Radical Options for Scotland and Europe

For public ownership and democratic control

Briefing 54: December 2022

Cuts, Financial Instability, Rate Rises & Trade Rivalry

Scottish Budget: 15 December
Real term cuts – worst for local government

According to the Fraser of Allander Institute, local government faces a real terms cut of 4.9 percent in the budget presented to the Scottish parliament on 15 December. COSLA, representing local authorities, unanimously condemned the budget as putting local government at 'real financial risk'. It will be 'our communities that will suffer'. COSLA called for the government to pause its plan to set up a National Care Service, budgeted at £1.7 billion. The Scottish government, like the Westminster government, had lowered the tax ceiling for the highest rate of tax – and also added a 1p in the £ to the two highest tax brackets.

Bank of England rate rise: 15 December
Up 0.5 percent to 3.5 percent

The Trades Union Congress commented that 'the rise could make a bad situation worse. The priority now should be protecting living standards and boosting the economy to stop the recession and protect people's jobs.' A survey of British firms' investment intentions, taken the previous week, showed them falling from +7 percent to -5 percent (Financial Times). The Bank's Financial Stability Committee commented that while financial conditions appeared less threatening than in the run up to the Great Financial Crisis of 2008 'there are a number of vulnerable companies with low liquidity, weak profitability, or high leverage. And some businesses are facing other pressures from higher costs of servicing debt, weaker earnings, and continued supply chain disruption. These pressures are expected to continue to increase over 2023, especially for smaller companies that are less able to insulate themselves against higher rates.'

Bank of International Settlements in Basle
Warning on debt levels

The BIS, responsible for monitoring global conditions, commented on 5 December 'overall asset price volatility ... is elevated in context of poor liquidity conditions across market segments ... in many core bond markets liquidity worsened ... mortgage real estate investment trusts a potential source of market dysfunction'. A further report published on 9 December noted that 'synchronised and sudden' monetary tightening had in the past been effective but warned' it holds the danger of 'risk to financial stability in an environment of high public and private debt levels'.

European Central Bank rate setting 15 December:
Interest rates up 0.5 percent: a 'steady and significant tightening of monetary policy'.

The ECB raised its interest rates by 0.5 percent to 2.5 percent. Christine Lagarde commented that this was in response to 'the substantial upward revision to the inflation outlook' and that 'we expect to raise them further and … significantly at a steady pace to reach levels that are sufficiently restrictive to ensure a timely return of inflation to our two per cent medium-term target. … The

Governing Council today also discussed principles for normalising the Eurosystem's monetary policy securities holdings. From the beginning of March 2023 onwards, the asset purchase programme (APP) portfolio will decline at a measured and predictable pace, as the Eurosystem will not reinvest all of the principal payments from maturing securities. The decline will amount to €15 billion per month on average until the end of the second quarter of 2023 and its subsequent pace will be determined over time.'

Ms Lagarde further commented 'we decided to raise rates today, and expect to raise them significantly further, because inflation remains far too high and is projected to stay above our target for too long … Food price inflation and underlying price pressures across the economy have strengthened and will persist for some time. Amid exceptional uncertainty, Eurosystem staff have significantly revised up their inflation projections … The past deterioration in the terms of trade, reflecting the faster rise in import prices than in export prices, continues to weigh on purchasing power in the euro area.'

Demand for tighter control over budgets of member countries
'Reform of the EU's economic governance framework should be concluded rapidly'

The ECB statement called on government to 'swiftly implement their investment and structural reform plans under the Next Generation EU programme. The reform of the EU's economic governance framework should be concluded rapidly. Eurosystem staff projections see wages growing at rates well above historical averages and pushing up inflation throughout the projection period.'

Italy attacks size and speed of credit tightening

On 16 December Italy's deputy prime minister Crosetto and defence minister Salvini attacked the policy as unjustified and will 'burn billions'. The differential between Italian and German ten year bonds (government borrowing costs) has risen to 2.15 percent.

EU Parliament approves a Carbon Border Tax:
counter to US Inflation Reduction Act

On 16 December the European Parliament approved a new tax regulation from the EU Commission to impose a Carbon Border Tax on all imports into the EU. The tax is designed 'to raise environmental standards globally' by penalising goods from countries with less stringent regulations. It is widely seen as a response to the US Inflation Reduction Act that subsidises a range of US products particularly for electric cars, batteries and IT equipment, where competition between the US and Germany has been most intense.