Through a glass, darkly: Uncertain outlook for the public finances

16 February 2021
Economic scarring could keep borrowing elevated for years

A look ahead to the March 2021 Budget
This year’s borrowing highest outside the two World Wars

Source: Office for Budget Responsibility.

A look ahead to the March 2021 Budget
Underlying debt continues to rise in two of the three scenarios.

A look ahead to the March 2021 Budget

Notes: Net debt excluding the Bank of England shown.
Bringing debt to its highest level in more than half a century

Debt in per cent of national income

Notes: Net debt (PSND) shown.
But servicing the debt is cheaper than it has been in three centuries

Debt interest as a per cent of revenues

Notes: Debt interest net of APF from 2009.
The long-term trajectory of debt

A look ahead to the March 2021 Budget

Notes: Illustrative paths for debt excluding the Bank of England
The November Spending review pencilled in cuts to previous plans

<table>
<thead>
<tr>
<th>Year</th>
<th>Change in Billions</th>
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<tbody>
<tr>
<td>2020-21</td>
<td>£251bn</td>
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<tr>
<td>2021-22</td>
<td>£48bn</td>
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<tr>
<td>2022-23</td>
<td>-£9bn</td>
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<td>2023-24</td>
<td>-£12bn</td>
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<tr>
<td>2024-25</td>
<td>-£12bn</td>
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Change on Budget 2020 plans (today’s terms)

A look ahead to the March 2021 Budget
Expect an increase in spending post-pandemic

- Cuts to previous spending plans of £12bn likely difficult to deliver
- ½ year of schooling lost: normal cost of >£30bn a good benchmark; inaction could hit revenues by much more
- Many additional demands on the NHS:
  - Poorer population health
  - Backlog of planned care: 5.3m fewer referrals since April
  - Pandemic preparedness: PPE, track-and-trace, additional capacity
- Growing public demand for other spending?
  - Keeping £20 per week UC increase ≈£6½ bn a year
  - Cost pressures on Local Government services: >£2bn/year by 2025
  - Social care
A look ahead to the March 2021 Budget

Where might this leave the current budget deficit in 2024-25?

- Baseline: £46bn
- Cuts not deliverable?: £12bn
- Continue UC uplift?: £7bn
- LG cost pressures?: £2bn
- Backlogs and additional demand
- Economic uncertainty

Optimistic scenario: - £63bn
Pessimistic scenario: + £55bn
So what should the Chancellor do?

- In the short run: Borrowing cheap, CX can relax about the deficit
  - Spending that makes recovery more complete likely to pay off

- In the medium run
  - Lasting increase in spending likely
  - Debt elevated for decades; interest rate risk increased
  - Don’t forget ageing: OBR estimates increase in annual spending on pensions, health and social care ≈£39bn per decade
  - Net tax rises (even more) likely
    - Much uncertainty, but £60bn plausible to “balance the books”
    - Any permanent giveaways would add further to this bill