"It is too early to say that we are 'out of the woods' "

The UK economy faces "a long period of healing", as it recovers from the recession, and the Government must ensure that it reduces the budget deficit severely, according to the Governor of the Bank of England.

Mervyn King warned that the huge budget deficit — set to hit around £178 billion in the current fiscal year — poses a tricky problem for the Bank because it requires financial markets to buy huge amounts of Government bonds, or gilts, to finance it. At the moment, the Bank has been buying up most of those gilts in a policy known as 'quantitative easing'. It is likely to stop its purchase quite soon, experts believe. If markets suspect that the Government is not serious in its stated intention to halve the deficit in four years, they could refuse to buy the gilts that the Government issues. This could lead to a slump in gilt prices, in turn pushing their yields up — and, with them, all sorts of long-term interest rates in the economy, including fixed mortgage rates.

"A massive sticking plaster"

Mr King said that the extraordinary degree of monetary and fiscal stimulus administered by governments and central banks world-wide represented little more than a "massive sticking plaster on the wounds". Turning his attention to the UK economy, Mr King said that our output fell by 5% last year (the biggest drop since 1931, incidentally) and by 10% compared to where it would have been, had the recession not happened. Recovery was starting, but it was gradual, he said. "There is a long period

of healing ahead. Although quarterly growth rates of GDP may soon turn positive in the UK, unemployment is likely to remain high. The sharp monetary squeeze resulting from the efforts by banks to contract their balance sheets is still casting a shadow over the future path of output and employment."

Mr King warned of an urgent need to re-balance the world economy to eradicate the huge surpluses and deficits of different countries (China and Japan in one camp, the USA and UK in the other). Otherwise, further financial crises could occur, he said. "The origins of the crisis lay in the inability to cope with the consequences of the entry into the world trading system of countries such as China, India, and the former Soviet empire — in a word, globalisation. The benefits in terms of trade were visible; the costs of the implied capital flows were not."

Mr King compared choices for economies to a game of sudoku, in which issues such as economic growth, trade deficits and employment levels are inter-related. "Sudoku for economists shows that countries cannot pursue incompatible economic policy frameworks for long."

The Governor once more called on the UK government to ensure that it took seriously the task of reducing the country's enormous budget deficit, "without which neither healthy growth nor financial stability are possible." He warned: "The patience of UK households is likely to be sorely tried over the next couple of years. There is little scope for growth in real take-home pay, which may remain weak even as output recovers."

"Recovery has been sluggish"

On the same day that the Governor was speaking, the head of the IMF warned that developed countries may slip back into recession if they abandon strategies deployed to battle the global financial crisis too early. Dominique Strauss-Kahn (pictured left) told reporters: "Recovery in private demand and employment are necessary conditions for governments to begin unwinding policies designed to support their economies, although the right timing depends on specific conditions in each nation.

"Recovery in advanced economies has been sluggish. We have to be cautious, because the recovery has been fragile. We are no longer at the edge of the abyss that loomed in early 2009, with all but a handful of Europe's economies now pulling out of recession, but it is less clear that we have reached safe ground. It's difficult to say the crisis is over until there is a sustainable private demand likely to make all of the public support useless." Mr Strauss-Kahn added that he saw a possible rise in unemployment in the near future. "It is too early to say that we are 'out of the woods'."

MPs critical of Government's Train to Gain scheme

One of the Government's flagship training schemes has been badly run, according to a committee of MPs. A report released last week by the Public Accounts Committee admitted that the scheme had helped 1.4 million people by 2009, but insisted that the mismanagement of the scheme raised serious concerns about its effectiveness.

Edward Leigh, chairman of the committee, said: "Despite providing work-based training for around 5% of the workforce, the Train to Gain programme has been mismanaged from the outset. Unrealistic targets were set in the first two years, only for the supply of training to be restricted as demand increased during the recession.

"The number of learners, the level of demand from employers and the capacity of training providers were at first all over-estimated. By the third year, demand for training, fuelled by substantially widened eligibility for the programme and by the recession, had increased to the point where the programme could no longer be afforded. Funding to training providers has been stop-start, with many now having to run down the capacity they had been encouraged to build up. Employers with new requirements are being turned away.

"What must happen now is for spending to be brought under control. In the light of experience gained over the last three years of what courses and qualifications have proved most valuable, funds need to be directed at the sectors with the most acute needs. With expenditure on Train to Gain totalling nearly £900 million by the end of 2008-09, it is sobering, to say the least, to learn that around one half of employers whose employees received training say that they would have provided similar training without any public subsidy."

A week before the Committee's report was published, the Policy Exchange 'think tank' concluded that the Train to Gain programme should be scrapped. A spokesman said: "Skills policy is too focused on meeting Government qualification targets, rather than delivering the skills that are needed. Train to Gain should be abandoned. Attempts should be made to incentivise employers who currently use external provision to develop in-house capacity. A small pot of money could be diverted from the Train to Gain budget to create a discrete strategic fund which employers could bid for to help develop this capacity."