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# Eliminating the deficit in this parliament?

Carl Emmerson

Presentation at IFS Public Finance Lecture, London

7 January 2015



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# Deficit to be eliminated by 2018?

- March 2015 Budget forecast an overall surplus in 2018–19
- Before the general election the Prime Minister stated:
  - “There’s a balanced plan to clear the deficit….. by 2018 we’ll be running a surplus”
  - David Cameron, Conservative Party Manifesto Launch, 14 April 2015 (http://press.conservatives.com/post/116374071635/david-cameron-speech-conservative-party-manifesto)

- New fiscal mandate requires the government to achieve a surplus on the headline public finances by 2019–20
  - and maintain a surplus thereafter
  - unless economic growth falls below 1%



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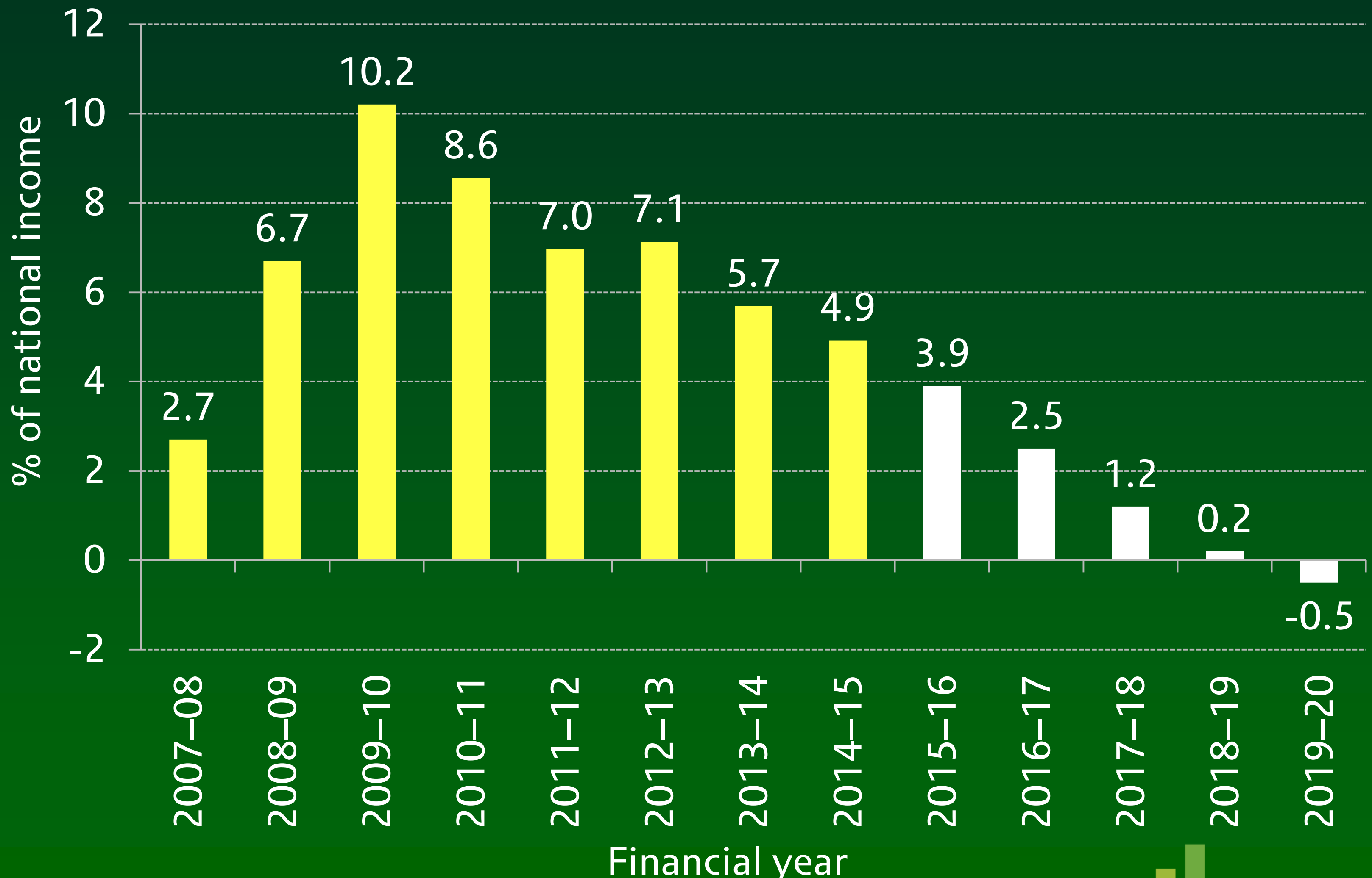
# Eliminating the deficit in this parliament?




Source: Office for Budget Responsibility.



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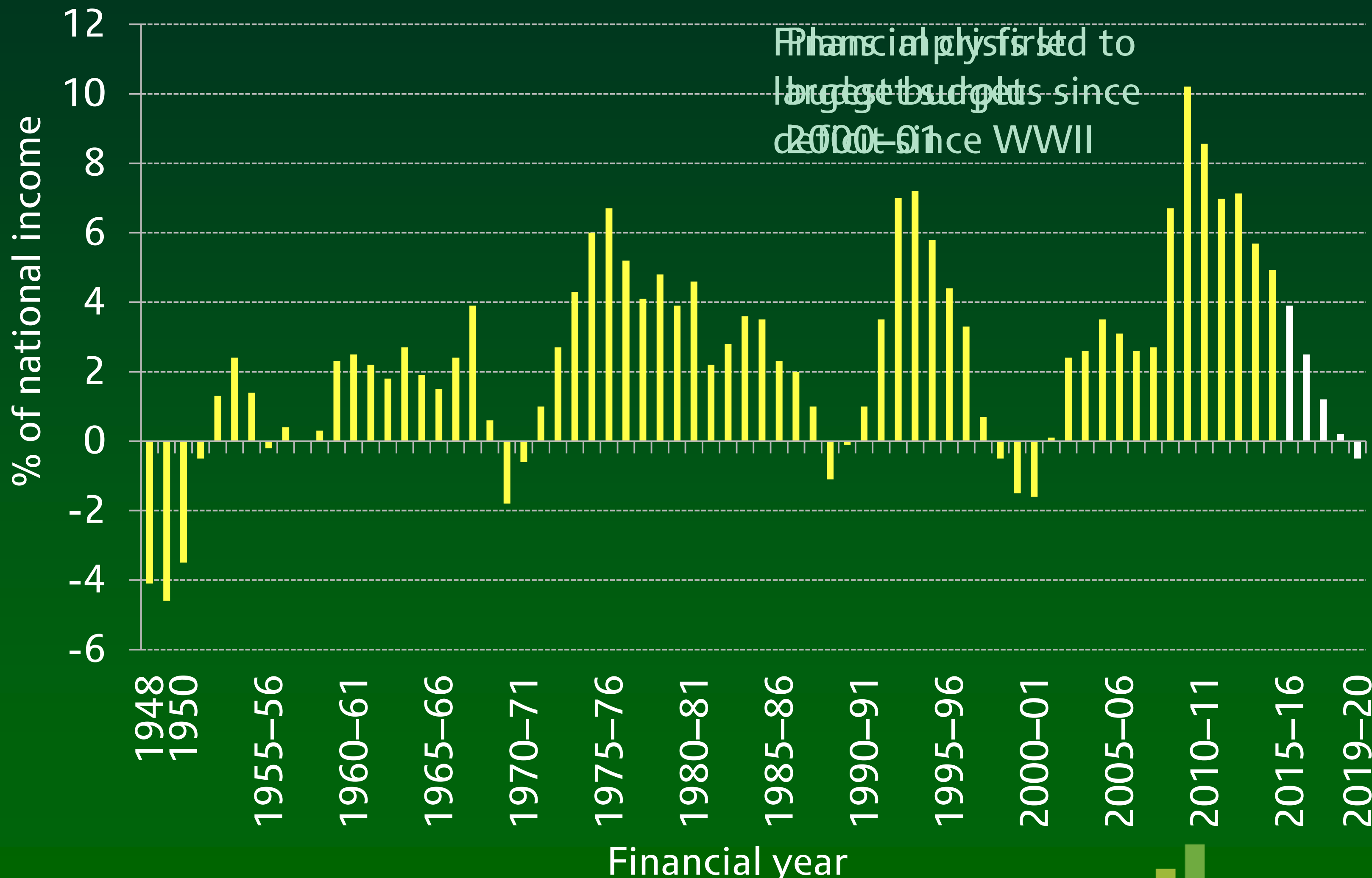
# Eliminating the deficit?






Source: Office for Budget Responsibility.

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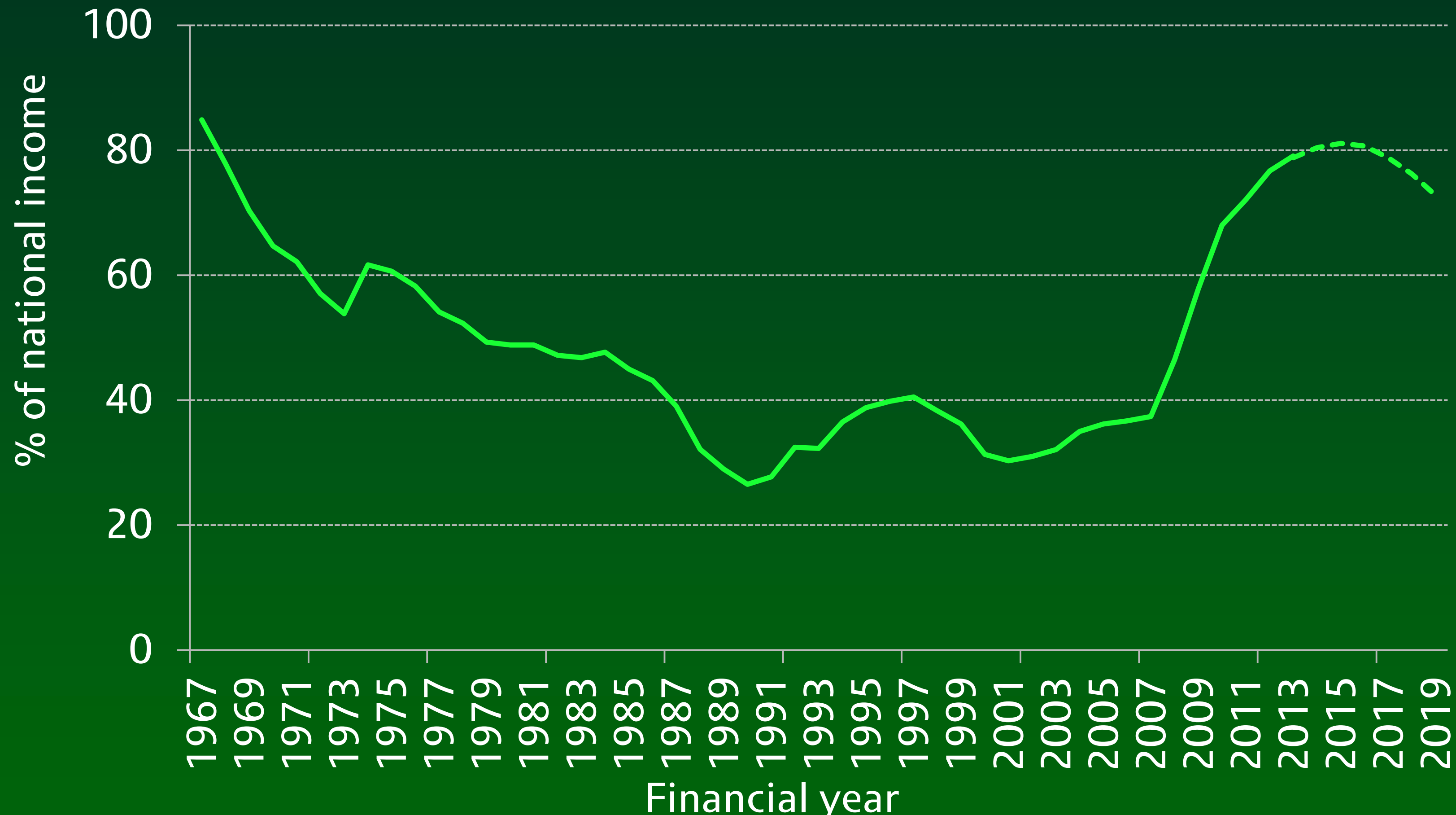
# Public sector debt high by recent historical standards






Notes and sources: see Figure 5.2 of The IFS Green Budget: February 2015.

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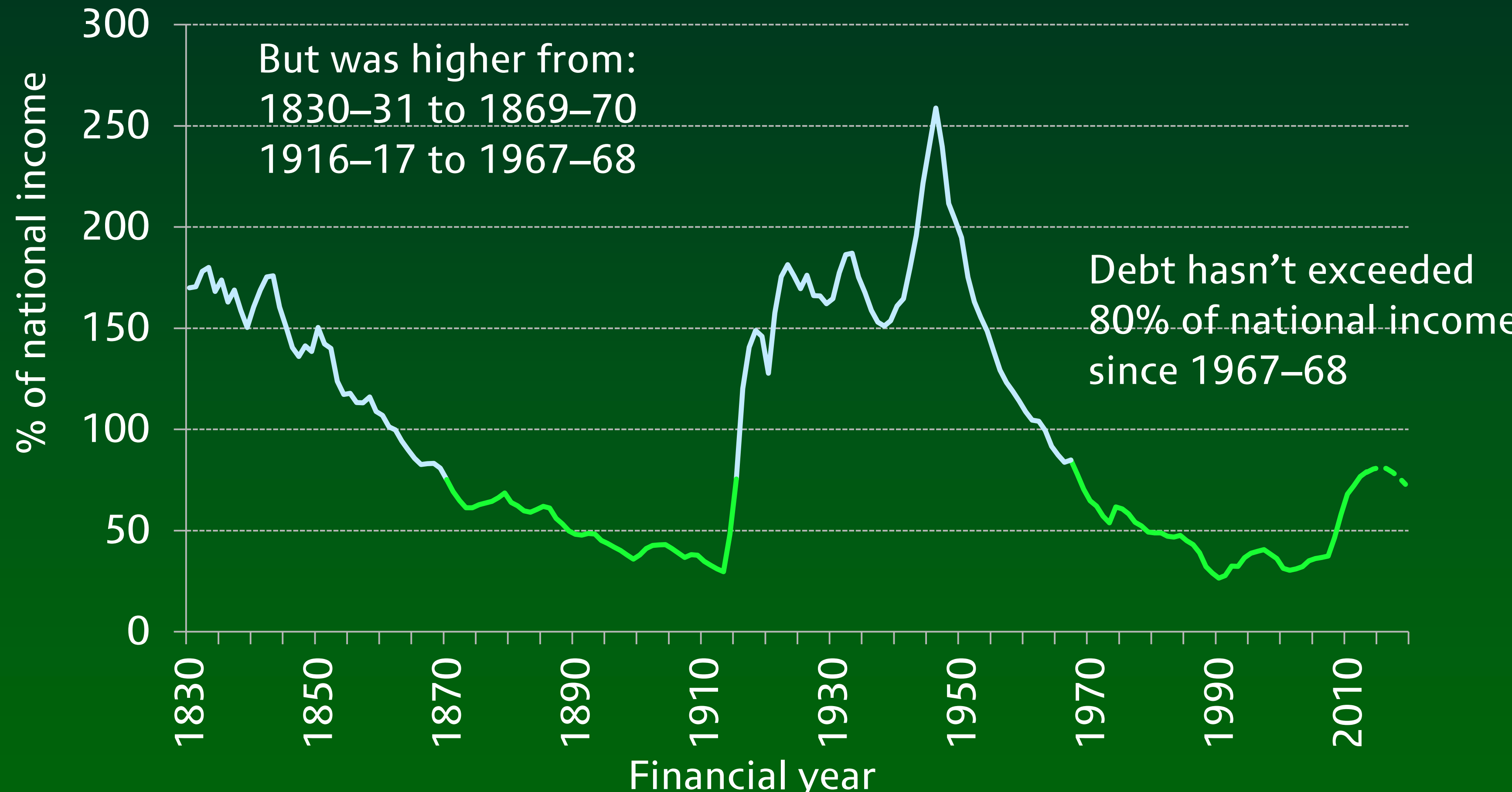


Notes and sources: see Figure 5.2 of The IFS Green Budget: February 2015.



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# Is a budget surplus always a good idea?

- All else equal lower debt would
  - reduce debt interest payments
  - provide greater scope to increase debt in the event of an adverse shock
- But governments might want to borrow in some periods:
  - investment spending
  - output stabilisation
  - adjusting gradually to shocks
  - forecast errors
  - tax-rate smoothing



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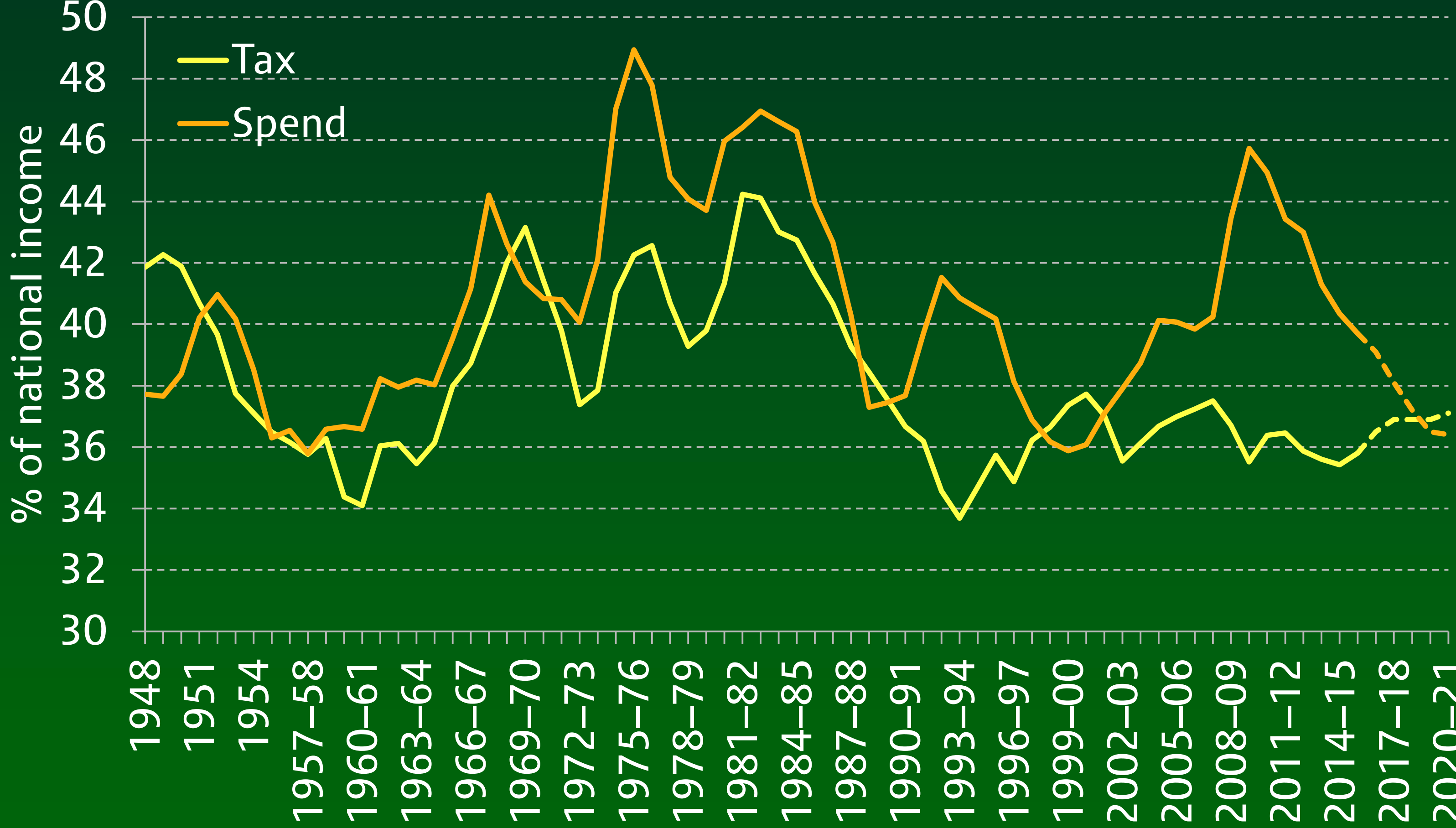
# Deficit to be eliminated with tax rises and larger spending cuts






Source: Office for Budget Responsibility.

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# Significant tax rise over the next few years

- July 2015 Budget (£15.9bn of tax rises, £9.4bn of tax cuts)
  - increase in tax on dividend income (£2.0bn)
  - increase in insurance premium tax (£1.7bn)
  - increase in vehicle excise duty (£1.4bn)
  - restriction of pension tax relief for those on high incomes (£1.3bn)
  - restriction of interest deductibility on buy-to-lets (£0.7bn)

- November 2015 Autumn Statement (£7.5bn tax rise)
  - apprenticeship levy on employers with large paybills (£3.1bn)
  - raising of referendum threshold for council tax rises (£2.2bn)
  - increase in stamp duty for second homes & buy-to-lets (£0.9bn)



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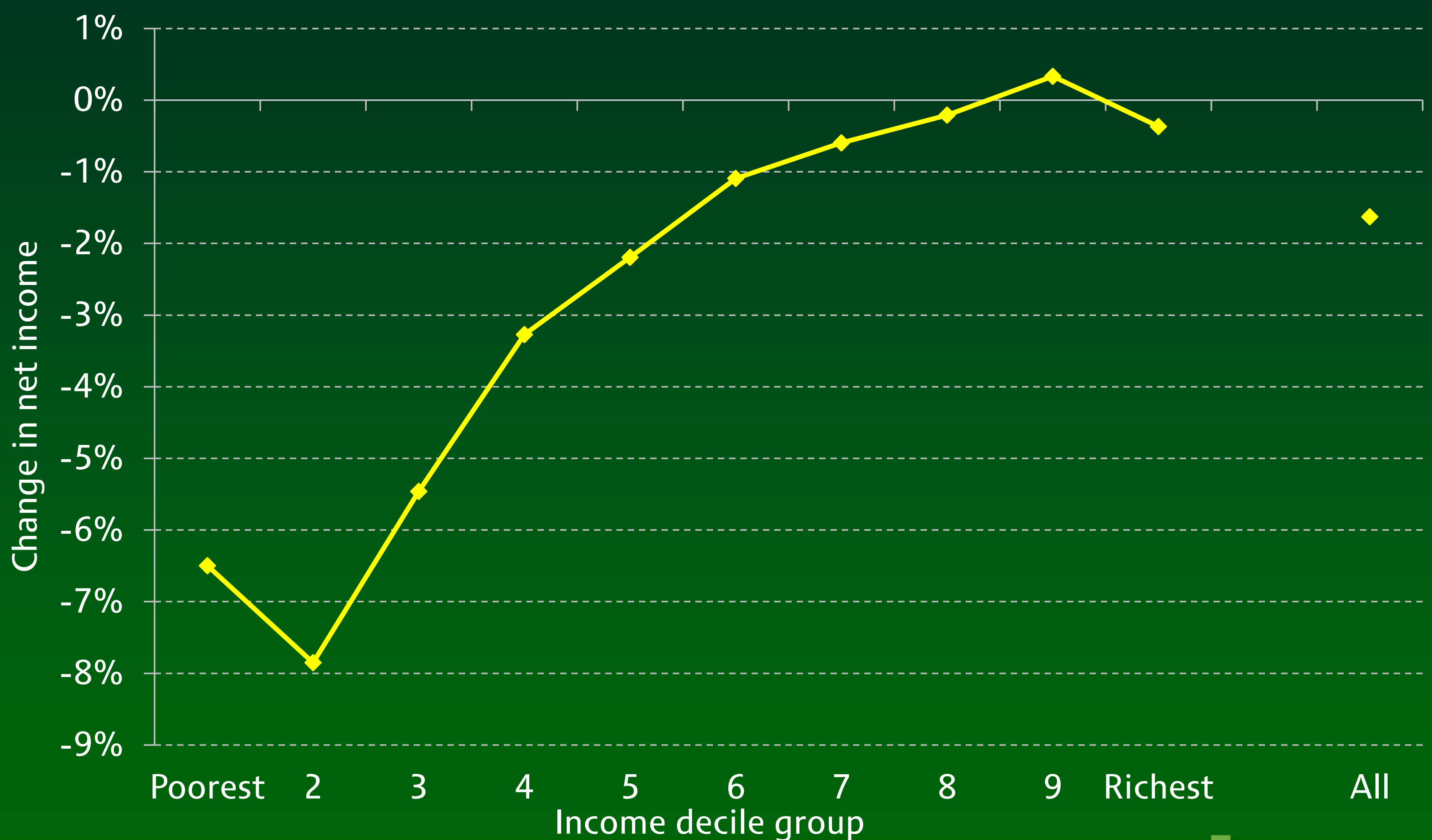
# Significant cuts to working age benefits

- Government still planning £12bn cut to annual benefit spending by end of the parliament
  - but less than half delivered by 2017–18
  - £4bn from freeze to 2020, £4-5bn additional cuts to universal credit, £1½bn cuts to housing benefit spending (plus other smaller changes)
- Benefit spending excluding state pensions in 2020–21 forecast to be at its lowest as a share of national income for 30 years

# Long-run impact of tax and benefit changes

## All changes introduced May 2015-April 2019 fully in place




Note: Assumes full take-up of means-tested benefits and tax credits.
Source: Hood (2015).



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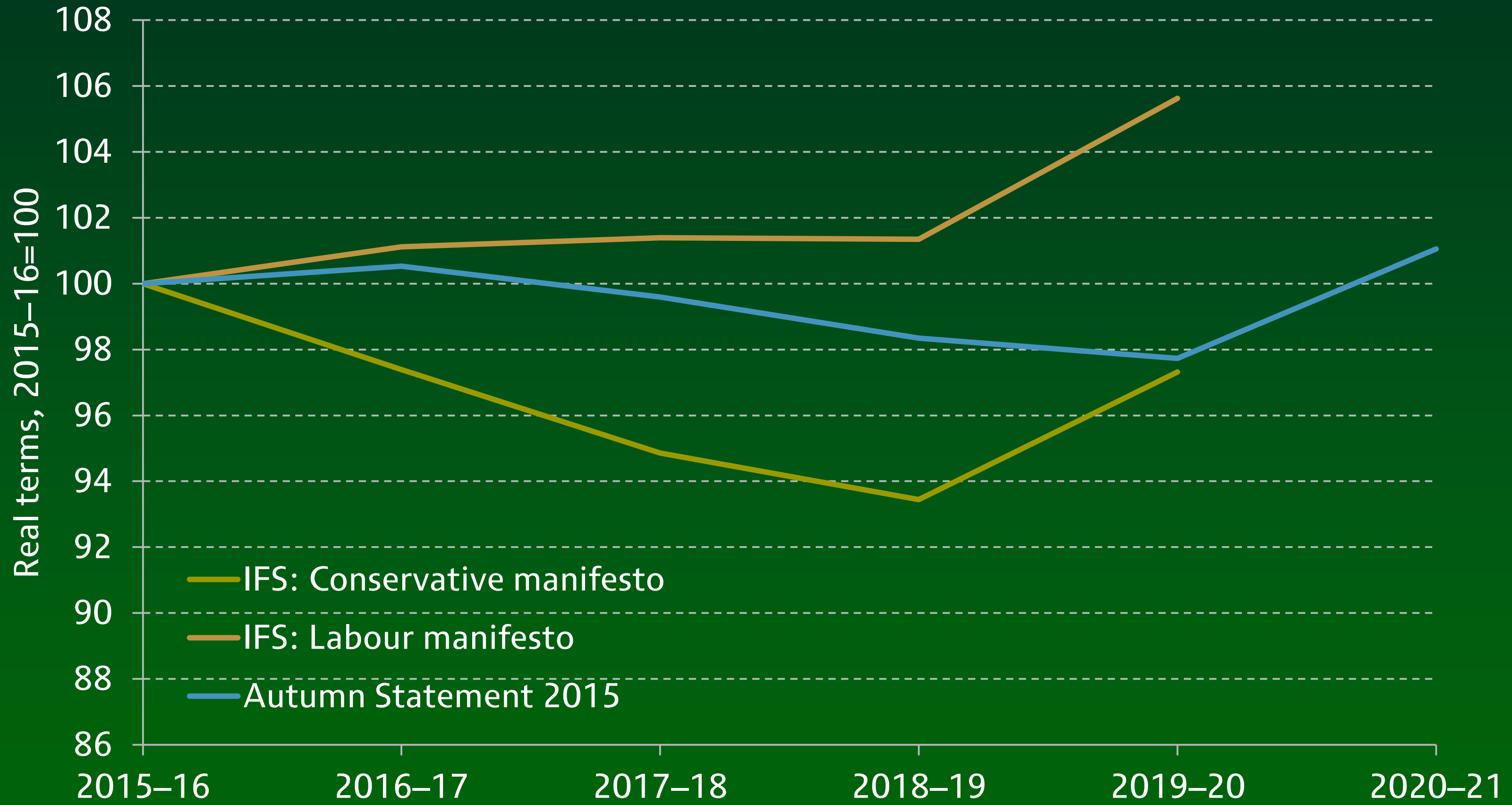
# Change in departmental spending






Notes and sources: Crawford, *et al* (2015).

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# Capital spending to rise, day-to-day spending to be squeezed

- Departmental spending to be cut by 2% in real terms by 2019–20: 12% cumulative cut since 2010–11
- Day-to-day spending across all departments set to be cut by 3% in real terms by 2019–20: 12% cumulative cut since 2010–11
- Departmental capital spending is to be increased by 5% in real terms up to 2019–20  but was cut over the last parliament
  - 2010–11 to 2015–16: cut by 17%
  - 2010–11 to 2019–20: set to be cut by 13%



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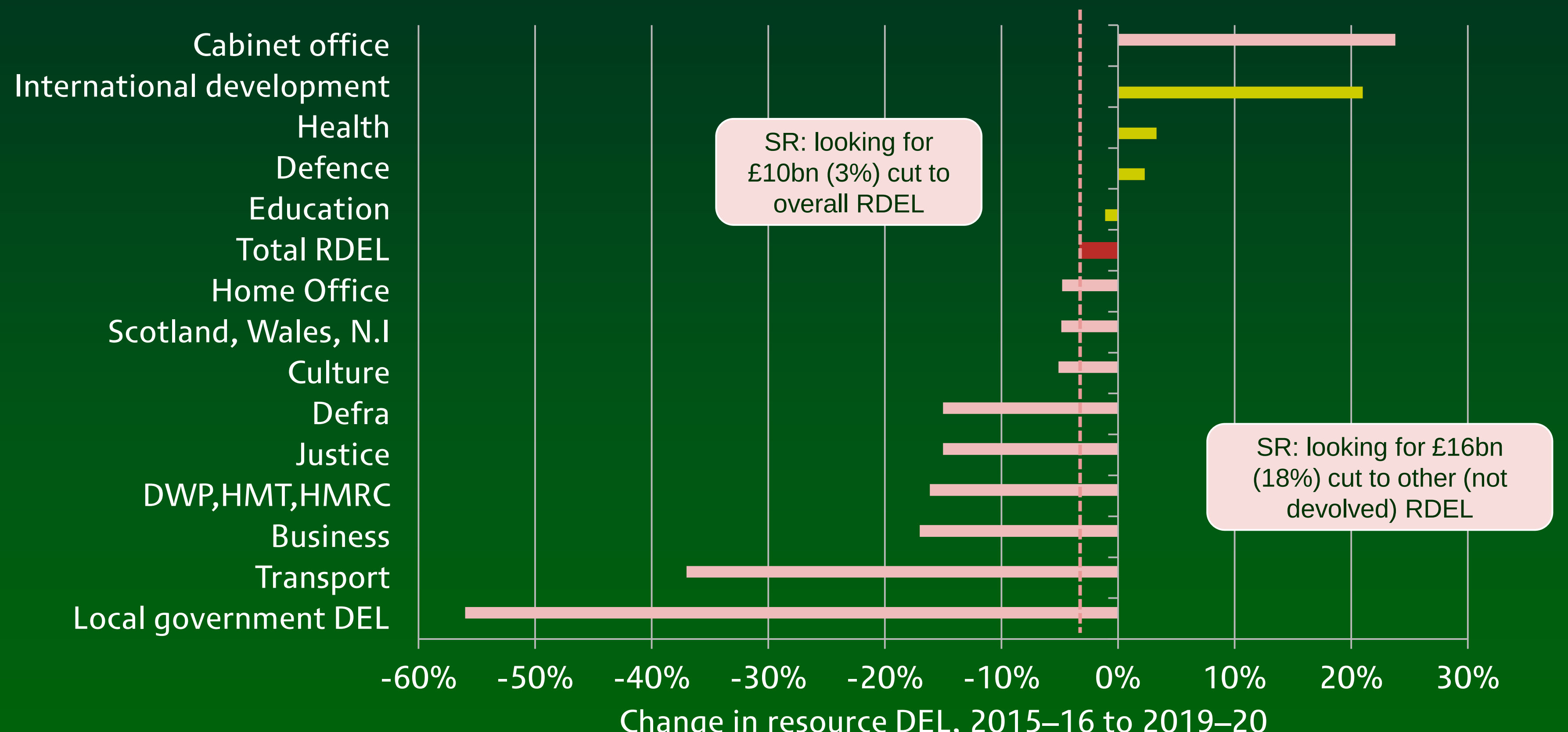
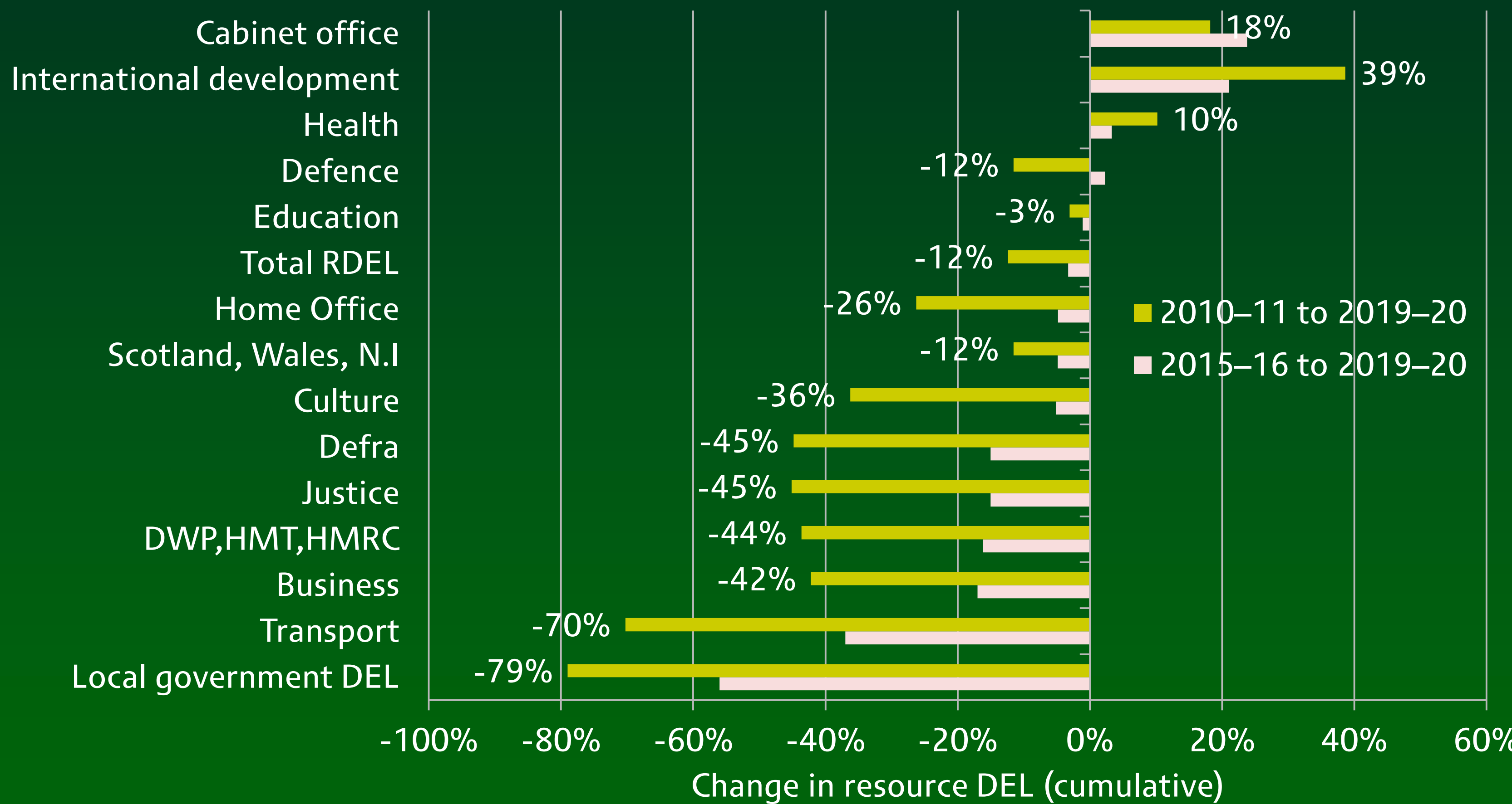
# Day-to-day spending cuts: 2015–16 to 2019–20




HMT estimates councils' spending power to be reduced by 7%, on average. But could vary substantially across England.

# Day-to-day spending cuts since 2010–11



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# Summary

- New fiscal mandate requires budget surplus from 2019–20 onwards
  - unless growth drops below 1% per year
  - advantages to reducing debt-to-GDP ratio, but there are reasons in favour of government borrowing in at least some years
- Plans imply the fiscal mandate being met
  - significant tax rises and cuts to working-age welfare
- Total day-to-day spending on departments to be cut less quickly over this parliament than last
  - but many departments still facing large cuts: e.g. transport and justice



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