

What Can We Learn From Liz Truss's Britain?

Last fall, British Prime Minister Liz Truss resigned after only 49 days in office. Where did Truss go wrong? What can Japan learn from her failure?

About This Issue

Market Turmoil Spelled the End of the Short-Lived Truss Administration - What Should Japan, Facing Its Own Ballooning Government Debt, Learn From Truss's Failure?

Masaki Taniguchi

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In the fall of 2022, Liz Truss became Prime Minister of the United Kingdom. However, her "Growth Plan 2022," issued shortly after she took office, caused turmoil in financial markets. Government bond yields rose and the pound temporarily fell to a historical low against the dollar.

Prime Minister Truss stepped down after only 49 days in office, taking responsibility for the disturbance ignited in financial markets.

Where did Truss go wrong?

What should Japan learn from her failure?

In this issue of *My Vision*, we seek the opinion of experts in British politics and economics.

Keywords...Delicate management approach adopted by government, dialogue with markets, path to fiscal and financial stability

Expert Opinions

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The Truss Debacle: How Neglecting Financial Stability Ignited an Economic Time-Bomb

Bill Emmott

Writer and Consultant on International Affairs, Former Editor-In-Chief of The Economist (1993 to 2006)

Keywords... "Trussonomics," financial time bomb, credible economic planning

The Market Judged the Timing, Content, and Approach of the Truss "Growth Plan" to Be Unsuitable

Sayuri Ito

Director, Economic Research Department, NLI Research Institute

Keywords...Timing, content, approach, market sentiment, review by fiscal watchdog

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Professor, Faculty of Law, Meiji Gakuin University

Keywords...Small government stance, northern English workers, unexpected market reaction

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Professor, Faculty of Law, Okayama University

Keywords...Party member dynamics, organizational issues, political inexperience

The UK Labour Party Seeks a "New Coalition" That Embraces Diversity

Kensuke Takayasu

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Keywords...Growth through investment and distribution, new coalition, relations with the trade unions

Interview period : March - April, 2023

Interviewer : Atsushi Inoue (Research Coordinator and Research Fellow, NIRA), Jonathan Webb (Research Coordinator and Research Fellow), Maiko Sakaki (Editor-in-Chief)

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The United Kingdom is currently excited about the coronation of its new king, Charles III. Nevertheless, the recent turmoil in the nation's political arena continues. In 2016, Prime Minister David Cameron resigned after losing a referendum on whether the nation should remain in the EU, and his successor, Theresa May, resigned after only three years in office following the stalling of negotiations related to Britain's exit from the EU. Her successor, Boris Johnson, who had popular support, led the Conservative Party to an overwhelming victory in the general election, and oversaw Brexit, was forced to step down after a series of scandals, for example involving his attendance at a party despite lockdown restrictions during the pandemic.

Liz Truss followed Johnson in the office of Prime Minister. A Liberal Democrat while at Oxford University, she transferred her allegiance to the Conservative Party following graduation. As Secretary of State for Environment, Food and Rural Affairs in Cameron's cabinet, Truss favored remaining in the EU, but following the referendum, she advocated for Britain's withdrawal from the union. As a follower of the thinking of Margaret Thatcher, an advocate of neoliberalism in the 1980s, she attempted to promote corporate tax cuts after becoming Prime Minister, and also announced a plan to curb energy costs that would entail massive government spending. This sudden policy change, which was not backed up by any financial resources, plunged the market into turmoil, resulting in a sharp depreciation of the currency, and declines in stock prices and the value of government bonds, a situation that forced Truss to resign after only 49 days in office. Not only was this the shortest tenure of a Prime Minister in British history, but when we compare the situation with Japan's own history, where (with the exception of Junichiro Koizumi and Shinzo Abe) Prime Ministers are well known to be frequently replaced after brief terms, Truss's tenure was shorter even than the 54 day term of the Cabinet of Prince Higashikuni, which immediately followed the end of the Second World War.

Currently, Japan's outstanding debt is more than twice the nation's GDP, and large-scale monetary easing measures have been in place for an extended period. Although there is widespread concern regarding the sustainability of Japan's fiscal and social security systems in view of the nation's declining birthrate and aging and declining population, Japan's government cannot simply tighten fiscal and monetary policies, and has no choice but to adopt a delicate long-term management approach. What happened in "Truss's Britain"? What should Japan learn from this? For this issue of My Vision, we asked five experts on British politics and economics to contribute their views.

Where Did Truss Go Wrong?

Bill Emmott, an international journalist and former Editor-in-Chief of The Economist, points out that the Truss government's intention to immediately and decisively implement major tax cuts without presenting a credible plan or framework for regulatory reform that would bring about long-term growth, and without indicating how to make up the budget shortfall, set off a "financial time bomb," causing interest rates to soar and the currency to plummet, in addition to generating volatility in the bond market, which had the potential to trigger a decline in the solvency of pension funds.

Similarly, Sayuri Ito, Director of the NLI Research Institute's Economic Research Department, criticizes Truss's "Growth Plan 2022" for the timing of fiscal expansion in the midst of

the worsening of public finances caused by the pandemic, in addition to soaring energy prices, the plan's policy content, its goal of stimulating the economy through major tax cuts despite the fact that Brexit lies behind low growth in the UK, and the plan's approach, the administration's stance of seeking to avoid verification of the budget proposal by the Office for Budget Responsibility (OBR), an independent fiscal watchdog. These were all criticized as inappropriate.

Why did Truss adopt policies that were doomed to failure? And why did the Conservative Party choose such a leader? According to Professor Daisuke Ikemoto of Meiji Gakuin University, in response to criticism of the "big government" stance of the Johnson administration, Truss oriented herself toward the "small government" stance that had represented the mainstream in the Conservative Party since the Thatcher administration. Professor Ikemoto indicates that despite this, political considerations in the run-up to the general election saw large-scale utility subsidies being proposed without clarification of the source of finances, inviting defection by the market.

In addition to this, Professor Takashi Narihiro of Okayama University tells us that under the party leadership election rules, which see party members casting the deciding vote, there is little hope for a reconsideration of Brexit, the real cause of the economic slump, and that the significant change in the face of the Conservative Party since the 2010 election, with members possessing little political experience, including Prime Minister Truss herself, occupying the core of the government, led to the blunder of launching the wrong policies without prior consideration of market reaction.

As the Conservatives Attempt to Defuse the Situation, What Next for Labour?

Prime Minister Rishi Sunak, who succeeded Truss, is attempting to defuse the situation by adopting a stance that sees the party avoiding major increases in spending, without shying away from raising taxes if necessary. However, the Conservative Party's approval rating continues to stagnate, and is far behind that of the Labour Party. Would a Labour government be able to restore the British economy to health?

According to Professor Kensuke Takayasu of Waseda University, the road ahead for the Labour Party, led by Sir Keir Starmer, is not necessarily an easy one. The party would like to adopt aggressive fiscal policies, but given the history of the collapse of the Truss administration, the UK does not have the reserves for public investment at present. The challenge for the party will be whether it can win the support of a broad range of people and form a "new coalition" through investment and distribution policies.

What Japan Should Learn From "Truss's Britain"

Should Japan take "Truss's Britain" as an object lesson? Bill Emmott's view is that Japan's current situation is similar to that of the UK in many respects, including low growth, high inflation, and long-term continuity of monetary policy. At the same time, Professor Narihiro, Professor Takayasu, and Ms. Ito argue that it would be difficult for Japan's Prime Minister to implement policies that require significant financial resources, such as large-scale tax cuts, on their own initiative, and that, as a net creditor nation with relatively ample funds, Japan is unlikely to immediately receive a rejection from the market. However, all agree that the risk of increased pain is greater if fiscal discipline is allowed to be relaxed beyond its limit. It will be necessary to listen carefully to the market and engage in thorough dialogues in order to determine the path to fiscal and monetary stabilization.

Professor Taniguchi is NIRA's President and a Professor in The University of Tokyo's Graduate Schools for Law and Politics. He holds a Ph.D. in Law from The University of Tokyo. Professor Taniguchi specializes in political science and contemporary Japanese politics.

Expert Opinions

The Truss Debacle: How Neglecting Financial Stability Ignited an Economic Time-Bomb



Bill Emmott

Writer and Consultant on
International Affairs,
Former Editor-In-Chief of The
Economist (1993 to 2006)

The economic fallout from Liz Truss's catastrophic 49-day tenure as Prime Minister of the United Kingdom is a stark reminder of the dangers, for any country, of formulating public policy without proper attention to financial stability. Truss came to power promising bold ambitious reforms that she claimed would transform the UK economy. Once in office however, instead of outlining a coherent plan for change, she immediately proposed the country's largest tax cuts in half a century, with no mention of how the accompanying budgetary shortfall would be overcome. Amidst the country's low economic growth, reliance on overseas borrowing, and surging inflation due to COVID and the War in Ukraine, her policies triggered a financial time-bomb that led to soaring interest rates, a plummeting currency, and bond market fluctuations that threatened the solvency of UK pension funds.

Truss's reckless policy likely resulted in part from inexperience, but also from her efforts to win the leadership election of a divided Conservative Party, whose credibility and cohesiveness had been strained by the consequences of Brexit and the scandal-ridden tenure of her predecessor, Boris Johnson. Toward that end, Truss sought a dramatic policy that could win the support of party members, while also having a significant enough impact before the general election in 2024 to lift the party's fortunes. In a bid to depict the policy as unique her campaign labelled it as "Trussonomics." Truss failed because she failed to produce any kind of credible framework for the regulatory reforms that were supposed to generate long-term growth. Had Truss pursued her goals in a different sequence however, announcing a small initial tax cut with plans for larger cuts once the details of her broader economic plan were clear, she might have remained in power.

Simply put, she forfeited all credibility. But her rapid downfall also highlights the existence of hidden time bombs in modern financialized economies. Sudden macroeconomic shifts can result in significant unexpected losses in parts of the financial system that have positioned themselves over-aggressively on assumptions about a continuation of previous conditions. That concern indicates that policymakers should prioritise gradualism and clear communication in order to preserve financial stability.

Japan's situation today, with slow growth, unusually high inflation and a remarkably long period of monetary policy continuity, mirrors that of the UK. As the Bank of Japan attempts to exit quantitative easing and the government boosts spending in sectors like defense, childcare, and education, policymakers must find a way to maintain financial stability. Japan cannot afford the consequences of setting off a catastrophic time-bomb like the one that ended Truss's premiership.

Bill Emmott is an independent writer and consultant on international affairs. He was a prominent figure at The Economist magazine from 1980, serving as the Tokyo bureau chief from 1983 to 1986 and the editor-in-chief from 1993 until his retirement in 2006. A well known expert on Japan, he has published several groundbreaking books on the country's past, present, and future, including "The Sun Also Sets" (1990), on the problems that would eventually lead to the collapse of the Japanese economic bubble, and "The Sun Also Rises" (2006), on the country's renewed potential in the 21st century. More recently, he has written on "The Fate of the West: The Battle to Save the World's Most Successful Political Idea" (2017) and "Japan's Far More Female Future" (2020).

He is the Chairman of the Trustees for both the International Institute for Strategic Studies as well as the Japan Society of the UK. In 2016 the Japanese government awarded him the "Order of the Rising Sun: Gold Rays with Neck Ribbon" for services to UK-Japan relations.

Expert Opinions

The Market Judged the Timing, Content, and Approach of the Truss “Growth Plan” to Be Unsuitable



Sayuri Ito

Director, Economic
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When Liz Truss issued her proposed “Growth Plan 2022” shortly after becoming Prime Minister, Britain experienced a three-way decline in the pound, the value of government bonds, and stock prices. The market viewed the growth plan as an extremely risky policy. The reason for this was the unsuitability of the timing, content, and method of the policy. At the time, the UK’s finances were deteriorating as a result of the pandemic, and inflation was accelerating due to soaring energy prices. A fiscal policy involving significant tax cuts and massive borrowing could have led to further price rises. In addition, the market was sensitive to the expected hike in the U.S. Federal Reserve’s policy rate, and in this sense also, the timing of the plan was clearly inappropriate.

The content of the growth plan was designed to reduce the tax burden on businesses by implementing significant tax cuts as a catalyst for economic revitalization. However, this prescription was the wrong one. It is true that corporate investment has been stagnant in the UK for the past seven or eight years, but the reason is not the heavy tax burden; the main reason is that since Brexit, uncertainty has increased with regard to factors such as regulations and relations with the EU, and companies have become less willing to invest. The situation was such that the government, which was formed with the support of hard-line conservatives, was unable to admit that Brexit was the cause of low growth. The only appropriate prescription would have been to work to stabilize relations with the EU and steadily implement policies offering low volatility and a high level of predictability.

There were also problems in terms of the approach taken in relation to the policy. A mechanism to ensure fiscal transparency in the UK had been created by the Cameron administration and maintained by successive conservative governments. An independent fiscal watchdog, the Office for Budget Responsibility (OBR), is tasked with reviewing the government’s budget proposals. However, the Truss administration believed that fiscal rules would hinder its own growth-oriented policies, and set out its policies without seeking a forecast from the OBR. It is highly likely that the market perceived this approach as a “fiscal risk.”

The UK has a high level of capital flow relative to the size of the nation’s economy. Its external debt and liabilities are also high, making policy management that does not cause capital outflows an extremely important issue. Truss’s failure was to destabilize market sentiment. Japan is still a net creditor nation with a relatively comfortable margin. Given this, there is a risk of laxness in fiscal discipline, and if this is not addressed, problems could worsen, resulting in greater pain later on. At this stage, a framework should be created that will ensure confidence in public finances in the medium-term.

Ms. Ito specializes in European economics, and is also an expert in the area of international finance. She maintains a close focus on the EU’s challenges as it faces numerous issues, and discusses their implications for policy and corporate strategy in Japan. After graduating from Waseda University’s School of Political Science and Economics, she worked for the Industrial Bank of Japan (as it was then known), before joining NLI Research Institute, and assumed her current position in 2019. Ms. Ito holds a Master’s degree from the Graduate School of Commerce, Waseda University. She is also a part-time lecturer at the Graduate School of Commerce, and a member of the Research Committee of the 21st Century Public Policy Institute of the Keidanren (Japan Business Federation).

Loss of Market Confidence Due to a “Quest for Popularity”



Daisuke Ikemoto

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Liz Truss won the Conservative Party leadership election that followed the resignation of Prime Minister Boris Johnson by ruling out the increases in corporate taxes and social security premiums that had been planned under the previous government, and by promising measures that favored the wealthy, including the abolition of the top income tax rate for high earners. Johnson's resignation has often been attributed to a series of scandals, such as his attendance at a party during lockdown, but in the background lay a conflict between stances within the Conservative Party. Johnson's government increased infrastructure spending in poorer areas to attract working class voters in the north of England, who had supported Brexit, towards the

Conservative Party. Most recently, it had also been forced to mobilize public finances in order to respond to COVID-19. As a result, it was necessary to raise taxes to finance the largest increase in fiscal spending in postwar Britain. In response to growing dissatisfaction within the Conservative Party with this “big government” approach, Truss attempted to return to the “small government” approach that had prevailed since Thatcher.

In a nutshell, Truss sought to be on the right (emphasizing small government) in the area of economic policy and liberal in regard to sociocultural policies such as immigration policy. However, the current majority of British voters want economic policies to the left (with an emphasis on equality and reduction of economic disparity) and conservative sociocultural policies, and Truss's position had the support of only around 2% of the electorate. Truss herself was aware that her policies were unpopular, and she needed to win over the majority of voters in anticipation of the next general election. The large-scale subsidies for energy bills added to Growth Plan 2022, which was announced immediately after her inauguration, should be understood not as a policy that Truss had sought to put in place from the beginning, but rather as one that was designed to appeal to voters and win her popularity.

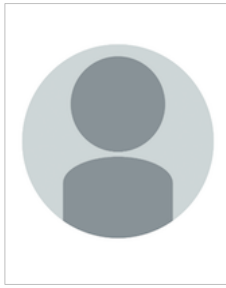
Truss differs from Thatcher in that she became Prime Minister through an internal party election, rather than winning the confidence of the people in a general election. It is likely that she planned to cut fiscal expenditure in order to balance the books after winning the general election, but political considerations in the run-up to the election saw this postponed, without clarification of the source of fiscal resources.

Since the Brexit referendum, the British political arena has become one in which the two major parties are competing to appeal to workers in the north of England, who have been left abandoned by the decline of the manufacturing sector. In response to this political transformation, Truss attempted to force through the policies she wished to pursue by winning popularity with voters, but she was thwarted by an unexpected reaction from the market. It is nothing if not ironic that Truss, who is essentially a market advocate, was forced to step down after being betrayed by the market.

Professor Ikemoto specializes in British and EU politics. Since the UK's withdrawal from the EU, he has been deepening his consideration of the best orientation for supranational political systems like the EU and the democratic politics of member states, and the direction of democratic politics in the new era. A graduate of The University of Tokyo's Faculty of Law, he holds a Ph.D. in Politics and International Relations from Oxford University. Following a term as an Associate Professor in Meiji Gakuin University's Faculty of Law, he assumed his current position in 2017.

Expert Opinions

Conservative Party Issues Lie in the Background of Truss's Failure



Takashi Narihiro

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In order to examine Liz Truss's failure, we need to look at the context in which she became prime minister. Here, we see the issues facing the British Conservative Party today.

One such issue is the fact that policies and persons not supported by the mainstream party membership are less likely to be selected. In the recent party leadership election, while Sunak won in the initial parliamentary party ballots, the party members supported Truss, and she won the ballot at the stage of voting by the party membership, the stage at which the final decision is made. The support for Truss shown by former Prime Minister Boris Johnson, who is popular with party members, and the unpopularity of former Finance Minister Rishi Sunak, who was seen to have betrayed Johnson, were also factors in the victory. Although the UK's economic malaise is clearly caused by its exit from the EU, "party member dynamics" have intensified, making it difficult to put forward policies that could overcome the opposition of the Brexit supporters who are the mainstream of the party's membership.

This situation has rendered the Conservative Party's policies related to economic growth unstable. Truss, like her predecessor, who was a proponent of large-scale investment without tax increases or increased social security contributions, brought with her an aspect of fiscal irresponsibility. Furthermore, she stepped back from aspects of the large-scale public investment that Johnson had promised and which received support during the 2019 elections, replacing it with policies that were expected to have an economic impact through significant tax cuts for the wealthy. This represented adherence to policies that the Conservatives have maintained since their return to power, but the effects of which are uncertain. There was even a question as to whether Truss would be excused this, not having "received baptism" in a general election.

Presumably another issue was the organizational problems that had existed since the 2010 elections. The party's leadership had increased the number of female and minority candidates, and an open primary system had been partially introduced. Combined with a string of losses in previous elections and expenses scandals, this changed the face of the Conservative Party membership dramatically. Truss and Sunak had only been elected for the first time in 2010, and Truss's ministers were also generally inexperienced in politics. Truss's failure was that, despite her inexperience as a politician, she did not position people in her cabinet who could rein in her own policies and function as leaders within the party. She also eliminated Sunak, her main rival in the party leadership race, and an advocate of fiscal prudence. The fact that the party was far from possessing any mechanism for considering market reactions in advance also led to a disregard for the review of the budget proposal by the OBR, the UK's independent fiscal watchdog.

The succeeding Sunak government is attempting to change course, adopting a stance of not increasing spending significantly but raising taxes if necessary. In Japan, it would be difficult for the Prime Minister to implement a policy requiring significant financial resources, such as a massive tax cut, on their own initiative, and it is therefore unlikely that Japan's Prime Minister will make the same mistake that Truss did. However, if extraordinary fiscal stimulus measures go too far, the market may react.

Professor Narihiro specializes in comparative politics, contemporary British politics, and European politics. His research focuses on party politics in the UK in comparison with other countries. He also conducts electoral analyses, for example a survey and study of the characteristics of the 2019 UK general election involving a preliminary analysis using panel data. Professor Narihiro completed coursework requirements for a doctoral degree in The University of Tokyo's Graduate School of Law and Politics, and has held his current position since 2010.

Expert Opinions

The UK Labour Party Seeks a “New Coalition” That Embraces Diversity



Kensuke Takayasu
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Jeremy Corbyn, the former leader of the UK Labour Party, was a cause of concern among the nation’s business and financial communities when he proposed a “big government” stance emphasizing social security and redistribution through taxation of the wealthy and large corporations. The party’s current leader, Sir Keir Starmer, has been working to restore confidence by sending a conciliatory message to the business and financial communities.

Concrete plans for “growth,” a key focus for the party, are yet to materialize. The Labour Party seeks to expand its fiscal policy, and, in fact, its growth strategy also includes proactive investment in measures addressing climate change. However, it also has no choice but to be cautious with regard to the scale of fiscal expenditure. As is evident from the example of the short-lived Truss

administration, which was criticized by the market for its imprudent borrowing plans, the ballooning of the current UK budget deficit as a result of pandemic responses and the continuing increase in the ratio of government debt to GDP despite a series of fiscal austerity measures leaves the government with little margin for public investment.

The Labour Party has long viewed “trickle-down” policies that favor a section of the wealthy stratum as problematic and seeks to realize growth through investment and distribution. However, whether the party can aptly respond to the high cost of living and how far the party will be able to go in improving wages and benefits for public sector workers, who represent a powder keg of discontent, is unclear, although certain proposals have been tabled. If the party fails in its responses, disappointment will undermine its strength.

The basis for the party’s gaining support for its policies is the formation of a “new coalition,” i.e., a coalition that supports the Labour Party. The Truss administration failed because it prioritized gaining popularity within the Conservative Party and viewed reality solely through a lens of convenience. The number of people struggling to make ends meet in the UK continues to rise. The Labour Party is striving to form new alliances and coalitions outside the party. It seeks to capture the votes of the Leave voters who originally supported the Labour Party by forging a practical relationship with the EU without rejecting Brexit. By eliminating the most left-wing factions that gained influence during the Corbyn era and distancing itself from the recent trade union strikes, the Labour Party is trying to win the support of ordinary voters, but it is also important that it finds a way to hold the party together.

It may be said that the UK was able to quickly change course because of the market’s immediate reaction to Truss’s policies. In the case of Japan, given that there has been no immediate rejection of the government’s policies by the market or the international community, if the government lacks the necessary prudence and prioritizes short-term popularity of a mere part of the society while fomenting external anxiety, it might fail in realizing the long-term interests of society before this is even noticed. It is essential that policymaking not fall prey to inward-looking thinking, but rather that it listens broadly to the voices in society and engages in dialogue with neighboring countries and the market.

Professor Takayasu specializes in comparative politics and political process theory. His research focuses on the political systems of Japan and the UK, including the parliamentary system, the Prime Minister/Cabinet system, and government/party relations. He seeks to elucidate the mechanisms of political power via methods including comparative analysis of the Japanese and British political systems. He entered a Ph.D. course in the Department of Government of the London School of Economics and Political Science (LSE), and took a Ph.D. in Political Science at the University of London/LSE. Professor Takayasu took his present position following terms as a Lecturer at the Graduate School of Law, Hokkaido University, and as Professor at the Faculty of Law, Seikei University.