Public finances: yet more tax rises ahead?

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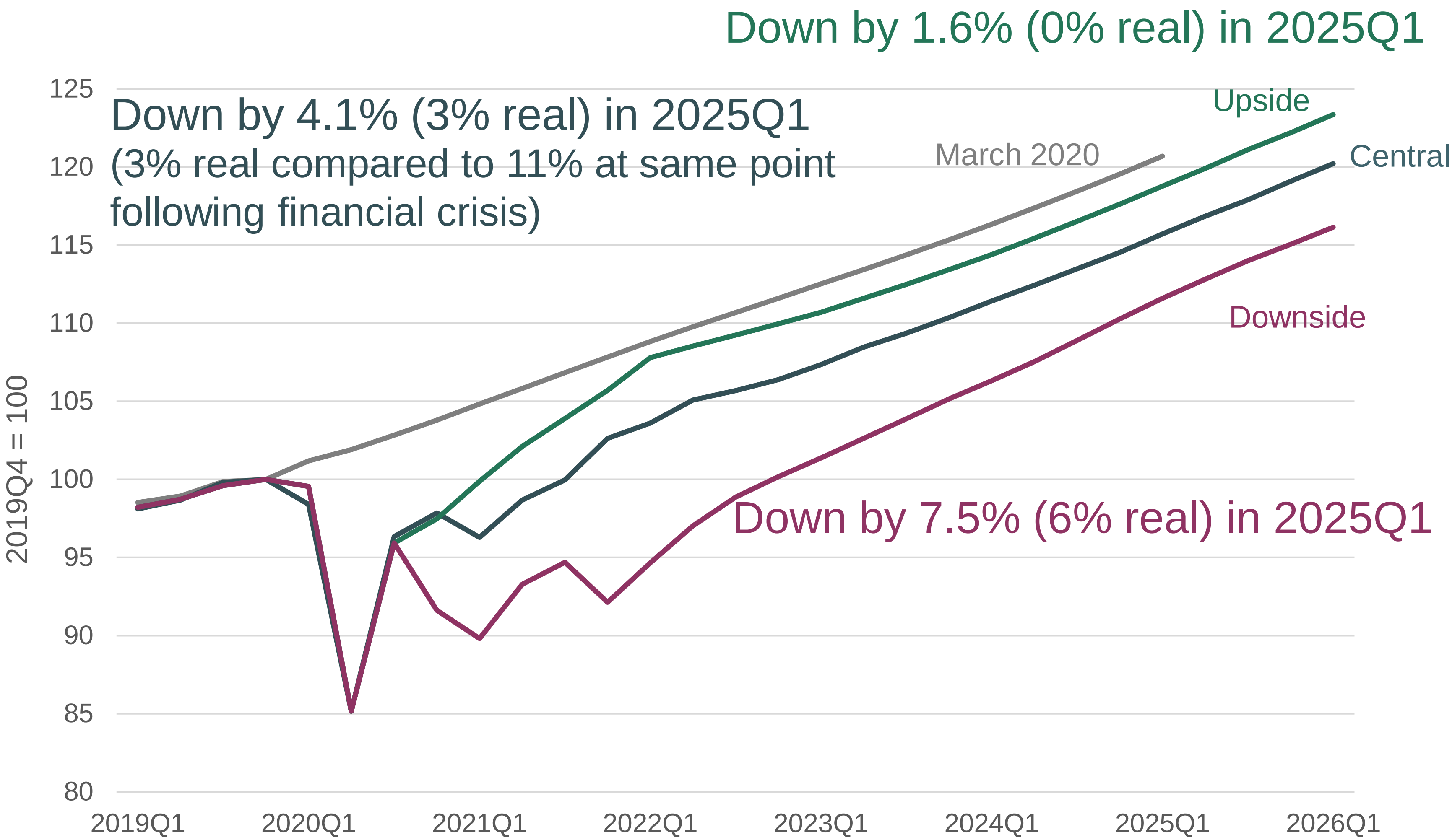
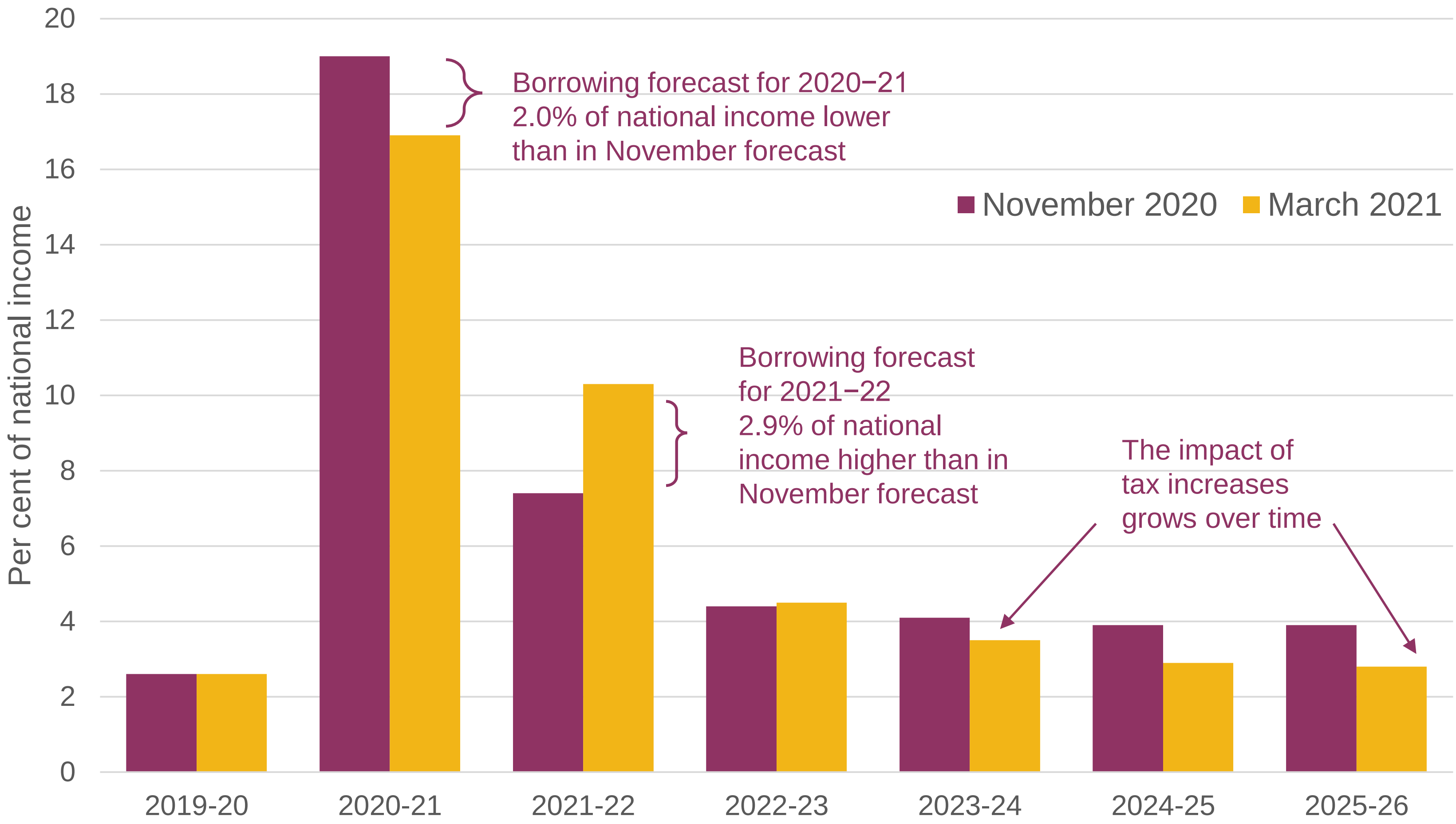
@TheIFS

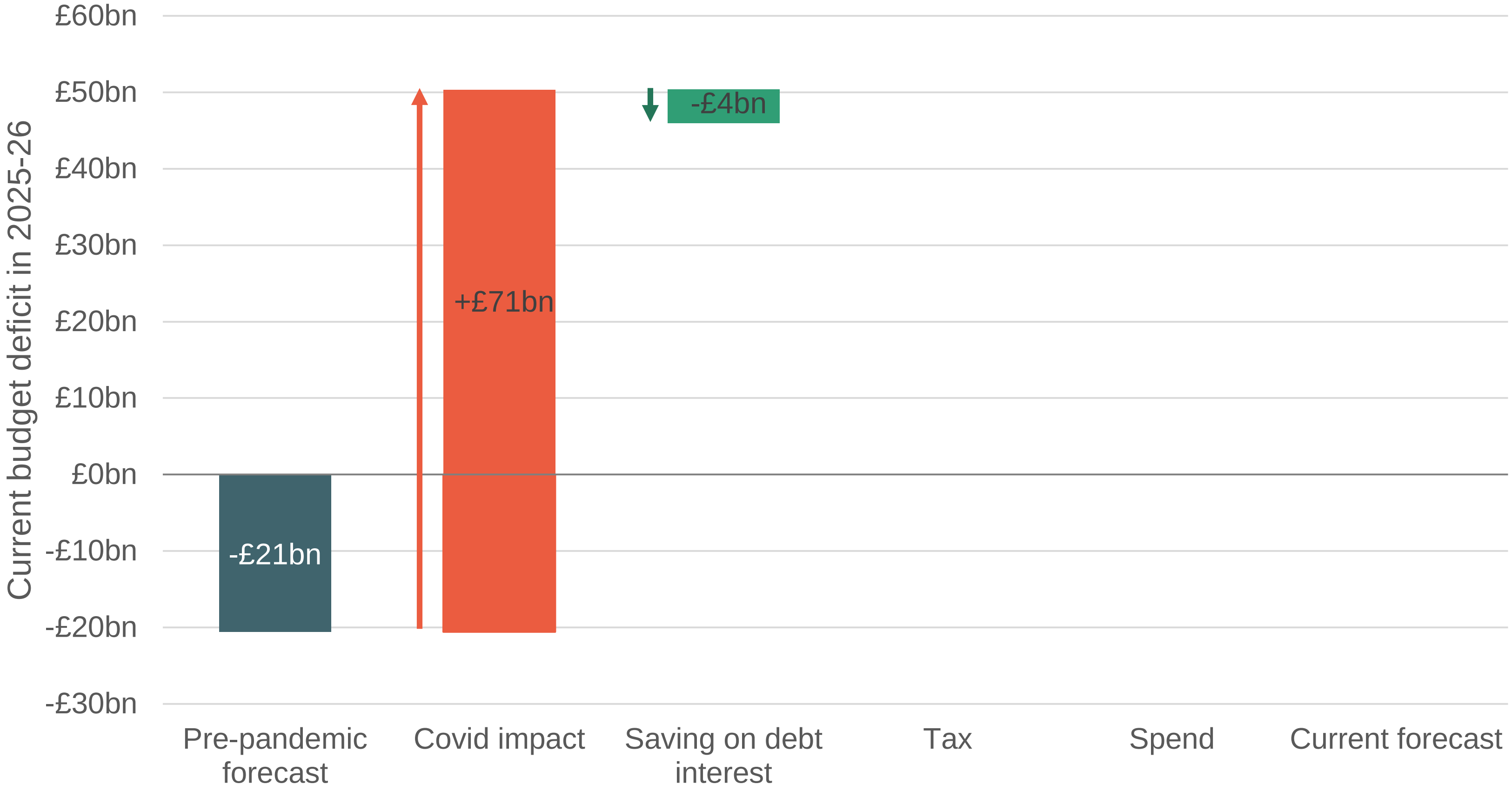
Permanent hit to nominal GDP



New support pushes borrowing up next year, later tax rises reduce it



Balancing the books before and after the pandemic



Note: cyclically-adjusted.

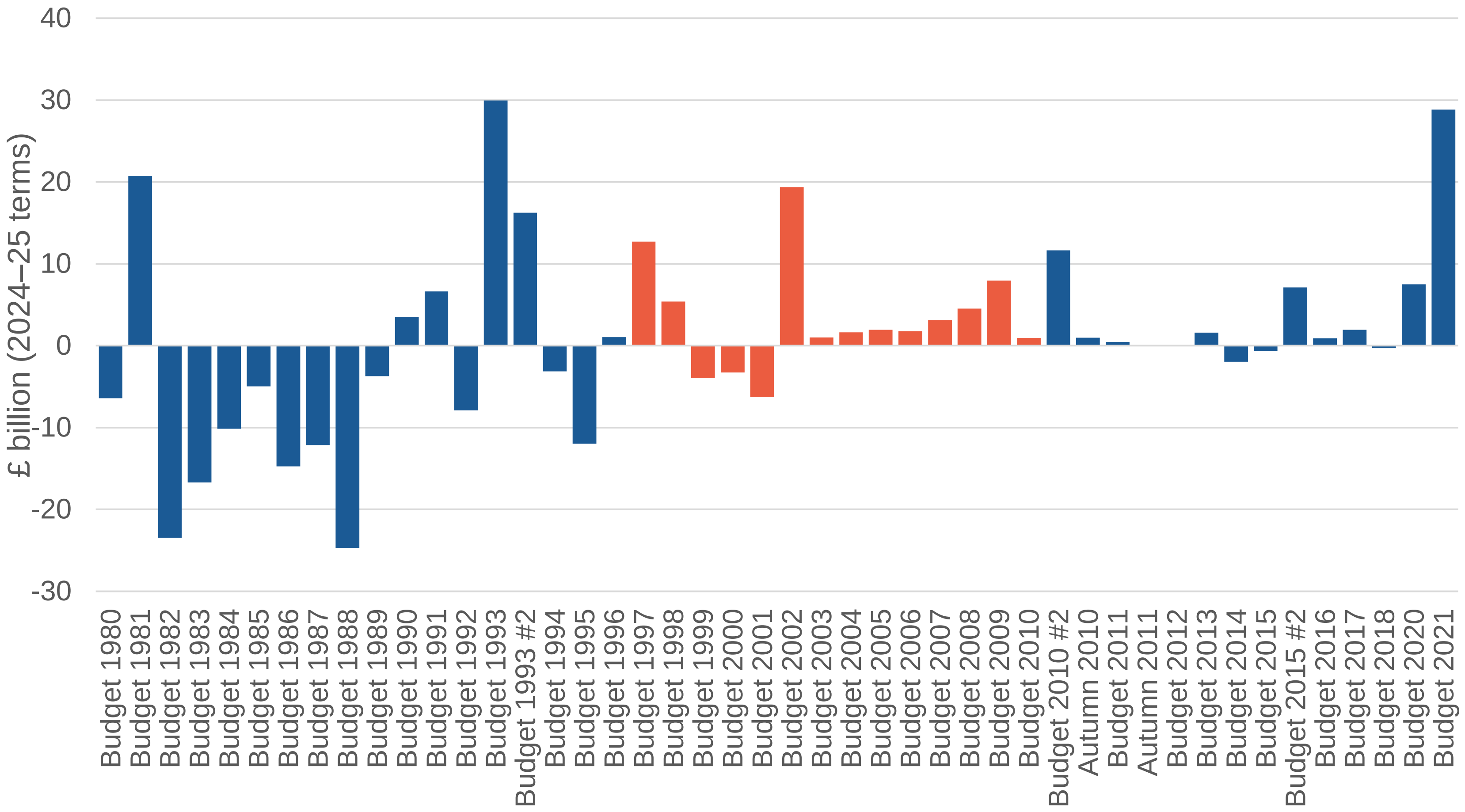
Debt interest risk

- Lower debt interest spending despite much more borrowing
- Not costless: much more exposed to rising interest rates or inflation
- Expansion of quantitative easing means additional debt effectively financed at Bank Rate
  - OBR forecast takes market expectations as of Feb 5, which were 0.5% for 2026Q1, this has since risen to 0.8%
  - +0.3ppt on all interest rates adds £7 billion to debt interest
  - just the change in 4 weeks for interest rates in 5 years time!
- Higher interest rates could be associated with stronger outlook for receipts, which overall would be good for the public finances

Balancing the books before and after the pandemic

Note: cyclically-adjusted.

Biggest tax rising Budget since Spring 1993



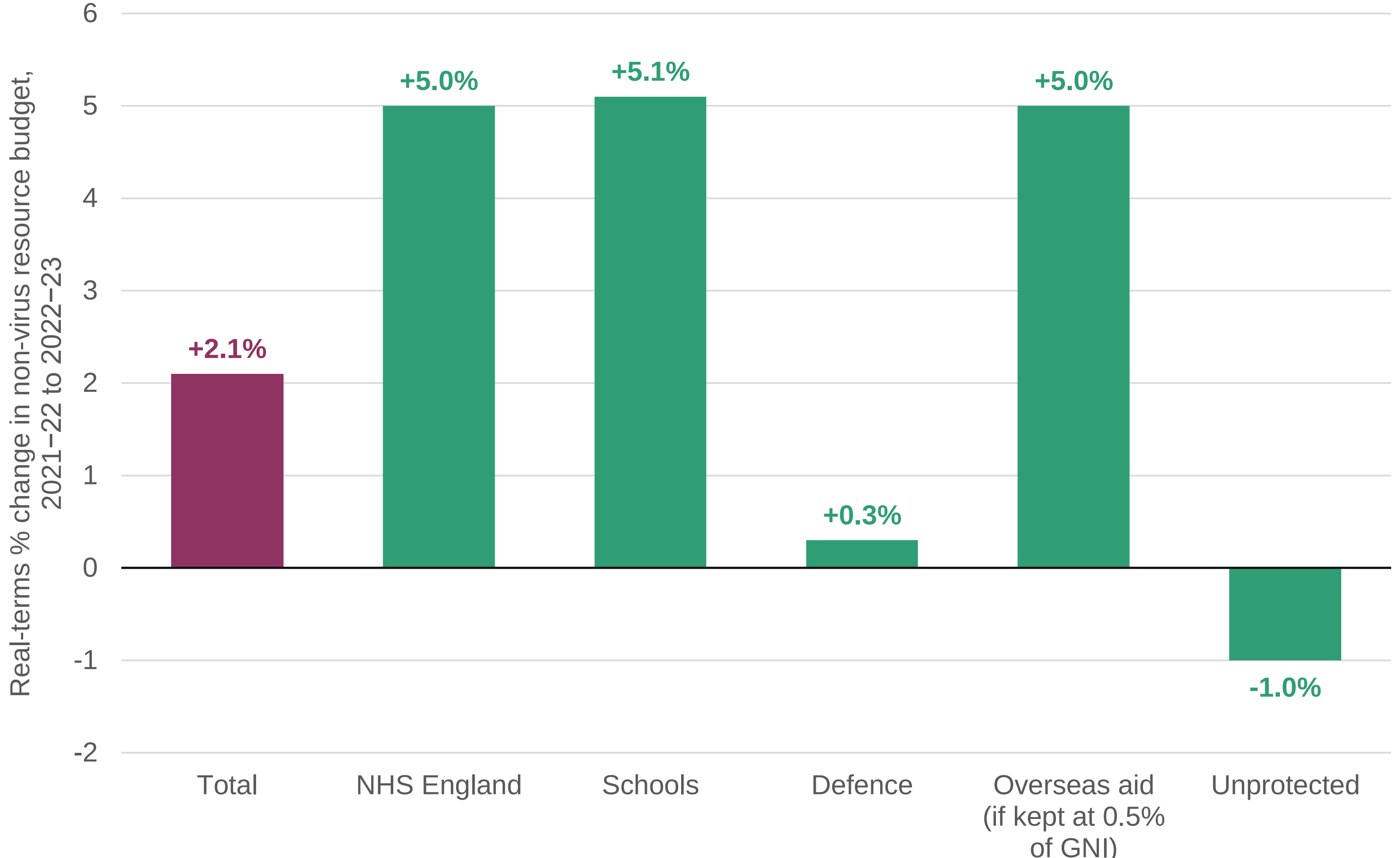
Balancing the books before and after the pandemic

Note: cyclically-adjusted.

Changes to non-virus resource budgets since last March

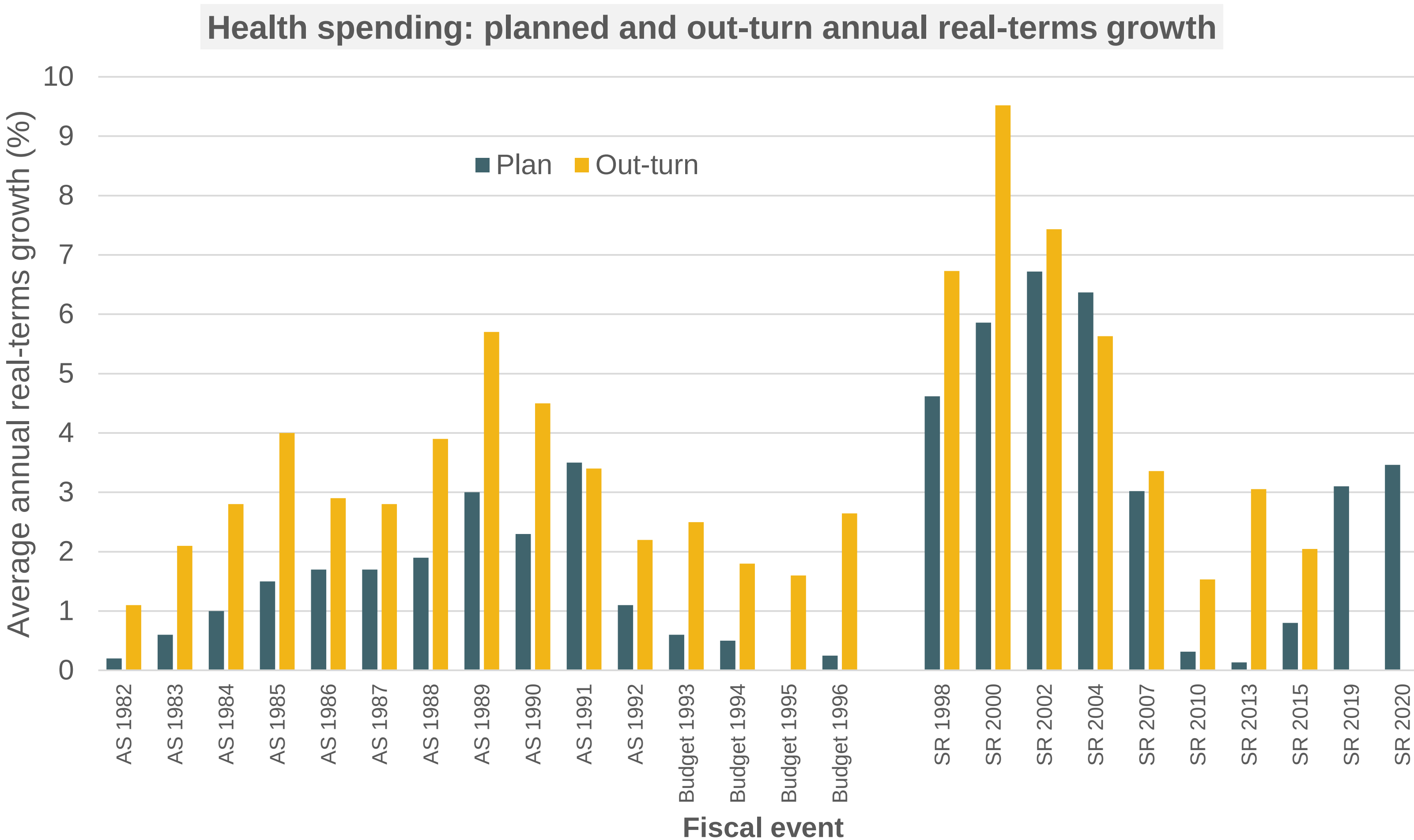
Note: Figures may not sum due to rounding. Source: OBR Economic and Fiscal Outlook, November 2020 and March 2021.

Some public services are facing a budget squeeze in 2022–23



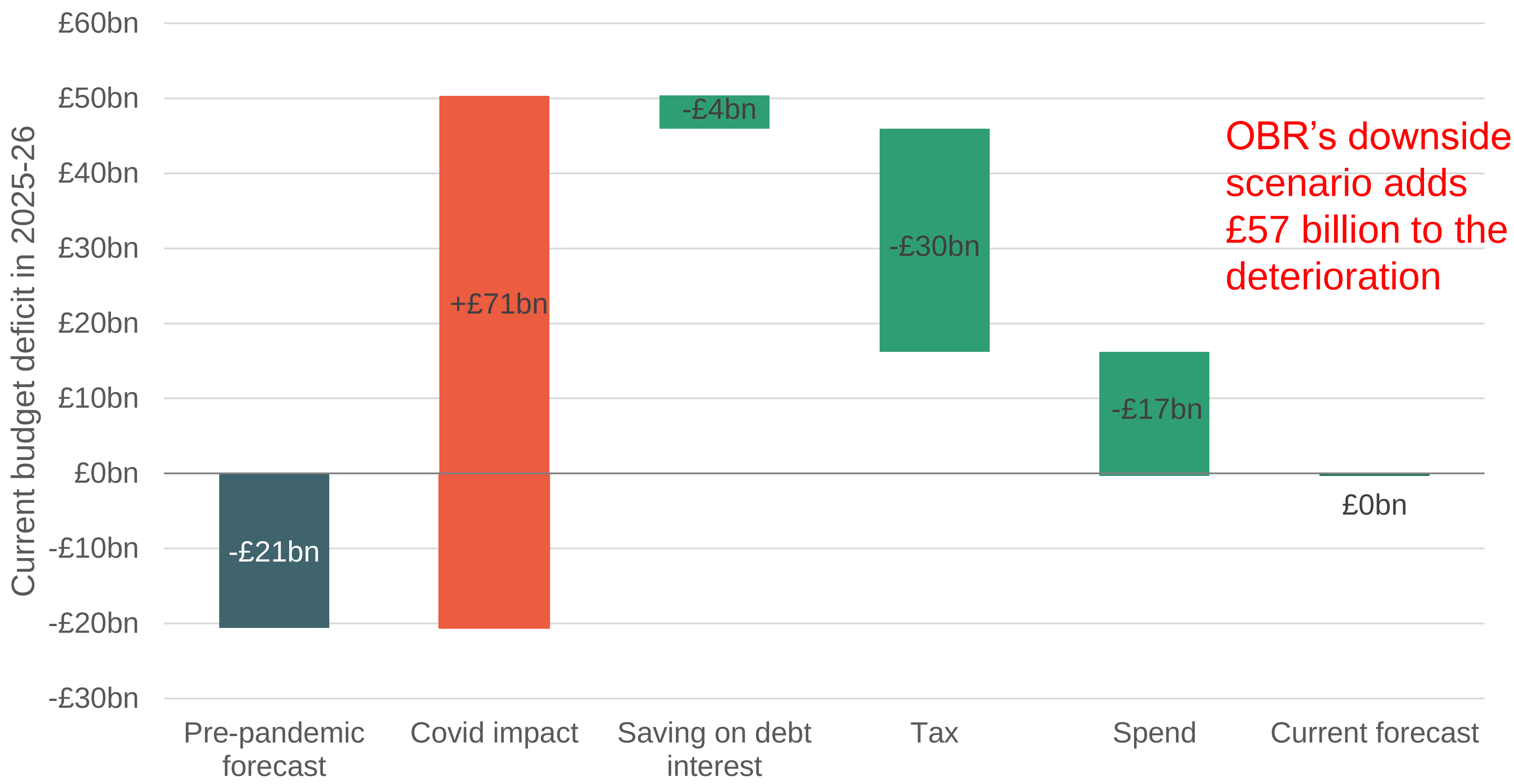
Source: OBR Economic and Fiscal Outlook, March 2021.

NHS spending plans are almost always topped up



Note: AS denotes Autumn Statement; SR denotes Spending Review. Figures refer to average annual real-terms percentage growth over the planning period (typically three years). For example, SR 1998 covered 1999−00, 2000−01 and 2001−02. Planned real growth rates are based on contemporaneous forecasts for the GDP deflator; out-turns use the November 2020 GDP deflator series. Out-turns are not yet available for SR 2019 and SR 2020. Source: IFS calculations using HM Treasury Budgets, Autumn Statements, Spending Reviews and Public Expenditure Analyses (various), with figures for AS 1982 to Budget 1995 taken from IFS Election Briefing 1997.

Balancing the books before and after the pandemic



Note: cyclically-adjusted.

Fiscal rules and fiscal tightening

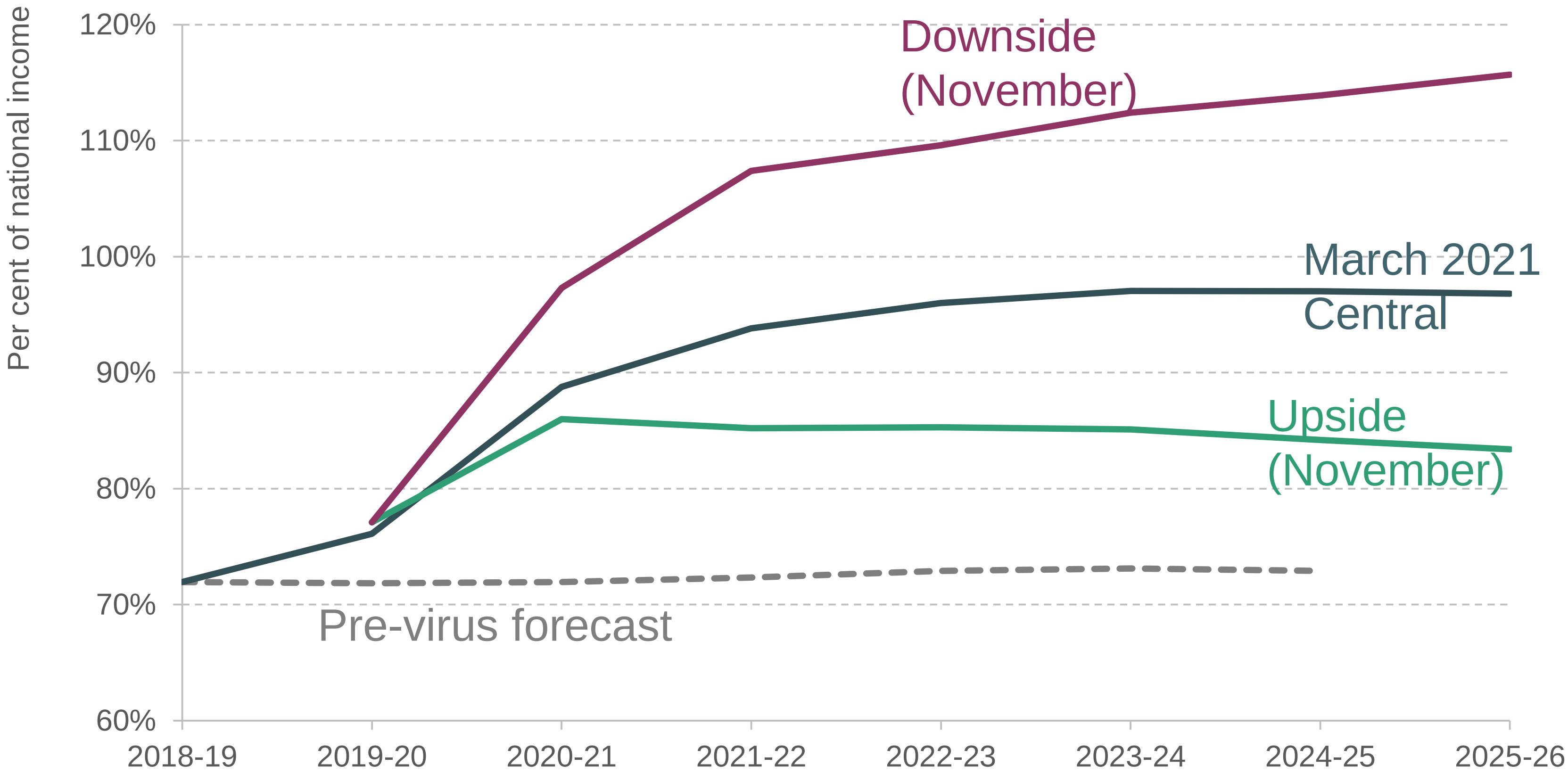
"in normal times the state should not be borrowing to pay for everyday public spending"

- much to commend it: underpinned Gordon Brown's golden rule and George Osborne's original fiscal mandate
- on course to meet under central scenario
- £57 billion more fiscal tightening needed under downside scenario

"over the medium term, we cannot allow our debt to keep rising"

- true over the longer-term
- on course to meet under central scenario

Debt just about stabilised



Notes: Net debt excluding the Bank of England shown.

Fiscal rules and fiscal tightening

"in normal times should not be borrowing to pay for everyday public spending"

- much to commend it: underpinned Gordon Brown's golden rule and George Osborne's original fiscal mandate
- on course to meet under central scenario
- £57 billion more fiscal tightening needed under pessimistic scenario

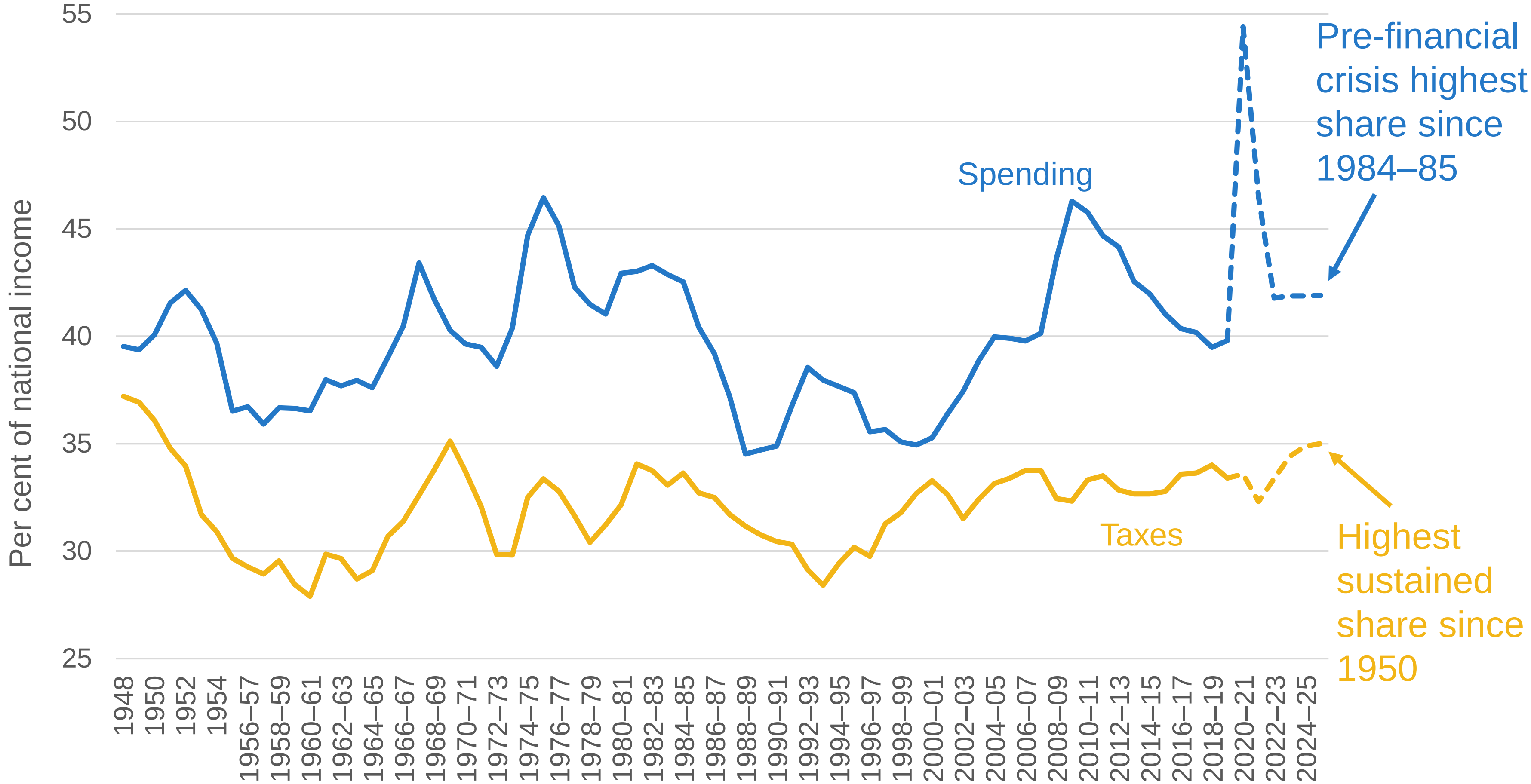
"over the medium term, we cannot allow our debt to keep rising"

- true over the longer-term
- on course to meet under central scenario
- £44 billion more fiscal tightening needed under downside scenario

"take advantage of lower interest rates to invest in capital projects that can drive our future growth"

- absolutely if borrowing locked in at low rates
- investment spending already planned to rise to highest sustained level of last 40 years: challenge is to spend it well

Tax & spend elevated as a share of national income



Conclusion: yet more tax rises coming?

- Dramatic worsening in economic outlook in last year
- Enormous package of support across 2020–21 and 2021–22
- Subsequent tightening might be sufficient to deliver current budget balance and stabilise debt
- But
  - biggest tax raising Budget since 1993: will these measures happen?
  - receipts hugely uncertain and interest rate rises could be painful
  - plans predicated on spending after March 2022 now being lower