but rather to stimulate debate and discussion.

Published by Green House 2014 © Green House. Some rights reserved.
Lorton Barn, Lorton Lane, Weymouth, Dorset DT3 5QH, United Kingdom.
+44 (0)1305 816514
info@greenhousethinktank.org
http://www.greenhousethinktank.org

You can download this publication from
http://www.greenhousethinktank.org/page.php?pageid=publications

ISBN 978-0-9573738-6-0
Print copies of this publication may be bought online from http://www.lulu.com/.

Existing Green House Publications (See next page for the Post-Growth Project)

'Sustainability Citizenship' by Andrew Dobson.

'Mutual Security in a Sustainable Economy: a Green Approach to Welfare' by Molly Scott Cato and Brian Heatley.

'The Dog That Didn't Bark: When banking crises did not occur and what we can learn from that' by Thomas Lines.

'Guardians for Future Generations' by Rupert Read.

'Free Universities: Re-configuring the Finance and Governance Models of the UK Higher Education Sector' by Molly Scott Cato.

'Offsetting Nature? Habitat Banking and Biodiversity Offsets in the English Land Use Planning System' by Mike Hannis and Sian Sullivan.

'Strangled by the Duopoly: The collapse of UK Democracy, 1975-2012, and some proposals for its revival' by John Hare and Rupert Read.

'Local Liquidity: From Ineffective Demand to Community Currencies' by Molly Scott Cato.

'Primary Commodity Prices and Global Food Security: Why farmers still struggle when food prices rise' by Thomas Lines.

'Greens and Science: Why the Green Movement is not anti-Science' by Anne Chapman.

All existing Green House publications can be downloaded free of charge from our website at http://www.greenhousethinktank.org.

Green House Post-growth Project

Everyone agrees that we are in the midst of a massive financial and economic crisis. We have suffered the biggest crash since the 30s, and it may get far bigger yet. How ought this ongoing crisis to be understood, and resolved?

There is the mainstream view: we have vast government deficits, and stagnant economies. We have a dire need for economic growth – and a deep-set need for austerity, bringing with it massive cuts in public services.

But what if that diagnosis, which reflects mainstream wisdom, is all wrong? What if the crisis that we are currently experiencing is one which casts into doubt the entire edifice of capitalist economics that sets growth as the primary objective of all policy? What if the fight between those who say that without austerity first there can be no growth and those who say that we must invest and borrow more now in order to resume growth is a false dichotomy – because both sides are assuming 'growthism' as an unquestioned dogma?

The aim of the Green House Post-growth Project is to challenge the common sense that assumes that it is 'bad news' when the economy doesn't grow and to analyse what it is about the structure of our economic system that means growth must always be prioritised. We need to set out an attractive, attainable vision of what our country would look like, once we deliberately gave up growth-mania – and of how to get there. And we need to find ways of communicating this to people that make sense, and that motivate change.

Existing Green House Post-growth Project Reports

'Green House's 'Post-growth' Project: an introduction' by Rupert Read.

'Joined up Economics: The Political Economy of Sustainability, Financial Crises, Wages, Equality and Welfare' by Brian Heatley.

'Smaller but Better? Post-growth Public Services' by Andrew Pearmain and Brian Heatley.

'The Paradox of Green Keynesianism' by Molly Scott Cato.

'Can't Pay? Won't Pay! Debt, the Myth of Austerity and the Failure of Green Investment.' by Molly Scott Cato.

Forthcoming Green House Post-Growth Project Reports

'Industrial policy and infrastructure – the depth of the challenge of a green transition' by Jonathan Essex.

'Post-Growth Politics' by Andrew Dobson.

'A new Post-growthist Common Sense: Challenging the Hegemony of Growthist Discourse' by Rupert Read.

Table of Contents

The author

Molly Scott Cato is a green economist and expert in the social economy who specialises in the issues of trade, work, money and cooperatives. She is Professor of Strategy and Sustainability at the University of Roehampton and has a PhD in economics from the University of Wales, Aberystwyth. Molly studied Politics, Philosophy and Economics at Oxford University.

Acknowledgments

I would like to acknowledge the courage and dedication of those people across Europe who are struggling to maintain civilized societies devoted to social justice and humanity in the face of an unprecedented assault. In particular I would like to thank the following for their insights into the campaigns that are taking place across Europe: Christina Laskaridis, Fathi Aloui, Noha el Shoki, Iolanda Fresnillo, Marie Moran, Mark Malone and Joao Camargo.

The author is also grateful to other members of Green House for their comments on an earlier draft of this report.

Summary

This paper presents a liberating idea: the idea that we are not burdened down with unpayable debts that presage a decade of low growth, hard work and a miserable existence. Rather we live in a rich and vibrant society but one which is disfigured by an exploitative and iniquitous financial system.

The central thrust of this paper is that, as a society, we need to face our debts head on and make an intelligent political decision about what to do about them.

The decision to prioritise the repayment of debts no matter what the cost to public services is a political rather than an economic decision. It is thus not only valid but necessary to challenge the false consensus around the politics of austerity.

The present debate is also misinformed since, in reality, we are not repaying our debts but are sinking further into historically high levels of debt that we have little prospect of repaying.

A parallel political decision is that public investment should be made through money borrowed; although the decision to run a perpetual national debt is an old one, dating back more than 300 years, it is not an inevitable one. At a time of national crisis it is worthwhile to reopen this question.

Paying for vital national investment through a national debt operates as a means of transferring wealth from working people who pay taxes to those who live from investment earnings and therefore perpetuates social injustice.

A debt-based economic policy creates an in-built pressure on the planet and its resources and so the system of paying for future consumption through the issue of public debt is a central cause of exponential economic growth and the environmental destruction it brings with it.

The period of austerity we are living through also prevents the investment in the infrastructure to support a sustainable economy that is urgently necessary.

To achieve a participatory and engaged debate about these issues the paper proposes the establishment of a Citizens' Audit which will seek to explore the size of our debt, who it is owed to, the consequences of repaying it, and alternatives to repayment.

As in Latin America, the debt Audit will be focused around the concept of odious debt: when citizens are not clear that they are acquiring responsibility for debts then they cannot be held responsible for them.

Debt: We Are All in It Separately

This paper presents a liberating idea: the idea that we are not burdened down with unpayable debts that presage a decade of low growth, hard work and a miserable existence. Rather we live in a rich and vibrant society but one which is disfigured by an exploitative and iniquitous financial system. This paper is part of Green House's Post Growth series, and so it explores the relationship between the funding of public investment through debt and the pressure for economic growth. Counter-intuitively, it is argued that it is not public investment itself that creates the pressure for damaging economic growth but the funding of such investment through debt-based finance. Recovering from the debt addiction is argued to be an essential step on the path to recovery from the growth addiction.

I take my cue from Shelley, who in 1820 argued that,

'The settlement of the national debt is on the principles before lucidated merely an arrangement of form, and however necessary and important is an affair of mere arithmetical proportions readily determined; nor can I see how those who, being deprived of their unjust advantages, will probably inwardly murmur, can oppose one word of open expostulation to a measure of such irrefragable justice.'[1]

Of course things have changed a bit since Shelley's day, but what has not changed is the reality that the economy is structured to serve the interests of a tiny minority. The liberating idea underlying this paper is that, if we live in democratic societies, we should not have to repay debts that were acquired in murky circumstances and without our full consent. Such debt, defined by legal writers as 'odious debt' should be repudiated. And liberating ourselves from these debts and from a policy of funding public investment through debt, will empower us to undertake the green transition that we urgently need to embark on.

The period of austerity we are living through is quite distinct from the austerity of the 1950s. Then, following a period of total war, our economy was literally exhausted and our material infrastructure devastated. The hard work of our grandparents' generation literally rebuilt the country. By contrast what we are experiencing today is a constructed politics of austerity, which justifies the sell-off of our remaining public assets and massive cuts to public investment. Given the urgent need to undertake a transition to a sustainable economy with green infrastructure this is an ecological as well as a social crime.

This report forms part of the Green House series on thinking beyond growth, so I need to explain at the outset how it fits into the wider picture. The need to return rapidly to economic growth is the dominant political message of our times and its rejection provides the rationale for the Post-Growth Project. The vast levels of public and private debt obviously make growth harder to achieve, since money is more likely to be spent paying down debts than investing in productive activity. So perhaps greens should celebrate the debt and the incapacitating austerity it brings with it? The problem is that the age of austerity is not an age of low consumption. Assets are being transferred and the wealthy and powerful are more capable of protecting the value of their assets than the majority who rely on savings or pensions.

The continuing payment of bonuses to financiers is infuriating from the standpoint of equity, but it also constitutes a threat to sustainability because the lifestyles of the wealthy are more environmentally destructive than those lower down the income scale. The Joseph Rowntree Foundation has supported research into the social impacts of policies to address climate change that indicates that those in higher socio-economic groups are responsible for more CO2 emissions. Using a dataset comprising 24,207 private households drawn from the Expenditure and Food Survey (EFS) for the period 2004–2007, with additional data imputed from the English House Condition Survey, the Annual Passenger Survey, and the National Travel Survey, the researchers analysed CO2 emissions by income decile. The most striking finding of this preliminary report is that: 'Mean average CO2 emissions are strongly correlated with income: households within the highest equivalised income decile have mean total CO2 emissions more than twice that of households within the lowest equivalised income decile. Emissions from private road travel and aviation account for a high proportion of this differential: aviation emissions of the highest income decile are more than six times that of the lowest income decile.'[2]

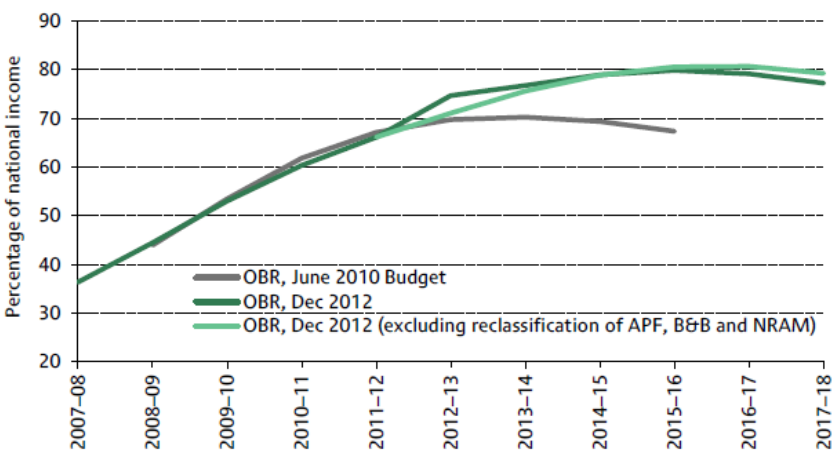
The final link between debt, growth and sustainability relates to the desperately urgent need to shift our economy towards a design that generates well-being with much lower levels of throughput of materials and energy. To some extent this requires a cultural shift, a rethinking of what we mean by well-being (I cover this in the companion report on 'The Paradox of Green Keynesianism' and it also forms a central theme of Green House's earlier paper on Green Welfare), but it also requires investment in the hardware of a green economy, whether this means renewable energy facilities or the less glamorous insulation of our millions of sub-standard homes. In spite of the repeated arguments of Greens, who have now been joined by David King (former Chief Scientific Adviser to the government)[3], money that is created directly by the Bank of England through the quantitative easing programme is not spent on green infrastructure but given to banks who either throw it into the black hole on their balance-sheets or pay it to their executives to fund their high-impact lifestyles. While the obvious route out of our environmental and financial difficulties would be to invest massively in green technologies and in the infrastructure to facilitate green lifestyles this cannot happen while finance is powerful enough to divert all money in its direction.

What's Debt Got to do with It?

The central thrust of this paper is that we need as a society to face our debts head on and make an intelligent political decision what to do about them. The constructed politics of austerity prevent us doing that, while also achieving important political advances for those who control financial assets and whose political project is aimed at the destruction of the public and the idealization of the private. So here I am addressing myself primarily to the public debt which is used as a justification for cuts in public spending that are damaging the economy and preventing us investing in the green transition we urgently need to undertake. Before we reach the meat of the paper I need to briefly address three important issues that are worth noting, but cannot be covered in full here. First we need to consider the entirety of debt with which the UK struggles and be clear about how much of it might be included in a debt audit.

The first point we need to get clear is that the statements about paying down our debts are at best misleading and at worst down-right deceptive. According to the Institute for Fiscal Studies the Chancellor has missed his targets for debt reductions—for which we have all been suffering—and the Treasury's forecast for net public-sector debt is that it will rise by 0.9% of national income in 2015-16 (to 79.9%). Stripping out the impact of various reclassifications of government financial liabilities made at an opportune time would show debt rising even faster to 80.6% of national income. Figure 4.3 from the same report shows that our deficit—the amount we borrowed in excess of what we earned in 2012—was the fourth highest in Europe at 6.2%, out-stripped only by Ireland, Spain and Greece. We also have ongoing liabilities for debts acquired under public-private partnerships (PPPs), that tend not to feature in official calculations of public debt.[4]

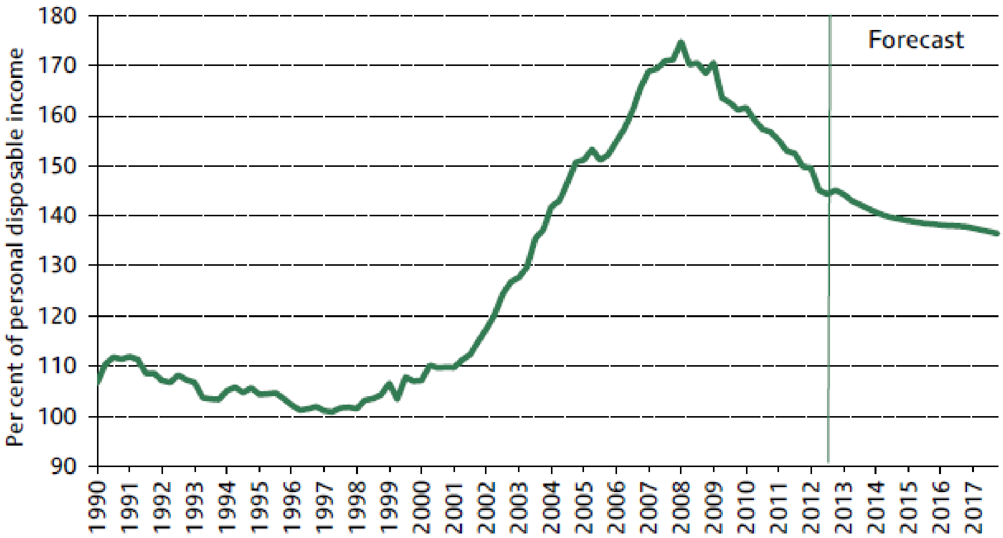
Figure 4.2. Debt not currently forecast to fall in 2015–16



Note: Figures for debt excluding the reclassification of the Asset Purchase Facility (APF), Bradford & Bingley (B&B) and Northern Rock Asset Management (NRAM) are authors' calculations using figures produced by the OBR.

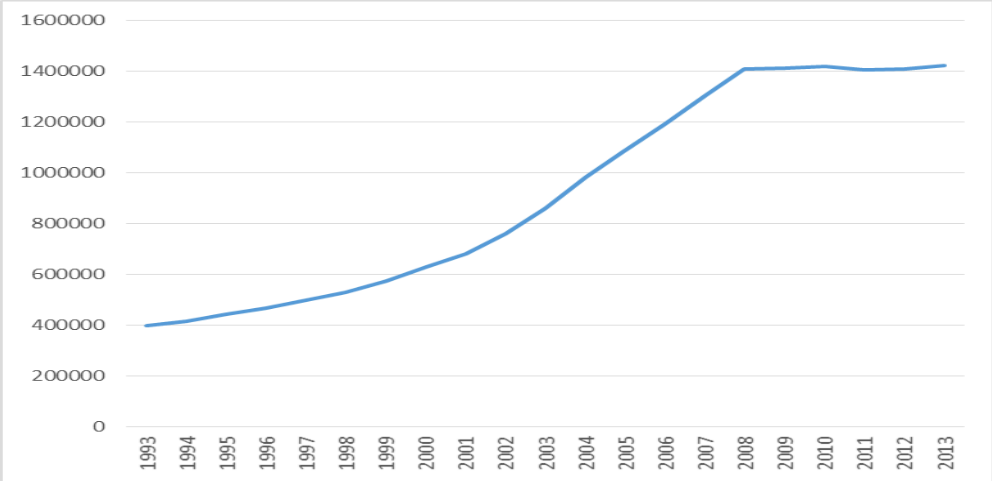
The second figure illustrates the debts for which UK citizens are responsible as individuals and households, where we see that household debts are enormous as a proportion of disposable income but are gradually being reduced from their 2008 peak. The big volumes here are comprised of private debts, acquired through mortgages taken out on over-priced homes, credit-card spending (which, as is argued in Heatley's paper, were acquired under political pressure in order to prevent the economy from imploding earlier than it did), and other forms of bank and private loans. All these categories of debt are part if the explanation for the stalling of UK economic activity, and an argument could be made that the debts were acquired from political-economic necessity rather than as a result of fecklessness of greed, at least on the part of citizens. Although this ‘personal’ debt represents a huge political and economic risk for the UK, in this paper I am concentrating on the public debt: the debt that is our responsibility as citizens because it results from IOUs issued on our behalf in the form of Treasury gilts.

Figure 2.21. Household debt-to-income ratio



In spite of the recent moral panic over ‘record levels’ of personal debt, sparked somewhat bizarrely by Iain Duncan Smith’s thinktank the Centre for Social Justice,[5] the graphic below based on the Bank of England’s data makes it clear that the historically high levels of debt were acquired during the boom and that since the bust households have been doing their best, as the previous graphic illustrates, to pay down their debts. In a sense this graphic reflects a similar picture for personal debts that we are experiencing for public debts, making stronger the claim that, if borrowing is a civic duty, personal debt cannot be considered entirely private.

Figure 1. Sterling net lending to individuals and housing associations, 1993-2013 (£m)



Note: Total monthly amounts outstanding (excluding student loans), seasonally adjusted, data given for April.
Source: Bank of England statistical database, Table LPMBZ2A.

Were We Ever Living Within Our Means?

As the quotation from Shelley makes clear, the existence of a vast public debt is not new. The UK's debt can trace its lineage back to the creation of the Bank of England in 1694, which was the other side of the coin of the creation of the national debt, originally called a 'fund for perpetual interest', rather like a perpetual motion machine. Initially the Bank was established privately by Scottish entrepreneur William Paterson who persuaded the government to raise £1,200,000 by selling the national debt to citizens who would redeem their share with interest in a fixed number of years. The scheme was accepted in 1694 and from then until the following year Paterson served as a director, when he fell out with the other members of the Court (or board) and was sacked. Paterson was an entrepreneur and the Bank of England was merely one of his many schemes to create money from thin air. He is probably most famous for the subsequent disastrous Darien project. In 1693 he set up the Company of Scotland Trading to Africa and the Indies, which sold shares of a proposed colony on Darien on the Panama isthmus. The Scots were keen to see their own advantage from expanding international trade and so there was no shortage of investors: about half a million, half Scotland's national capital, was invested.

Where there is a bank there must be a debt. The glory of the Glorious Revolution was the acquisition by Britain from the Dutch of the magical process of fractional reserve banking.[6] The inability of the French to create the money they needed to fight the wars that disfigured Europe through the 18th century left them with no alternative but to impose punitive taxes, leading to economic suffocation and eventually revolution. The rest really is history: a history of beleaguered citizens knuckling down to a generation of austerity in Britain and French politicians supporting their citizens against the depredations of financially generated depression. The contrasting policies of Cameron and Hollande today are in a direct lineage from the adoption of private finance in Britain more than 300 years ago.

Paying for vital national investment through a national debt operates as a means of transferring wealth from working people who pay taxes to those who live from investment earnings. But the environmental consequences are even more serious. A debt-based economic policy creates an in-built pressure on the planet and its resources. When the government creates money through issuing bonds it creates a parallel future demand for goods and services—goods and services which can only be produced by using energy and resources. So the system of paying for future consumption by public debt, just like the system of creating money as private debt, is a central cause of exponential economic growth and the environmental destruction it brings with it. Building up an ecological debt is far more serious than a mere balance-sheet debt: this is why we might choose as our slogan: 'Drop the debt, or the planet gets it'.

Although the relationship is not inevitable, capitalist states tend to fund themselves through the use of private, debt-based finance. The charging of interest and the creation of new debts that multiply the volume of money many times over means that there will always be a pressure to create new debts and a limited ability to repay existing ones. In such an unstable situation the risk of default is so prevalent that Andrew Haldane, of the Bank of England, and Mark Kruger, of the Bank of Canada, argue[7] that 'default is a natural feature of the market mechanism'. Even if the value of the debts/credits created were always unrealistic in terms of the capacity of the debtor to repay, when the deal collapses the creditor is always motivated to protect as much as possible of his asset. With national debt default this becomes a political process.

A detailed case-study of default is provided by Argentina, whose default in 2004/5 has been subjected to rigorous academic analysis. Argentina's problem began through its close association with the dollar, to which the Argentinian peso was pegged in 1991. Following years of economic crisis and the off-shoring of the majority of country's reserves, in 2001 the financial system collapsed. By this stage the government could pay neither its own employees nor its foreign creditors; there was so little currency in circulation that a range of novel currencies and payment mechanisms were in use, as well as widespread use of barter.[8] What followed was the largest sovereign debt default thus far known: the government had half a million creditors to whom it owed a total of $81bn.[9] After lengthy and complex negotiations the majority of the creditors settled for new bonds to the value of only 35% of their existing holdings.[10] By March 1st 2002 President Néstor Kirchner could claim that the restructuring had been a triumph, and that 70-75% of bondholders had accepted it.[11] It is worth noting that losses were suffered by off-shore bond-holders as well as domestic ones: almost 40% of the defaulted debt was held by Argentinians, compared with 60% held offshore.[12] Details of the Argentinean debt are given in Table 1.

Table 1. Value of Argentina's Public Debt before and after the 2003 Default

	December 2003[a]	After the swap[b]
Bonds eligible for the swap	104.1	36.2
BODENs[c]	18.5	19.4
Provincial guaranteed bonds	9.7	10.5
IMF loans	15.5	13.8
Other multilateral loans	16.7	15.1
Guaranteed loans	14.1	15.0
Short-term debt	2.5	3.2
Total debts	188.6	120.8
Hold-outs		20.8

[a]Corrected for the effect of transfer into pesos. [b]Assuming 80% participation
[c]Bonds compensating banks for the effect of transfer into pesos.
Source: Economist (2005),[13] based on data from the Argentine Ministry of Economy.

The default was not the end of the Argentine economy. Although it was frozen out of the credit market for around a decade the removal of the dollar-peg straitjacket, combined with rising commodity prices, enabled Argentina to flourish economically in the first decade of the 21st century. Kruger and Haldane argue against such an outcome on the basis of moral hazard on both sides: it 'applies to both debtors (by blunting incentives to' undertake the necessary adjustment and reform) and creditors (by blunting incentives to undertake effective risk management).'[14] Their proposal is rather for a 'standstill', a national drawing of breath while the political, rhetorical, and financial tools can be put in place to ensure that interest payments continue to be made:

'The importance of 'standstills', the decision to invoke which lies with the debtor. The advantages are: 'prevent creditor co-ordination' they can 'break the circuit of destabilizing and, ultimately, self-fulfilling creditor expectations'. They can help to 'align creditor and debt incentives'. Thirdly they can allow a breathing-space to introduce macroeconomic policy adjustment.'[15]

Debts can be extended, transferred to different holders, and interest rates changed, to enable money to continue to flow from debtor to creditor.

In the case of eight recent defaults—those of Russia (1998-2000), Ukraine (1998-2000), Pakistan (1999), Ecuador (1999-2000), Argentina (2001-5), Uruguay (2003), Moldova (2002), and the Dominican Republic (2005)—the sharing of the losses between debtor and creditor seems to relate more to the political power of the debtor than the position in international commercial law. Hence Argentina and Russia were able to negotiate a loss for their creditors or around 75% and 50% respectively, while in the case of the Dominican Republic a rescheduling meant that the debt would eventually be repaid in full. In all cases cited, the countries saw a return to a positive inflow of private capital within five years, suggesting that any deterrent effect to a default based on fear of loss of investment is not well grounded. Costs of non-domestic finance also appear to return to their pre-default levels within two years. The authors conclude that the major cost associated with sovereign default is economic and social dislocation, rather than exclusion from future borrowing.

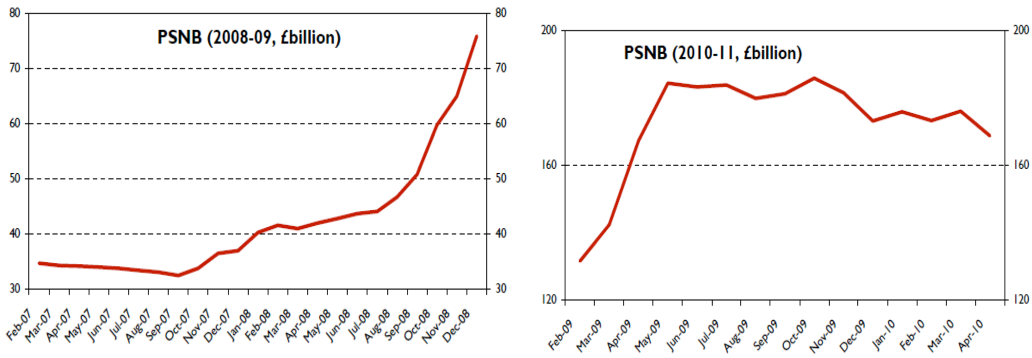
Learning from Latin American Debt Crises

The narrative around the sovereign debts of Western nations has followed the interests of the financial class, leading Simon Johnson to suggest that we have been the victims of a 'quiet coup'.[16] In rejecting this narrative I find support in theoretical and practical developments from Latin America. It may seem surprising at first that we have something to learn about debt from the countries of Latin America: after all were they not the very countries who went spectacularly bust one after another towards the end of the last century. That is really the point, because some of the more creative thinkers and politicians on that continent began to ask themselves why countries like theirs, so well-endowed with resources, should not be able to manage their economies so as to achieve prosperity for their people. Their economists, such Eduardo Galeano and Oscar Ugarteche, theorised that the neo-colonial exploitation of countries of Latin America has been effectively achieved through the use of financial mechanisms, leading to a history of repeated debt crises. This region was particularly vulnerable because of finding itself in the backyard of the dollar, and because of the willingness of its politicians to follow monetary regimes that linked their currencies to that of their powerful neighbour. It is difficult to read the history of monetary policy in South America except as a choreographed exercise in using successive processes of debt acquisition, interest payment, and restructuring as a subtle means of expropriating the region's resources at very low prices. In an ideological move that can speak to the present situation in Europe, Ugarteche concludes that 'A common sense was created that Latin Americans had lived beyond their means. Austerity was the solution and that meant reducing the wage bill.'[17]

In this section I address the issue of sovereign debt in the context of our own democracy: the United Kingdom. This is peculiarly appropriate, since one of the things that we have learned from the financial crisis is that the rootless nature of capitalism was always more apparent than real, and that when there are losses to be paid, the geographical and political location of the companies that owe become very relevant indeed. This is a lesson of special importance to us in the UK, which has long been at the heart of the global financial system that facilitated the movement of the global economy into a morass of debt. This gives the issue a particular importance, due to the national dependence on financial services as a source of fiscal revenue and foreign-exchange earnings. In this section I use the UK to illustrate how a Citizen's Audit might work and the sorts of questions it might ask.

To make progress in addressing our mountain of public debt we need to begin by anatomizing our national debt as it currently stands. This is a highly political question and attempts to answer it have been obfuscated by the politicisation of the discussion: we need to ask how much of the current public debt was caused by reckless public spending, and how much was the result of the acquisition of debt without proper understanding by, or accountability to, the citizenry. The two graphics below indicate the rates of public borrowing for the periods February 2007-December 2008 and February 2009-April 2010 and are highly suggestive of an answer to this question. We can see the rate of public borrowing begin to rise massively from autumn 2008, when the financial crisis began to hit. By February 2009 we are on a completely different axis. So the financial crisis had an impact on our public-spending but the causation is not simple or direct. The intervening variables include a fall in tax revenues, higher rates of welfare spending, as well as a contraction in the size of the economy.

Graphical Representation of UK Public Sector Net Borrowing, December 2008 and April 2010 compared



Source: Public Sector Finances of the Office for National Statistics website: http://www.ons.gov.uk/ons/taxonomy/index.html?nscl=Public+Sector+Finance

Because money is not a fixed commodity but one whose value fluctuates wildly depending on levels of confidence estimates for the cost to the UK of the banking sector in recent years also vary considerably. According to the *Guardian*'s fact-check team, estimates vary between £1.162trn and £456bn.[18] Some useful work in forensically examining UK debt has been undertaken by the London-based New Economics Foundation. They reach some fairly stark conclusions:

- 'Public sector support for the banking sector amounts to at least £1.2 trillion committed, equivalent to 85 per cent of GDP – the highest level of any comparable economy
- In order to maintain existing levels of activity they [the government] currently have to borrow £12 billion a month; the projections we reproduce in this report indicate that in 2011 they will have to borrow £25 billion a month.'[19]

They remind readers that this monthly total is equivalent to half the current expenditure on education or a quarter of the expenditure on health services. So, point one is that the debts we have taken on were the result of an emergency need to keep the financial system functioning. They were not the result of loose spending by a Labour government.

At present, the decision to focus on austerity means that millions are losing out through falling living standards, reduced public services, and unemployment. If we took the alternative course of repudiating some of our debts who would be the losers?

Table 2 reproduces some figures from the UK Debt Management Office. These indicate that around a third of our national debt is in the hands of foreign creditors, but that a larger share is owned domestically, allowing us to engage in political negotiations between interest groups. The data shown in the graphic indicate that only 29 per cent of the gilts currently in circulation are held by overseas investors, with slightly more (30%) being held by UK insurance companies and pension funds. The nature of ownership of government debt is an aspect of the sovereign debt crisis that has not been widely discussed: we might wish to debate the relative merit of claims made by global financiers and rentiers to the national wealth of our economies, compared with our own citizens. In the case of bonds held domestically a different kind of negotiation might be possible: downgrading bondholdings according to a taper, perhaps, so that the wealthiest lose the largest share of their holding. In the case of institutional bond-holders, such as pension funds, a political process might weigh losses to these funds against parallel losses or gains to vital public services. Pensioners and future pensioners might be defending their financial interests now to the detriment of the social and health services they will come to depend on in five or ten years' time.

Table 2. Distribution of UK Gilt Holdings at 30 September 2011, £m (based on market values)

	Q2 2007	%	Q2 2013	%
Insurance companies and pension funds	228,619	50.1	342,226	30.5
Overseas	144,424	31.6	414,267	25.2
Bank of England (Asset Purchase Facility)	0	0	378,293	27.9
Monetary Financial Institutions[a]	-11,231*	n/a	113,576	8.4
Other financial institutions	68,377	15.0	99,932	7.4
Households	13,804	3.0	6,775	0.5
Building societies	1,101	0.2		
Local authorities and public corporations	664	0.1	1,933	0.1
Total	445,758		1,357,002	

*This is a 'repo' or repurchase position, meaning that the DMO was involved in a forward purchase deal with banks; in later tables 'banks' are referred to as 'other financial institutions'.
Source: UK Debt Management Office (2011), *Quarterly Review*, October-December; available on the DMO website.

The entirely novel policy of quantitative easing (QE) adopted as a mark of real desperation in March 2009 has led to the strange anomaly that just over a quarter of our public debt is actually owed to ourselves. This is distinct from the money we owe ourselves indirectly in our roles as pensioners or investment holders (which has declined from 50% to 30% following the crisis). This is money whose owner is titled 'Bank of England Asset Purchase Facility' and that sits unattended in the accounts while the politics of austerity rage on. This raises two questions: why have we decided to promise to pay ourselves back indefinitely rather than cancel our debts to ourselves; and, if the Bank of England can create enough money to buy back a third of our national debt, why doesn't it just go to town and buy back the rest as well? There may be answers to these questions but my hunch is that they are political rather than economic.

This brings me to the third point in my argument: are there proposals we could come up with for restructuring the debt so that we find ways of avoiding the destruction of the institutions of a civilised society we most value? It is this question that provides the rationale for a process known as ‘debt audit’ that has been undertaken by a number of Latin American societies. In a democracy decisions about who gains and who loses in situations of crisis should be open to public debate, and yet the obfuscation and complexity of financial arrangements have made this impossible, and have left citizens accepting the simplistic and frequently dishonest spin that ‘we are all in this together’ and that we have been ‘living beyond our means’. So the critical question is who would lose out if we acknowledged that repayment of a debt on this scale is inconsistent with living in a civilised society, and began a policy of negotiating with creditors that they would not see the whole of their lending repaid? This question drives the audit process, since the pressures to prevent a country from defaulting depends on the motives and relative power of those who will gain or lose:

‘It is worth recalling that in a restructuring procedure, the different creditors do not have the same objectives. A retail bondholder does not aim to have the same exchange offer as that of an investment bank or a vulture fund. On the one hand, we might be talking about the lifetime savings of a senior citizen, while on the other hand, it might be someone that makes a business by investing in distressed debt on a regular basis.’[20]

The most significant purpose of the audit would be to enable us to find answers to this question but we can begin to sketch some answers. For those who have investments in pension funds, they may see their pensions reduced but the public services they also mainly benefit from will be protected, so it will be a trade-off, but one that is fairer because those with larger savings will lose more, in contrast to the spending cuts that hit the poorest hardest. The overseas and other financial institutions would also lose out but this could be seen as compensation for the massive investment bubble they benefited from, and gained from, and which caused the banking and credit crisis that landed us all in this mess. These are just preliminary suggestions: it would be precisely this open and transparent discussion of how the value and the losses should be shared that the Audit

Commission would be established to lead.

Hoist by their Own Odious Petard

The idea of establishing a national audit committee comes from Ecuador, where President Correa was elected in 2005 to preside over an economy which was oil-rich but whose wealth was being drained and whose people were left in poverty because 50% of national income was being spent on servicing foreign debt. In July 2007 he established a Debt Audit Commission to explore whether these debts had been acquired legitimately. The Commission reported in November 2008 and found that a series of Ecuadorian bonds were unlawful, and recommended that Ecuador should refuse to make payments on them. President Correa responded by repudiating this debt on the basis that it was 'improperly authorised by previous administrations and involved onerous interest rates, commissions and prepayments'. By the following April Ecuador had successfully renegotiated the bonds, reducing their value by 65%.[21]

The discussion around which spending citizens should rightful be held responsible for is focused around the appealing concept of 'odious debt', which dates back to the 19th-century, when the US wished to avoid responsibility for the debt of the states it had absorbed into its territory as a result of the Spanish-American War, specifically, the debt that Cuba had incurred under its colonial rules. It holds that:

'debt should not be transferable to successor regimes if (a) it was incurred without the consent of the people and (b) was not for their benefit (Alexander N. Sack, 1927; Ernst Feilchenfeld, 1931). The underlying principle is that just as an individual does not have to repay money that someone fraudulently borrows in her name, and a corporation is not liable for contracts that its chief executive officer enters into without authority to bind the firm, a country should not be responsible for debt that was incurred without the people's consent and was not used for their benefit.'[22]

An idea which was developed for a single pragmatic requirement and had gathered dust in legal libraries came back to public attention in 2003, when the US Treasury Secretary used it as justification for repudiating the debts incurred by Saddam Hussein when it took over Iraqi territory. It derives from a strong moral sense that those responsible for acquiring debts should not be able to force this responsibility onto others who have neither consented to nor benefited from them:

'It is morally repugnant to saddle the population of a country, down unto generations yet unborn, with the obligation to repay debts that are truly odious in the Sackian sense. Most people instinctively believe that the consequences of reprehensible acts should be visited exclusively on the malefactors (in this case, the corrupt regime and its complaisant creditors). The question is whether this moral imperative can be translated into a workable legal theory.'[23]

The concept of 'odious debt' has been related to debt acquired by regimes that have been regarded as illegitimate in international law either because they were oppressive, or undemocratic, or because a change in state regime rather than just government had taken place, in the case of Cuba and Iraq due to external invasion. But might we extend this concept to stable western democracies, whose citizens are now struggling with oppressive debts? Recalling Sack's two conditions—that the debt was incurred without the consent of the people and was not for their benefit—can we apply these conditions to our own situation in the UK?

This is not the place to enter into a philosophical or legal discussion of consent, but such a route might be fruitfully followed in an area where ignorance on the part of the citizenry was so widespread. A clear finding of the various popular books that have emerged in the wake of the financial crisis is the opacity surrounding the behaviour of financial institutions and their employees, which left many key policy-makers and politicians, not to mention the citizens who trusted them to regulate the sector, ignorant of the 'dark arts'.[24] The role of the public in supporting the banks that are headquartered on their soil was not well understood,[25] suggesting that meaningful consent to the financial costs of this can be questioned.

Whether or not it was for the benefit of UK citizens is perhaps more problematic. In a situation where the Chancellor of the Exchequer publicly stated that we were within hours of the cash-point machines failing, there was clearly a strong public need to support the monetary system, which required nationalising the banks at vast public expense.[26] But UK citizens were unfortunate that some of the world's largest banks were headquartered on their territory, and this led to their supporting a banking system for the general global good at their personal national expense. Whether the tax receipts during the boom justified the cost of the bust to the UK balance-sheet is one question that a Citizens Audit could seek to answer. Despite the repeated trumpeting of the contribution financial services makes to the Exchequer, government data demonstrates that it pays less in corporation tax than utilities and business services and considerably less than North Sea oil companies.[27] In 2012/13 the financial services sector paid slightly less than £5bn in corporation tax while the manufacturing sector, which it is starving of cash, contributed just under £5bn. The banking levy contributed an additional £1.5bn in that year.[28]

Following a series of debt crises and defaults during the 1990s, the IMF attempted to create a 'sovereign debt restructuring mechanism' which, while unsuccessful, did lead to changes in the legal position surrounding default, enabling creditors to protect their interests via 'collective action clauses'.[29] However, as Panizza et al. point out, national governments are in a much stronger legal position than corporations since they have legal protection of their assets even if located on foreign territory, and because 'a sovereign cannot credibly commit to hand over assets within its borders in the event of a default',[30] a point whose validity appears to have been undermined by the use of default as a pretext for instituting large-scale privatisation of public assets in Greece and Italy as a sequel to the Eurozone crisis. However, they make clear that this protection from pursuit by private creditors has declined over time in US law, so that 'sovereign immunity no longer plays an important role in shielding sovereign debtors from creditor suits'.[31] If owed money by a sovereign, creditors have to make a decision about whether they are likely to gain more via expensive litigation than via a rescheduling agreement, meaning that over time nation-states are coming to have similar legal standing to that of corporations. However, given the difficulty of enforcement, a sovereign's willingness to impose a default seems to be a function of political will, rather than legal restraint, as the example of Argentina demonstrates.

The concept of 'odious debt' has been linked to discussions of the morality of debt forgiveness in the case of highly indebted countries: 'Most people instinctively believe that the consequences of reprehensible acts should be visited exclusively on the malefactors'.[32] Citizens of European democracies that now see the IMF austerity programmes visited on them might ask whether a similar moral suasion might be used in their defence. In the case of highly indebted poorer countries of the majority world, the discussion around the morality of debts has been extended into a discussion around the need for a debt 'jubilee',[33] and this may be a route that the countries of Western Europe could choose to follow.

The reason the focus of this paper is on government debt is that it is there that the argument about the debt being odious can be most clearly made: the relationship between an implicit guarantee to the banking sector that most citizens were unaware of but are now paying for is clear. But what about the less direct ways in which we have been inveigled into paying off long-term and expensive debts via the PPP arrangements that have funded so many schools and hospitals? Might they also be considered odious debts? Especially in a situation where, following an investigation into the deals made, the Public Accounts Committee concluded that 'The rewards to investors and managers of the funds appear to us to mean that the private sector was receiving excessive profits on the back of Government funded projects at the expense of the taxpayer.'[34]

And, as we saw in the earlier graphic on page 7, and has become the subject of media discussion recently,[35] it is the very high levels of individual debt that are likely to become the most urgent and problematic once interest rates begin to rise. If citizens were encouraged to take on debts for the sake of maintaining aggregate demand in the economy (see my earlier report in this series 'The Paradox of Green Keynesianism' for an explanation of how this was done), then to what extent is that a personal rather than a political responsibility?

It may be unsatisfying to read a report that raises so many questions that it cannot answer, but that is really my purpose here. I am seeking to raise the questions that lie behind the false consensus of austerity politics; and I am proposing, in the Citizens' Audit, a mechanism by which these questions can be sharpened, analysed and debated. Until we undertake some such process we have permitted the technocrats to take our democratic power from us in a less direct but none the less complete way as the troika have done in Ireland and the technocratic government has done in Italy.

Why We Can't Be Green If We're In the Red

For the Chancellor-as-Thrifty-Housewife made popular by Prime Minister Thatcher and maintained (without the use of make-up or women's clothing) by George Osborne, nothing is as shameful as the opprobrium of failing to repay your debts. Monetary theorists see things rather differently. A country that has defaulted may face some temporary difficulty in raising loan finance, but this is likely to be short-lived. A research study from the Bank of England did not find this a compelling argument against default, arguing that 'Overall, the empirical evidence suggests that sovereign default is not necessarily associated with any loss of market access'.[36] If the choice is between destroying the social cohesion and supportive public institutions that we count as our due or renegotiating with wealthy foreign creditors then this is a debate that should be held publicly rather than made for us by our betters and turned into a hegemonic and unchallengeable 'consensus'.

The most resounding lesson from the 2008 financial crisis should be that creating our money privately, through banks, and with debts attached is not a civilized way to deal with the need to facilitate exchange. The alternative means of creating money is via a central bank that spends money into the economy (see Robertson and Huber, 2000). The resort to quantitative easing in the UK undermines the decades of argument that such a means of money creation was impossible and makes calls for the transfer of money creation from private to public sectors much more credible. Creating money in this way would have the considerable benefit that at its first creation the money would be available to be spent for public purposes rather than private profit and could fund the building of the green infrastructure that a sustainable society will require. The Green Party passed a policy to create money in this way at its conference in September 2013.

Many important demands on investment are not being heard because of the deafening ubiquity of the politics of austerity. From the perspective of Green House the most important demand is for transitional investment to enable the transition towards a green economy. We propose the idea of 'transitional investment' to define how all finance should be invested to underpin a sustainable future. A transitional investment is one which, while requiring the investment of energy now, will ensure that less energy will be required in future; one might take the example of the concrete needed to support a wind-turbine. If the investment of energy merely increases future demand for energy, say through the installation of a system of recharging points for electric cars, leading to a higher demand for the production of such cars, it cannot be considered 'transitional investment'.

Determining what constitutes a transitional investment needs a related concept with a longer pedigree, the idea of Energy Return on Energy Invested (EROEI). An orthodox financial market will focus its decisions about investment on the highest financial return. However, from a sustainability perspective the more useful measure of the value of an investment is energy return on energy invested. For finance to be considered to be Green Finance it would need to balance a measure of ROI with a measure of EROEI (energy return on energy invested).[37]

The existence of a green investment gap is evidence of the failure of the financial markets to allocate capital in the long-run interests of society. We would suggest that, while it is possible to earn vast and rapid returns through merely taking positions on derivative products, there is never likely to be adequate investment in green infrastructure where returns are slower, lower, and should be measured in terms of social and environmental rather than narrowly financial benefit. The introduction of an EROEI criterion will prevent the benefits in green investment with a high EROEI from being offset by investment that increases energy or carbon emissions elsewhere.

But most importantly neither this essential pro-sustainability investment nor the investment needed to maintain our schools and hospitals will be possible until we challenge the narrative of austerity that says we must cut and cut again to pay our creditors. We should ask who those creditors are, how we came to owe our lives to them, and what would happen if we decided to negotiate our debts rather than allowing them to control our lives. Until we do this the attacks on the lives and livehoods we share as a civil society will continue and intensify.

Endnotes

[1] Shelley, A Philosophical View of Reform, 1820
[2] Fahmy, E., Thumim, J. and White, V. (2011), 'The distribution of UK household CO2 emissions: Interim report' (York: Joseph Rowntree Foundation).
[3] Writing in the Guardian, 'Quantitative Easing Should be Aimed at Green Economy': http://www.theguardian.com/environment/2012/jun/26/david-king-quantitative-easing-green
[4] For information on the nature of these funding deals see David Hall's Critique of PPPs (2008), available here: http://www.epsu.org/IMG/pdf/PPPs-crit-finalLAYOUT-2.pdf
[5] Maxed Out: Serious Personal Debt in Britain, November 2013, available here: http://www.centreforsocialjustice.org.uk/UserStorage/pdf/Pdf%20reports/CSJ_Serious_Debt_report_WEB_final.pdf
[6] French, D. (2006), 'The Dutch Monetary Environment During Tulipmania', The Quarterly Journal of Austrian Economics, 9/1: 3-14.
[7] Haldane, A. and Kruger, M. (2001-2), 'The Resolution of International Financial Crises: Private Finance and Public Funds', Bank of Canada Review, winter.
[8] Cato, M. S., 'Argentina in the Red: What can the UK's Regional Economies Learn from the Argentinian Banking Crisis?', International Journal of Community Currency Research, 10: 43-55.
[9] Olivares-Caminal, Rodrigo (2008), 'Sovereign bonds: A critical analysis of Argentina's debt exchange offer', Journal of Banking Regulation, 10/1: 28-45.
[10] Hornbeck, J. F. (2004), 'Argentina's Sovereign Debt Restructuring', CRS Report for Congress, available here: http://fpc.state.gov/documents/organization/39301.pdf, downloaded, 4 Nov. 2011.
[11] 'A victory by default? The successful restructuring of Argentina's debts has set a painful new benchmark for creditors', *Economist*, 4 Mar. 2005.
[12] Olivares-Caminal, op. cit. 29.
[13] Economist, A victory by default? The successful restructuring of Argentina's debts has set a painful new benchmark for creditors, 3 March; available on the website.
[14] Haldane and Kruger, 'Resolution', p. 6.
[15] Op. cit. p. 7.
[16] Johnson, S. (2009), 'The quiet coup', Atlantic Magazine, May.
[17] Op. cit. p. 8.
[18] Top marks to Polly Curtis and Jill Treanor for sticking at this question: http://www.theguardian.com/politics/reality-check-with-polly-curtis/2011/sep/12/reality-check-banking-bailout
[19] New Economics Foundation (2011), Where Did Our Money Go? Building a Banking System Fit for Purpose (London: Nef).
[20] Olivares-Caminal, op. cit. 29.
[21] Gentile, C. M. (2010), 'The Market for Odious Debt', Law and Contemporary Problems, 73: 151-174 (Fall 2010). Available at: http://scholarship.law.duke.edu/lcp/vol73/iss4/11.
[22] Jayachandran, S. and Kremer, M. (2006), 'Odious Debt', American Economic Review, 96/1: 82-92.
[23] Buchheit, L. C., Gulati, G. M., and Thompson, R. B. (2007), 'The Dilemma of Odious Debts', Duke Law Journal, 56/5: 1201-62.
[24] Cable, V. (2009), The Storm: The World Crisis and What it Means (Atlantic Books); Lanchester, J. (2010), Whoops! Why Everyone Owes Everyone and No one Can Pay (London: Allen Lane).
[25] Mellor, M. (2010), The Future of Money (London: Pluto).
[26] Treanor, J. (2009), 'Cash machines were monitored every hour during banking crisis', Guardian, 11 October.
[27] HMRC (2013), Corporation Tax Statistics, available here: http://www.hmrc.gov.uk/statistics/ct-receipts/corporation-tax-statistics.pdf
[28] HMRC tax statistics Table 11.1, available here: http://www.hmrc.gov.uk/statistics/ct-receipts/table11-1a.pdf
[29] Panizza, U., Sturzenegger, F. and Zettelmeyer, J. (2009), 'The Economics and Law of Sovereign Debt and Default', Journal of Economic Literature, 47:3, 651–698.
[30] Op. cit., p. 653.

[31] Op. cit., p. 654.
[32] Kremer, M. and Jayachandran, S. (2002), 'Odious Debt', NBER Working Paper No. 8953.
[33] Busby, J. W. (2007), 'Bono Made Jesse Helms Cry: Jubilee 2000, Debt Relief, and Moral Action in International Politics', International Studies Quarterly, 51/2: 247-275.
[34] Public Accounts Committee - Forty-Fourth Report: 'Lessons from PFI and other projects', July 2011, para. 12.
[35] In November 2013 the BBC reported that individual debt had reached a record £1.43 trillion (http://www.bbc.co.uk/news/business-25152556); while the Independent was reporting that such debt had doubled in the past decade: http://www.independent.co.uk/money/loans-credit/1430000000000-britains-personal-debt-timebomb-8950372.html
[36] De Paoli, B., Hoggarth, G. and Saporta, V. (2009), 'Output costs of sovereign crises: some empirical estimates', Bank of England Working Paper no. 362.
[37] Murphy, D.J.; Hall, C.A.S. (2010). "Year in review EROI or energy return on (energy) invested". Annals of the New York Academy of Sciences **1185**: 102–118