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Britain needs a ‘whatever it takes’ moment

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Since 2008, the UK has slid into a deep economic and political predicament. Growth has stagnated to a degree far worse even than in the 1970s. The Tory leadership’s wager on the Brexit referendum spectacularly backfired, leaving the UK isolated from Europe and at the mercy of its special relationship with the US, many of whose political class regard the UK as a basket case. After years of austerity, the Labour party lurched to the left and then back to the centre. The Tory party has been eclipsed by the populist nationalism of Reform.

Any British government should be worrying first and foremost about how to restart growth. Instead, Keir Starmer is beset by shades of the gilt market panic triggered by the Liz Truss government in 2022. The debt level is higher than in recent years, but there is no cause for panic. UK debt is at far from critical levels and of long duration. Whether you want to “take back control” or launch progressive economic policy, a democracy dogged by fear of bond market vigilantes is unhealthy. In a country that is a monetary sovereign, this climate points to one thing: a disconnect between the government and the central bank.

Since 1997, the independence of the Bank of England has become a sacred cow. But independence is what you make of it. And in the wake of the gilt market crisis of September 2022, relations between the Bank of England and the UK government need a reset.

In normal times, there is no doubt that an inflation-targeting independent central bank can serve a country well. But since 2008, the UK and other advanced economies have not had the luxury of such simple problems.

To their credit, central bankers around the world have not stood on orthodoxy. After 2008, the US Federal Reserve rescued the global banking system and, through quantitative easing, it stabilised the Treasury market in the face of huge deficits. In Europe, things were trickier. Both the Bank of England under Mervyn King and Jean-Claude Trichet’s European Central Bank played cat and mouse with national governments. This was a high stakes wager that between 2010 and 2012 escalated bond market tension and triggered a disastrous turn to austerity.

Shaken by the impact of those shocks, their successors, Mark Carney and Mario Draghi adopted a more protective stance (assuming you were not the government of Greece). Recall that Draghi’s legendary slogan, “Whatever it takes”, was uttered to face down the City of London’s bond vigilantes. In 2015, Draghi launched QE — financial repression by another name. In 2016, Carney used

the authority of the Bank of England to stabilise markets following the vote for Brexit, an exemplary demonstration of how central banks can underpin democratic choice, even when those choices are wrong headed.

All these were independent central bankers steeped in the best practice of the 1990s, who recognised that historic crises demanded radical action.

It was the price surge of 2021-2023 that poisoned the atmosphere. Though the shock came mainly from the supply side, central banks ended up in the dock. Nowhere more so than in the UK. The Bank of England reacted with aggressive normalisation. Faced with a cost of living crisis, the governor called for workers to accept real wage cuts. In early 2022, as gas prices were at record levels and Russia's army was poised to invade Ukraine, the Bank adopted a stringent programme of quantitative tightening, elevating interest rates. When the Truss government got itself in trouble, the Bank took almost a week to come to the rescue.

Rather than enacting a charade of normality, it is time to recognise that in 2025 the UK faces a period of historic transition. To meet this challenge, what is needed is a new concordat with the Bank. This should not ignore inflation-ary pressures or the long-run trajectory of debt, but should affirm the priority of reviving investment-led growth.

One could follow Trump in demanding interest rate cuts. The Bank could shadow the ECB in its commitment to capping Eurozone yields. But the top priority should be to lay the ghost of September 2022. The Bank's slowing of QT last month was a concession. An immediate and complete end would send the right signal.

Such a concordat will not by itself restore sanity to politics, solve the housing problem or rebuild the NHS. But it would help to lift the fear of bond market crisis, which is paralysing the effort by democratic politicians to answer the fundamental questions facing the nation.