

Can the UK Afford MMT? The Question Doesn't Make Sense

The question of whether the UK could "afford to adopt" Modern Monetary Theory contains a category error worth discussing, because the confusion it reflects is widespread.

At its core, MMT is primarily a description of how currency-issuing governments already operate. Asking whether Britain can "afford" MMT is like asking whether it can afford to adopt double-entry bookkeeping, or whether it can afford to acknowledge that the Bank of England exists. The UK doesn't need to "adopt" MMT. The institutional mechanics MMT describes are already how the British state functions.

What MMT actually claims

The core MMT insight is simple: governments that issue their own currency operate differently from households and businesses. When the Treasury authorises spending, it doesn't first rummage through a vault of accumulated taxes. It instructs the Bank of England to credit accounts. The Bank must comply as it has no legal power to refuse parliamentary-authorized expenditure. Money flows into the economy. Taxation and bond issuance happen after spending, draining reserves (money in the banking system) that were created by the act of spending in the first place.

This operational reality is documented in Treasury publications, Bank of England bulletins, and peer-reviewed institutional analyses. Berkeley, Ryan-Collins and colleagues traced these mechanics in detail in *The Self-Financing State*. The government's main account at the Bank of England starts each day at zero. Spending happens via balance sheet expansion, which is a form of money creation. The sequence runs opposite to household budgeting.

Nor is this understanding confined to obscure academics. Alan Greenspan, hardly a radical, explained it plainly in a speech given in 1997:

"Central banks can issue currency, a non-interest-bearing claim on the government, effectively without limit. They can discount loans and other assets of banks or other private depository institutions, thereby converting potentially illiquid private assets into riskless claims on the government in the form of deposits at the central bank. That all of these claims on government are readily accepted reflects the fact that a government cannot become insolvent with respect to obligations in its own currency. A fiat money system, like the ones we have today, can produce such claims without limit."

Greenspan continued: "To be sure, if a central bank produces too many, inflation will inexorably rise as will interest rates, and economic activity will inevitably be constrained by the misallocation of resources induced by inflation. If it produces too few, the economy's expansion also will presumably be constrained by a shortage of the necessary lubricant for transactions. Authorities must struggle continuously to find the proper balance."

This is the former Chairman of the Federal Reserve stating, on the record, that currency-issuing governments cannot become insolvent in their own currency, while simultaneously noting that inflation is the binding constraint. Both parts matter. The mechanics are real. So are the limits.

The Full Funding Rule, often cited as the reason for "borrowing," requires that government issue bonds to match deficits. It dates to 1981 and was rooted in monetarist theory the

Treasury abandoned when it switched to inflation targeting in 1992. It persists through convention and could be changed by ministerial decision. No Act of Parliament would be required.

None of this is seriously contested by anyone who has studied the mechanics

The Bank of England's evasions

If the mechanics are so clear, why does confusion persist? Partly because institutions that should know better actively muddy the waters.

Consider a response from the Bank of England's Engagement and Enquiries Group to a member of the public who asked whether the government creates money. The Bank replied: "The government finances its expenditure through a combination of current tax revenues and the issuance of government bonds ('gilts'), which it sells to investors via the Debt Management Office (DMO). Neither the act of taxation nor the issuance of government bonds directly affects the overall amount of money in the economy. In that sense, the money the government spends is coming from existing money in circulation."

This is the orthodox framing: government must tax or borrow first, then spend. But notice the peculiar admission buried in the middle: "neither the act of taxation nor the issuance of government bonds directly affects the overall amount of money in the economy." If the government were genuinely spending pre-existing money obtained from taxes and bond sales, those transactions would affect money in circulation. The statement contradicts itself.

The letter continues:

"The Bank of England can create and destroy central bank reserves ('base money'), which is how for example it conducts 'Quantitative Easing' (QE)... But the Bank of England has operational independence from the government, and QE decisions, and all other monetary policy decisions, are made solely for the purposes of achieving the Bank of England's remit of price stability, e.g. low and stable inflation, and not for the purposes of financing government spending."

Here the Bank acknowledges it can create money, but insists this power is used only for monetary policy, never to finance government spending. This is a policy choice dressed up as an institutional fact. The Bank's operational independence is real, but it doesn't change the underlying mechanics. When the Treasury authorises spending and draws on the Consolidated Fund, the Bank of England credits the relevant accounts. It has no legal discretion to refuse. The spending happens first; QE, taxation, and bond issuance are separate operations that occur afterward.

Most revealingly, the letter then admits:

"In principal governments or their central banks, can create certain types of money, which could be used to pay for government expenditure. But in practice, this has tended to be associated with high inflation and other adverse economic consequences. Which is why many countries, including the UK, have strong institutional arrangements to prevent this from happening, such as an independent central bank tasked with an inflation target."

So within three paragraphs, the Bank of England has said: first, the government finances spending from existing money; second, the Bank can create money but only for price stability purposes; and third, actually, governments can create money for expenditure, but institutional arrangements exist to "prevent this from happening."

This is incoherent. Either governments can create money for spending or they can't. The Bank's own technical publications, its Quarterly Bulletins from decades past, and the legal framework governing the Consolidated Fund all confirm that they can and do. What the Bank appears to be doing in this public communication is defending a useful political fiction: the idea that spending is constrained by available funds rather than by policy choices about inflation risk.

The contrast with Greenspan's directness is instructive. The former Federal Reserve Chairman stated the mechanical reality plainly and acknowledged the inflationary constraint without equivocation. The Bank of England's response, by contrast, attempts to simultaneously affirm the mechanics, deny their implications, and then partially concede them. This internally inconsistent position satisfies neither accuracy nor accessibility. The pattern is characteristic of institutional communications shaped more by political considerations than by explanatory clarity.

Mechanics versus policy

The institutional mechanics of government spending, including the Consolidated Fund, the Bank of England's role, and the spending-then-taxing sequence, are MMT-independent. They're factual descriptions of how the UK Exchequer operates. You don't need to "believe in" MMT to accept them, any more than you need to believe in a particular school of physics to accept that gravity exists. An accountant tracing the ledgers would find the same thing. This is how the system works.

MMT proponents often go beyond describing mechanics, however. They put forward specific policy proposals that are genuinely contestable. These are economic and political choices that deserve separate scrutiny.

Zero Interest Rate Policy. Some MMT economists argue that the "natural" or default interest rate for a currency-issuing government should be zero. The reasoning is that since government "debt" is really just money in another form, paying interest on it is a policy choice that distributes income to bondholders. This is arguably a coherent position, but it remains a policy proposal rather than an accounting observation. Whether zero rates are wise depends on views about inflation, asset prices, financial stability, and income distribution that the mechanics alone don't resolve.

The Job Guarantee. This is perhaps the signature MMT policy prescription: government as employer of last resort, offering a job at a fixed wage to anyone who wants one. Proponents argue it provides an automatic stabiliser (spending rises in recessions, falls in booms) and anchors prices through the "buffer stock" of employed labour. Critics worry about implementation, the quality of guaranteed jobs, and whether it would actually control inflation as claimed. Whatever its merits, the Job Guarantee is an economic programme rather than a description of existing institutions. You can accept every word of how MMT economists describe the mechanics of the monetary system and still oppose a Job Guarantee.

Imports as benefit. Some MMT economists frame imports as unambiguously good for the importing nation: you receive real goods and services, and in exchange you provide currency you can create. Exports, by this logic, are a cost, with real resources leaving the country. This framing contains a kernel of truth, since imports do represent real consumption, but it's a specific analytical choice that downplays the constraints of an open economy. Britain can't print dollars or euros. Persistent trade deficits can pressure the exchange rate, raising import costs and feeding inflation. The treatment of imports as pure benefit is an MMT-specific framing that arguably understates the vulnerabilities of a mid-sized open economy like the UK.

The point is this: when someone invokes "MMT," you need to ask which part they mean. The mechanics of money creation are real and largely uncontroversial among people who've studied them. Zero rates, Job Guarantees, and particular views on imports are policy positions that require separate arguments. Conflating the two, and treating contested policies as though they follow automatically from correct accounting, shouldn't go unchallenged.

Accountants versus economists

The institutional mechanics of government spending, that is how money moves through government accounts, when accounts are credited, and what sequence spending and taxation actually follow, are accounting questions. They have factual answers. You trace the ledgers, follow the debits and credits, and report what happened. An accountant examining the Exchequer's operations would tell you: spending creates deposits, taxation drains them, bond issuance swaps one government liability for another. These are descriptions of what the books show, free of ideological content.

Economists, by contrast, are in the business of interpretation. Give the same national accounts to a neoliberal and you'll hear about fiscal incontinence and intergenerational theft. Give them to a Marxist and it becomes evidence of late capitalism devouring itself. Both conclusions were reached with the same numbers. The conclusion was already written before anyone opened a spreadsheet. You can be a neoliberal economist or a Marxist economist, as the profession accommodates both. But there's no such thing as a neoliberal accountant. Nobody accuses bookkeepers of ideological bias when they're examining a set of accounts.

Too often, economists who lack knowledge of the institutional mechanics, sometimes deliberately and sometimes through neglect, allow their ideological priors to determine what they claim the constraints are. They treat "the government must borrow before it can spend" as a factual description when it's actually a misunderstanding of how the system operates. The accounting shows this clearly. When economists misrepresent the mechanics to support their preferred policies, they're doing politics dressed up in technical language.

The Bank of England's muddled public response is a case in point. Rather than clearly stating the mechanical reality and then explaining the policy choices made to manage inflation risk, it offers a confused account that simultaneously denies and admits the government's money-creating capacity. This serves no one, except perhaps those who benefit from public confusion about how the system actually works.

This doesn't mean accountants should make policy. The accounting tells you what is: how money moves, what the balances show. It doesn't tell you what ought to be, or how much to spend, on what, or with what risks. That's where economics, politics, and judgment come in. But we need to separate the two cleanly. Establish the mechanics first, with accounting precision. Then have the political argument about what to do, without either side pretending their preferred answer is dictated by the mechanics.

The real constraint

Greenspan put his finger on the actual issue in testimony to the House Budget Committee in 2005, discussing Social Security:

"I wouldn't say the pay-as-you-go benefits are insecure in the sense that there is nothing to prevent the Federal Government from creating as much money as it wants and paying it to somebody. The question is, how do you set up a system which assures that the real assets are created which those benefits are employed to purchase? So it is not a question of security. It is a question of the structure of a financial system which assures that the real resources are created for retirement as distinct from the cash. The cash itself is nice to have, but it has got to be in the context of the real resources being created at the time those benefits are paid and so that you can purchase real resources with the benefits, which of course are cash."

Yes, the government can create unlimited cash. That capacity doesn't extend to creating unlimited real resources. The cash is "nice to have" but meaningless without goods and services to purchase. An economy that prints money faster than it produces things becomes Argentina.

The question isn't "can we afford it?" in the sense of finding enough pounds. The question is whether the real resources exist, such as skilled workers, materials, and productive capacity, and whether deploying money to claim those resources will crowd out other uses or bid up prices. These are hard questions requiring judgment. They aren't resolved by noting that the Bank of England can credit accounts.

The real questions

Once you clear away the category error, the substantive questions emerge.

What are the actual constraints on government spending? Inflation. Productive capacity. Skilled labour. Import dependence, since 30% of UK consumption is priced in foreign currency, mainly dollars, and you can't print those. Planning dysfunction. Supply chains. How well can policymakers identify those constraints in advance? Poorly. The recent inflation surge demonstrated this painfully. Central banks with sophisticated models got inflation catastrophically wrong for over a year in 2021-22. If professionals can't reliably identify the productive frontier, the suggestion that politicians will calibrate spending to stay just below it deserves scepticism.

What happens when they get it wrong? Inflation erodes real wages. Currency depreciation raises import costs. Monetary policy tightens brutally to restore credibility. The people who suffer most are those on fixed incomes and without assets.

Should we obsess over debt-to-GDP ratios? To paraphrase Abba Lerner: a 100% debt-to-GDP ratio is what happens when the face value of government debt equals the value of the flow of domestic production that occurs during the period when the Earth completes one orbit around the Sun. When put that way, the concept seems rather stupid. The reason is that it is rather stupid. We're comparing a stock of government debt to a flow of income. To be strictly comparable, we need to compare stocks to stocks, or flows to flows.

The debt-to-GDP ratio has become the primary metric around which fiscal debates revolve, but it's a conceptually muddled measure dressed up as precision. What matters is whether the debt is serviceable (it always is for a currency issuer in its own currency), whether the spending it financed was productive, and whether the inflation constraint is being respected. A country with 150% debt-to-GDP that invested in productive infrastructure may be in a far stronger position than one with 50% debt-to-GDP that let its capital stock rot. The ratio tells you almost nothing about this. Yet chancellors rise and fall on whether the line on the chart is pointing the right direction during an arbitrary forecast period.

Have fiscal rules actually worked? Here we should be honest: the track record is poor. Britain's fiscal rules have, in practice, consistently produced austerity and declining economic growth. The requirement to balance spending against taxation, treating the government budget like a household budget, ignores everything the accounting tells us about how the system actually works. A rule that requires current spending to match current revenue will almost never be optimal. It prevents counter-cyclical policy, biases against investment, and treats deficit reduction as an end in itself rather than asking what the deficit is actually for.

The problem is that we've had the wrong constraints, derived from a faulty model of government finance. Rules that target arbitrary debt ratios or mandate balanced budgets embed the household analogy into policy. They force governments to cut when they should spend and create the very stagnation they claim to prevent. Britain's infrastructure gap, its productivity collapse, its decade of lost growth: these are partly the consequences of fiscal rules that misunderstood what they were constraining.

Acknowledging that existing fiscal rules have failed points toward the need for better ones. Rules that account for inflation risk, productive investment, and the actual mechanics of government finance, rather than rules built on the false premise that the Treasury is a large household. The failure of current rules does not mean constraints are illusory.

Should the UK borrow more for productive investment? Almost certainly yes. That's a judgment about specific projects and their returns, informed by the accounting reality that "borrowing" for a currency-issuer isn't what the word implies. But it's still a judgment requiring evidence and careful planning.

The bottom line

The UK already operates the way MMT describes. It has since 1971, arguably since the end of the Gold Standard in 1931. The question isn't whether to "adopt" this framework but what policy conclusions follow from it.

We mustn't conclude that because the government creates money, fiscal constraints are illusory and "brave leadership" can spend freely on desirable things. The constraint shifted from reserves to inflation. That's a different constraint, but a constraint nonetheless. Understanding how money works is the beginning of economic wisdom, not the end. Correctly describing the mechanism does not resolve the policy debate. The hard questions remain: how much inflation risk is acceptable, how do we identify productive capacity, what investments actually generate returns, how do we manage an open economy dependent on imports?

Those questions require judgment, evidence, and humility about what we don't know. They aren't answered by observing that the Bank of England can credit accounts. Nor are they answered by pretending the government is a household that must earn before it spends. Both sides of this debate have been guilty of letting ideology masquerade as accounting. The accounting is clear. The politics remains contested. We should stop confusing the two.

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