

The economic and political horizon Implications for the UK's public finances

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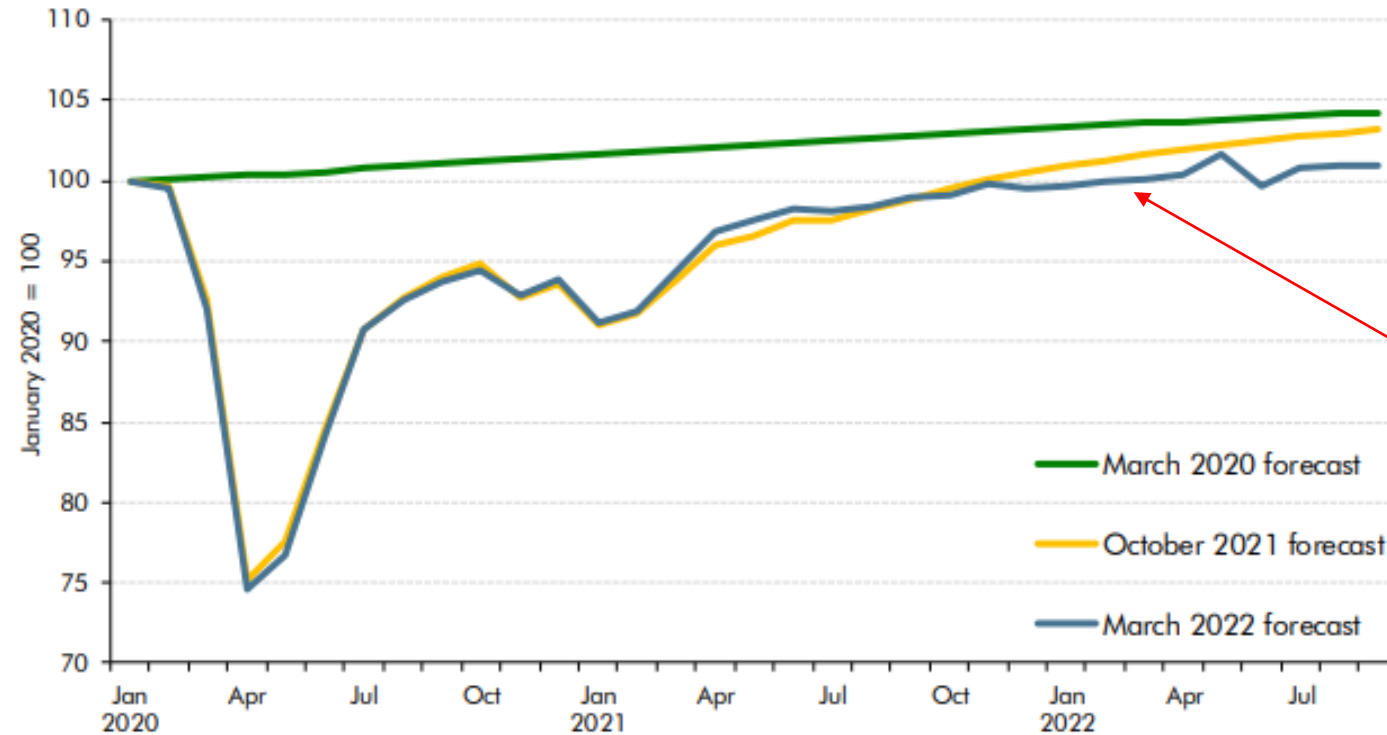
Spring Statement 2022

- Outcome of economic impacts over 13 years, notably the 2008 banking crisis, Brexit and Covid-19
- Also, the outcome of the particular relationship between the PM and the Chancellor, representing different elements of contemporary Conservatism
 - PM: increase spending and cut taxes
 - Chancellor: maintain fiscal discipline and bring down the deficit
- The 2021 Budget and Spending Review were a distinct move away from 'Thatcherism' (as a Conservative dominant philosophy) towards something more 'Heathite' or even social democratic

The Economy

- Growing more strongly than expected earlier in the year
 - Though Ukraine conflict will surely reduce GDP growth
- Longer term [permanent] hit from Covid (-2%) and Brexit (-4%) now built in to base unless policy changes are made (OBR estimates)
- Deficit to fall leading national debt to level off – though well above levels of the early 2000s
- Inflation expected to rise 8-9 (10?) per cent then fall back to target
 - May impact on debt interest costs
- Unemployment largely avoided by furlough and loans to companies, now falling and expected to fall further

UK GDP, January 2020 to Summer 2022



Note: This chart shows our October 2021 forecast for the monthly real GDP release from the ONS. It is slightly higher than the forecast published in Chart 2.10 of the October 2021 EFO, which was for real GDP, adjusted downwards for apparent measurement issues. We explained the adjustment in the footnote on page 42 of that report.
Source: ONS, OBR

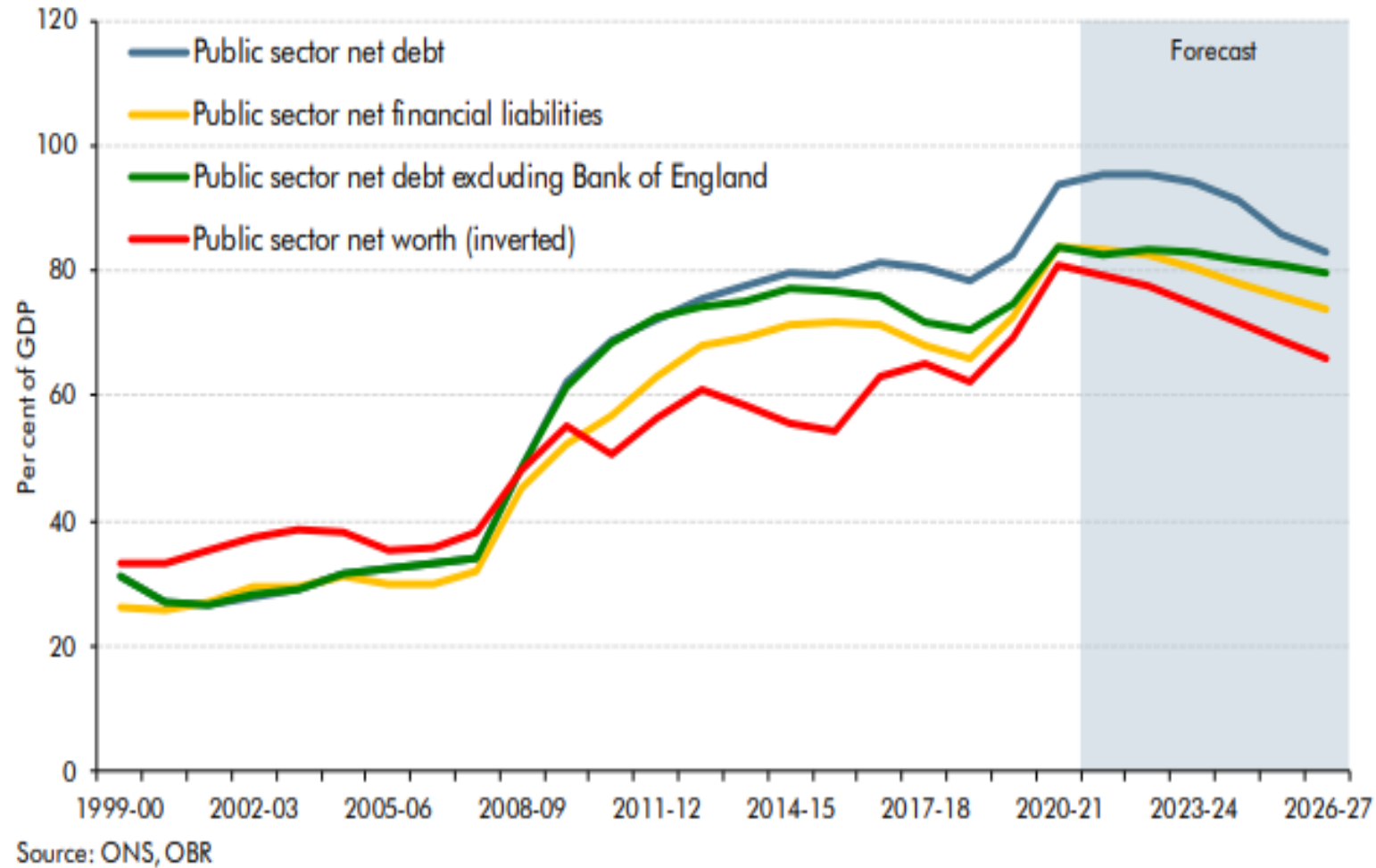
Return to GDP of January 2020, though below pre-Covid expectations

Overview of the economy (forecast)

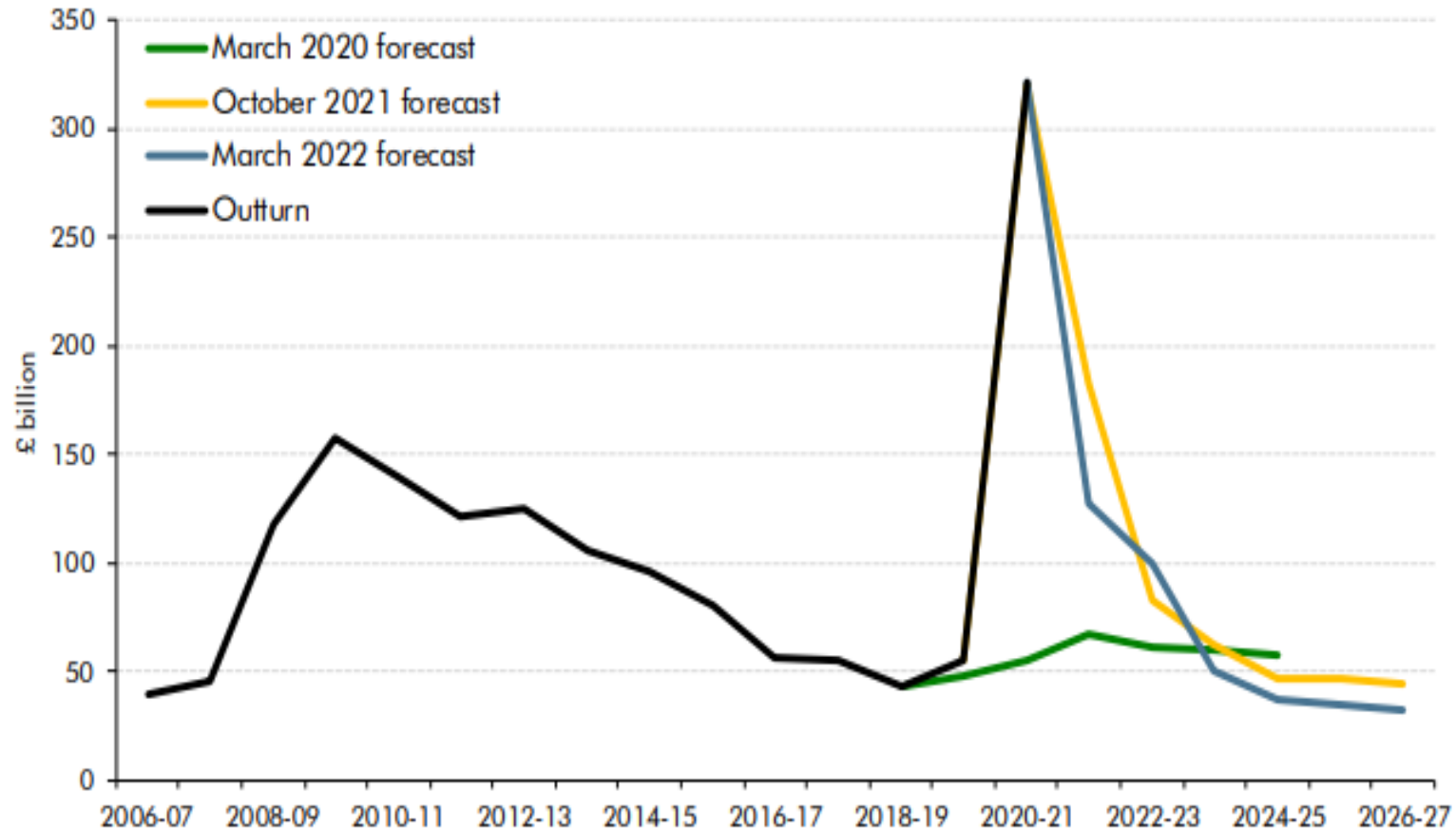
Table 1.1: Summary of the OBR's central economic forecast (percentage change on year earlier, unless otherwise stated)¹

	2021	Forecast				
		2022	2023	2024	2025	2026
GDP growth	7.5	3.8	1.8	2.1	1.8	1.7
GDP growth per capita	7.4	3.5	1.5	1.9	1.6	1.5
Main components of GDP						
Household consumption ²	6.1	5.4	1.0	1.5	1.1	1.2
General government consumption	14.5	2.6	1.2	1.4	1.6	2.0
Fixed investment	5.3	6.0	5.2	1.8	3.6	3.2
Business investment	-0.7	10.6	5.6	3.6	5.4	4.5
General government investment	11.9	-1.1	7.8	-2.0	1.1	1.7
Private dwellings investment ³	12.6	2.6	2.7	0.8	1.5	1.5
Change in inventories ⁴	0.6	-0.3	0.0	0.0	0.0	0.0
Net trade ⁴	-1.2	-0.6	-0.1	0.5	0.0	-0.1
Consumer Prices Index (CPI) inflation	2.6	7.4	4.0	1.5	1.9	2.0
Employment (millions)	32.4	32.7	32.9	33.1	33.2	33.3
Unemployment (% rate)	4.5	4.0	4.2	4.1	4.1	4.1
Productivity - output per hour	1.2	-0.2	1.0	1.6	1.3	1.3

Public sector balance sheet



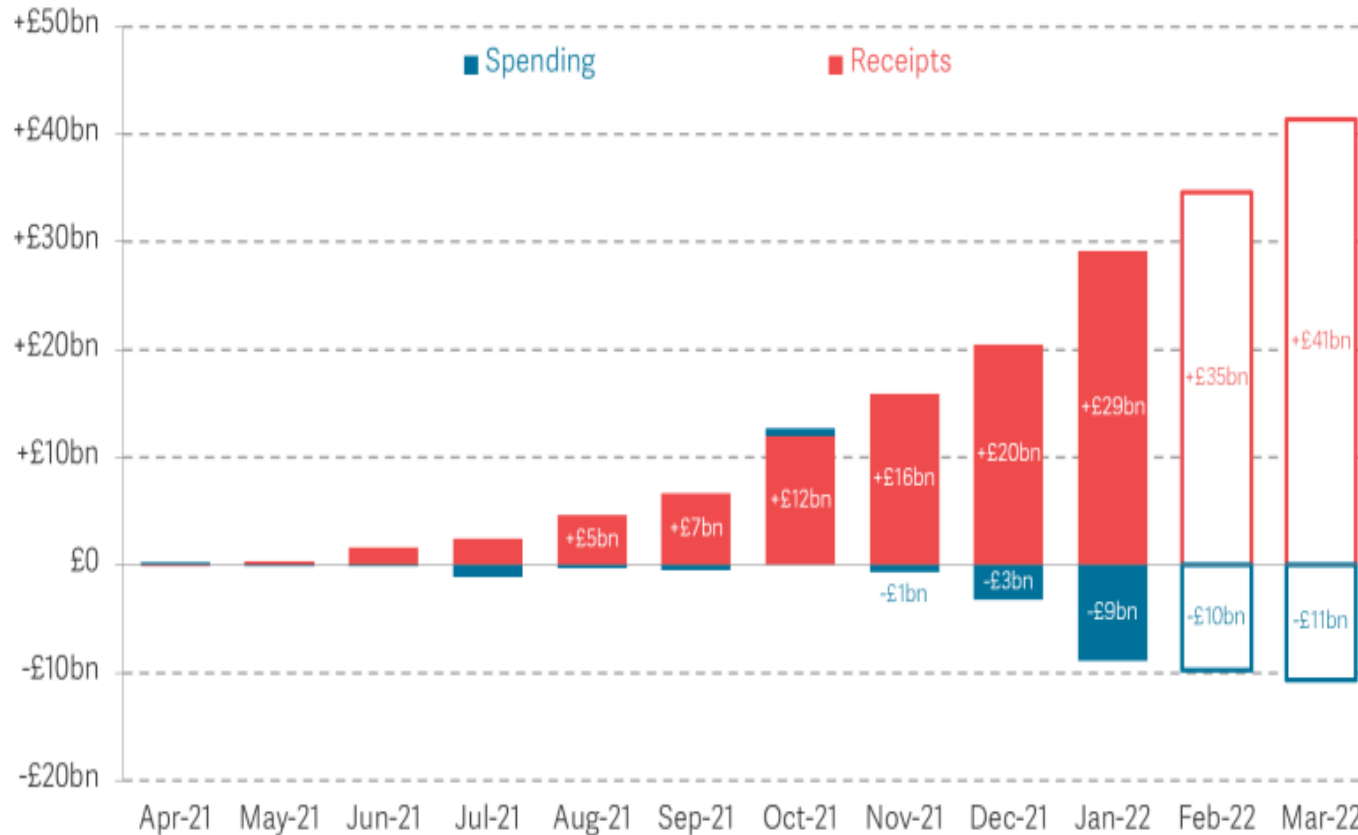
Public sector deficit and the pandemic



Source: ONS, OBR

Borrowing set to come in £30bn lower than expected this year

Changes in central government current receipts and expenditure, outturn relative to forecast : UK



Receipts surge
offset somewhat by
more spending

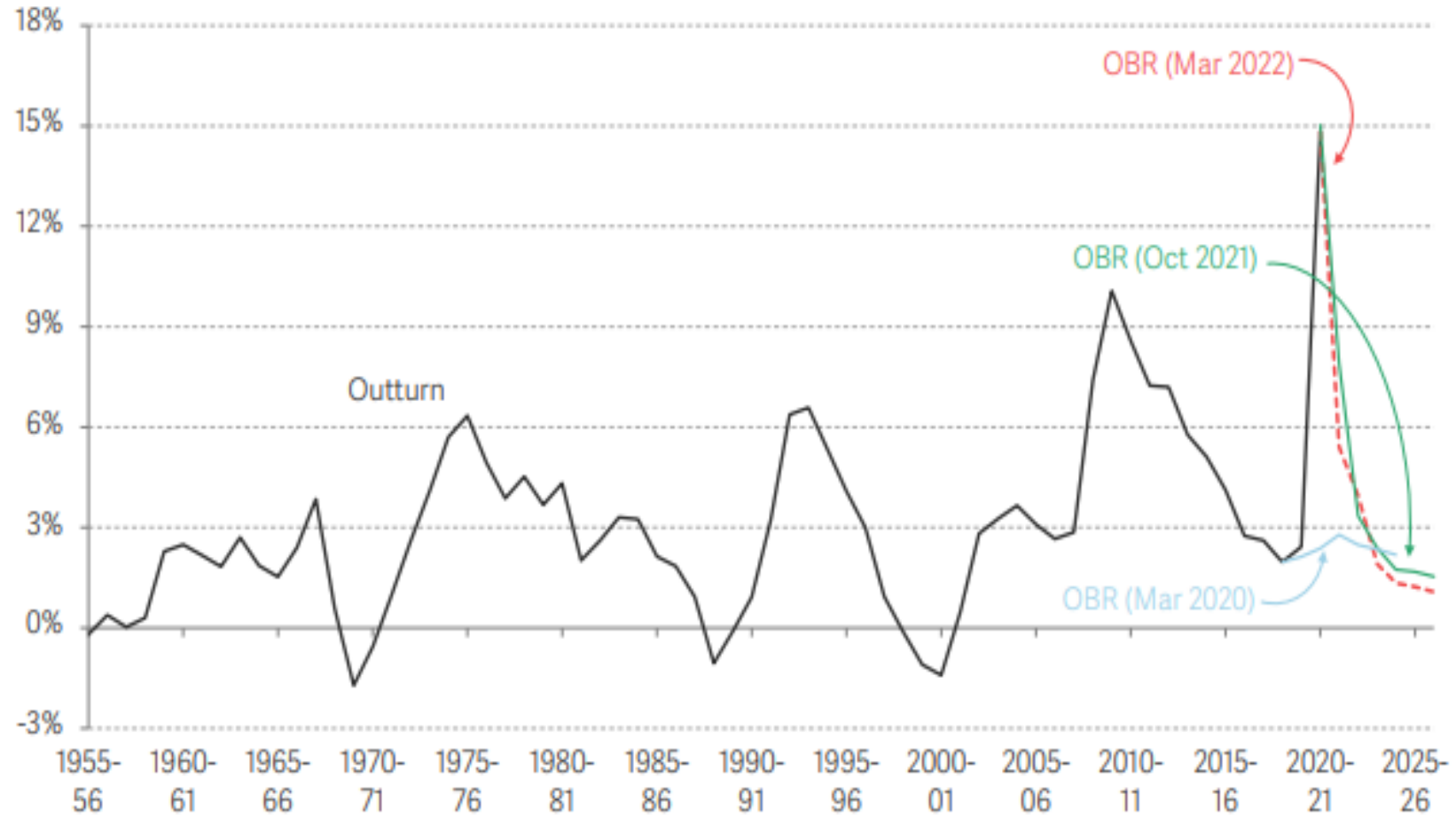
Reflects higher
inflation impact on
gilts, which will
build in the final 2
months of the year

If this is the case,
and receipts
continue to
improve, borrowing
will come in around
£30bn better than
the expected
£183bn

Note: Figures exclude PSNB-neutral intra-public sector transfers: (1) the Asset Purchase Facility (affecting central government receipts and public corporations net borrowing); and (2) grants to local authorities (affecting central government expenditure and local authorities net borrowing). Negative spending numbers in the chart represent increased spending compared to previous OBR forecast. The final two bars represent projections based on extrapolating growth in revenues (excluding self-assessment tax returns) from November to January forward and using the estimated increase in debt interest spending on indexed-link gilts based on the RF economic scenario (see later slides) and the OBR's ready reckoner between RPI inflation and interest payments (other spending items were kept fixed at the January level). Source: RF analysis of ONS, Public Sector Finances; OBR, Economic and Fiscal Outlook, various.

FIGURE 20: **Borrowing is falling even more rapidly than previously expected**

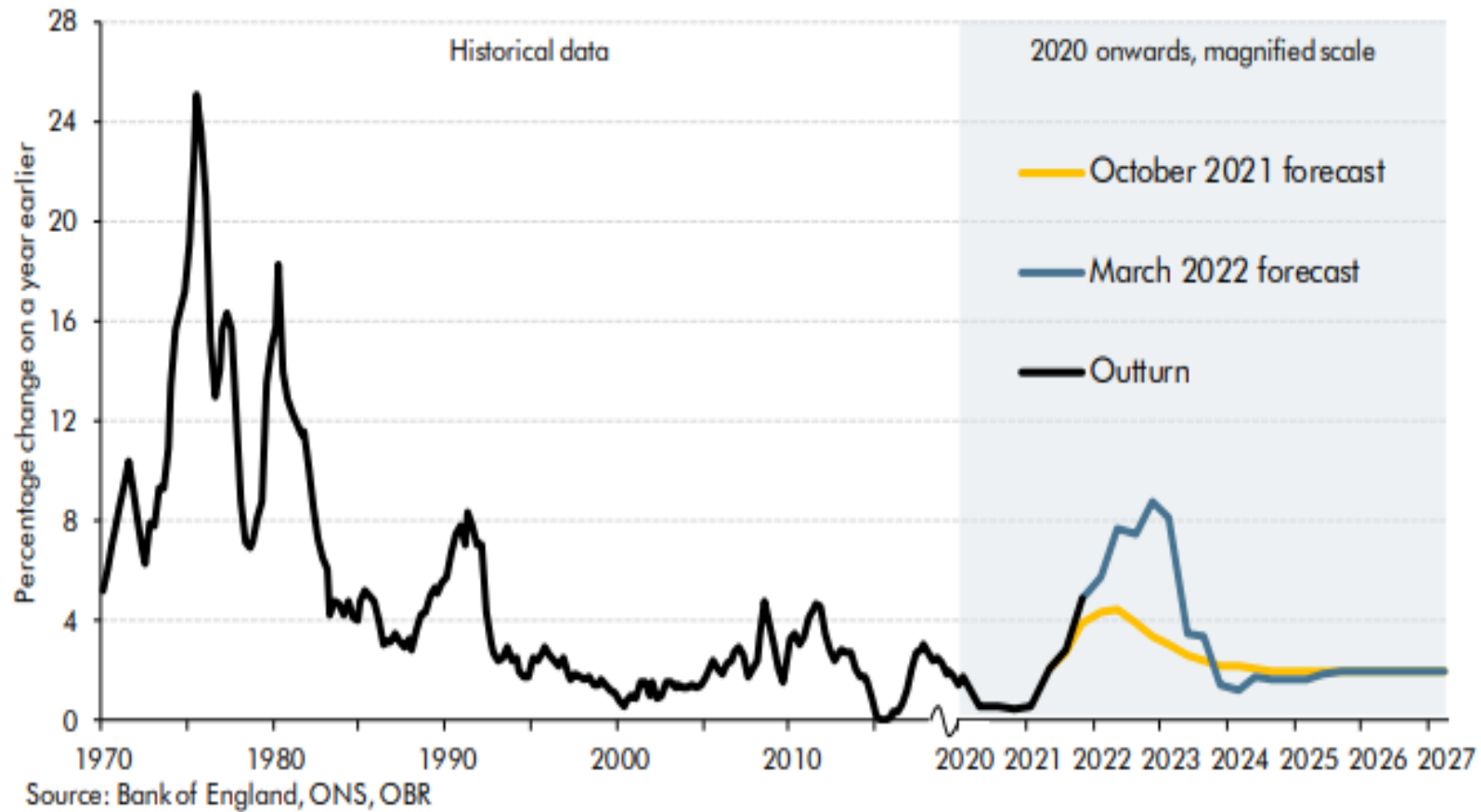
Public sector net borrowing, as a share of GDP, outturn and select OBR forecasts: UK



SOURCE: ONS, Public Sector Finances; OBR, Economic and Fiscal Outlook, October 2021 and March 2022.

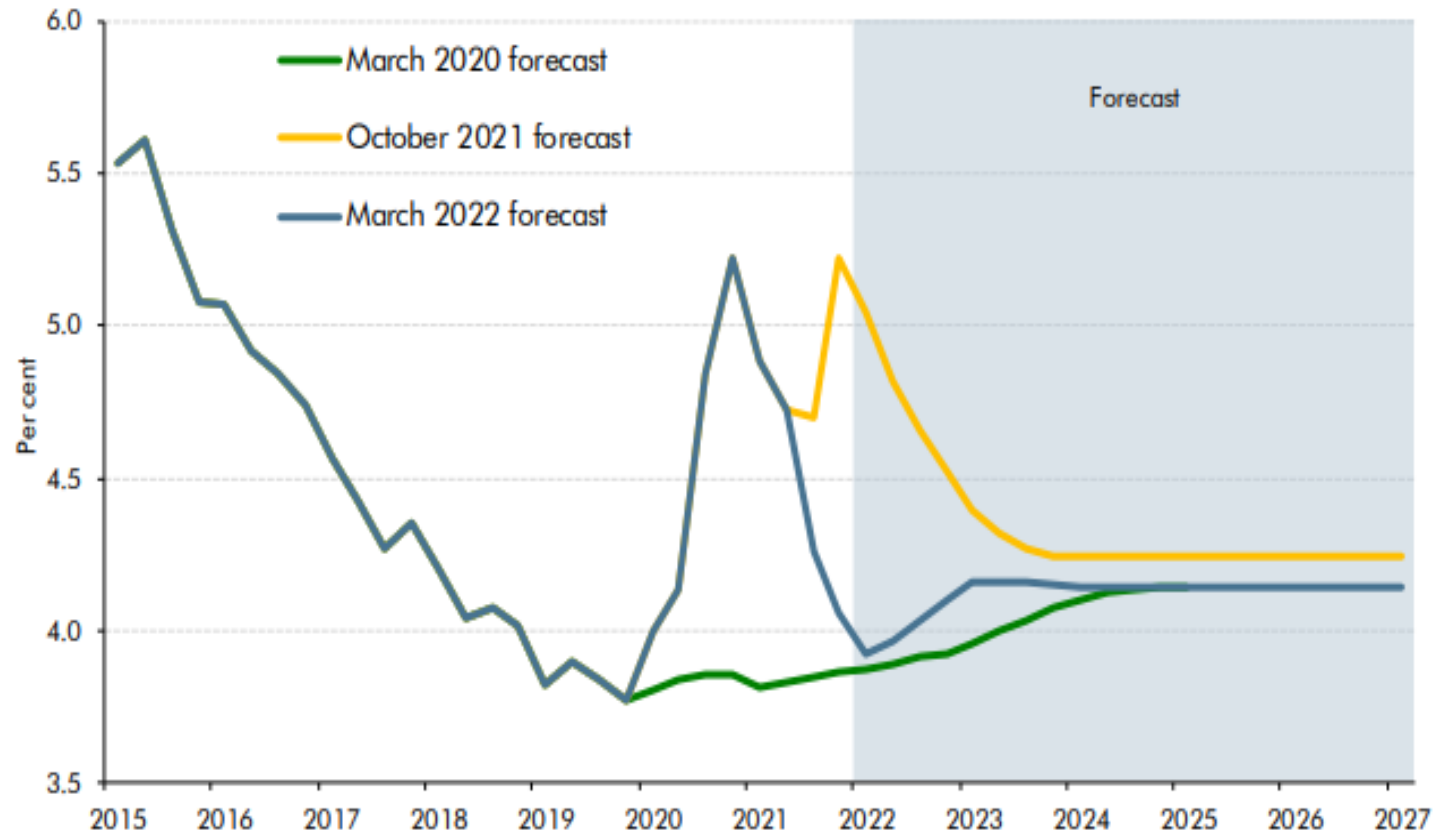
Inflation (CPI)

- not the 1970s, but not good



Unemployment

- though the Ukraine crisis/inflation rules may yet worsen this



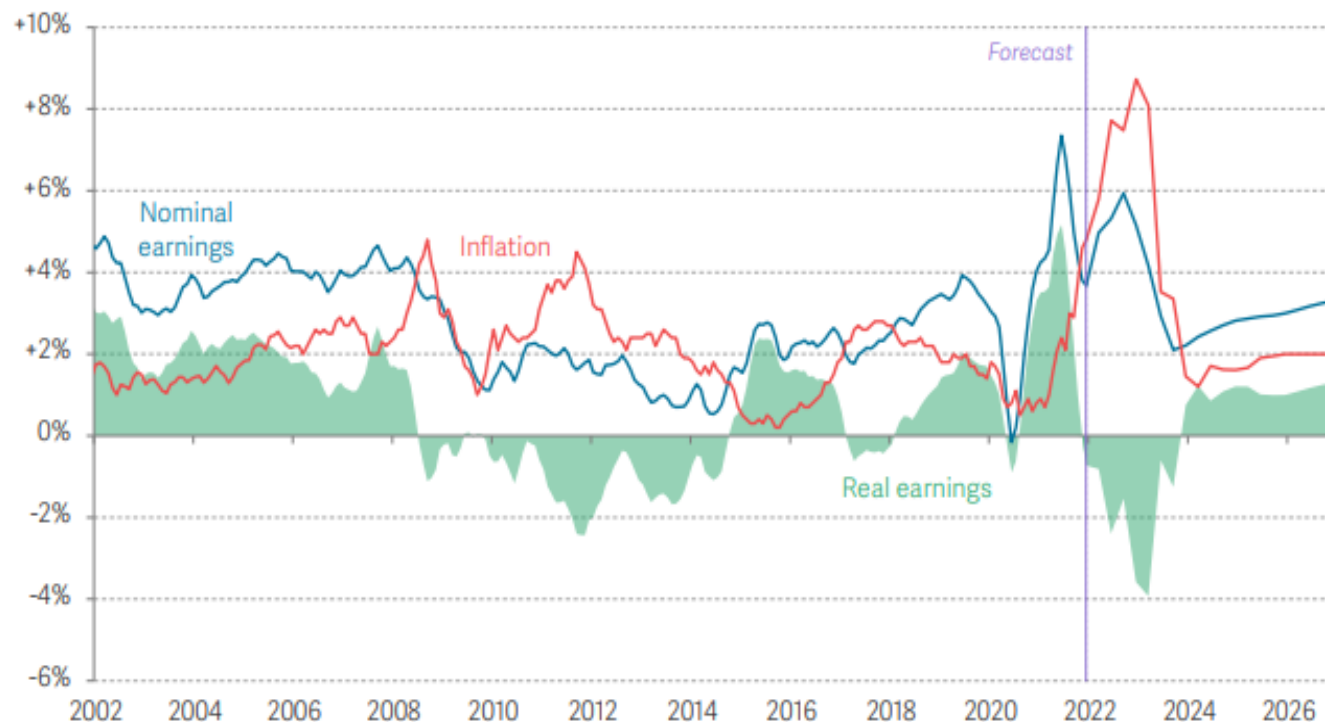
Source: ONS, OBR

Big pay rises?

- not sufficient to stop falling real household incomes

FIGURE 4: **Despite strong nominal wage growth, real wages are set to fall until the end of 2023**

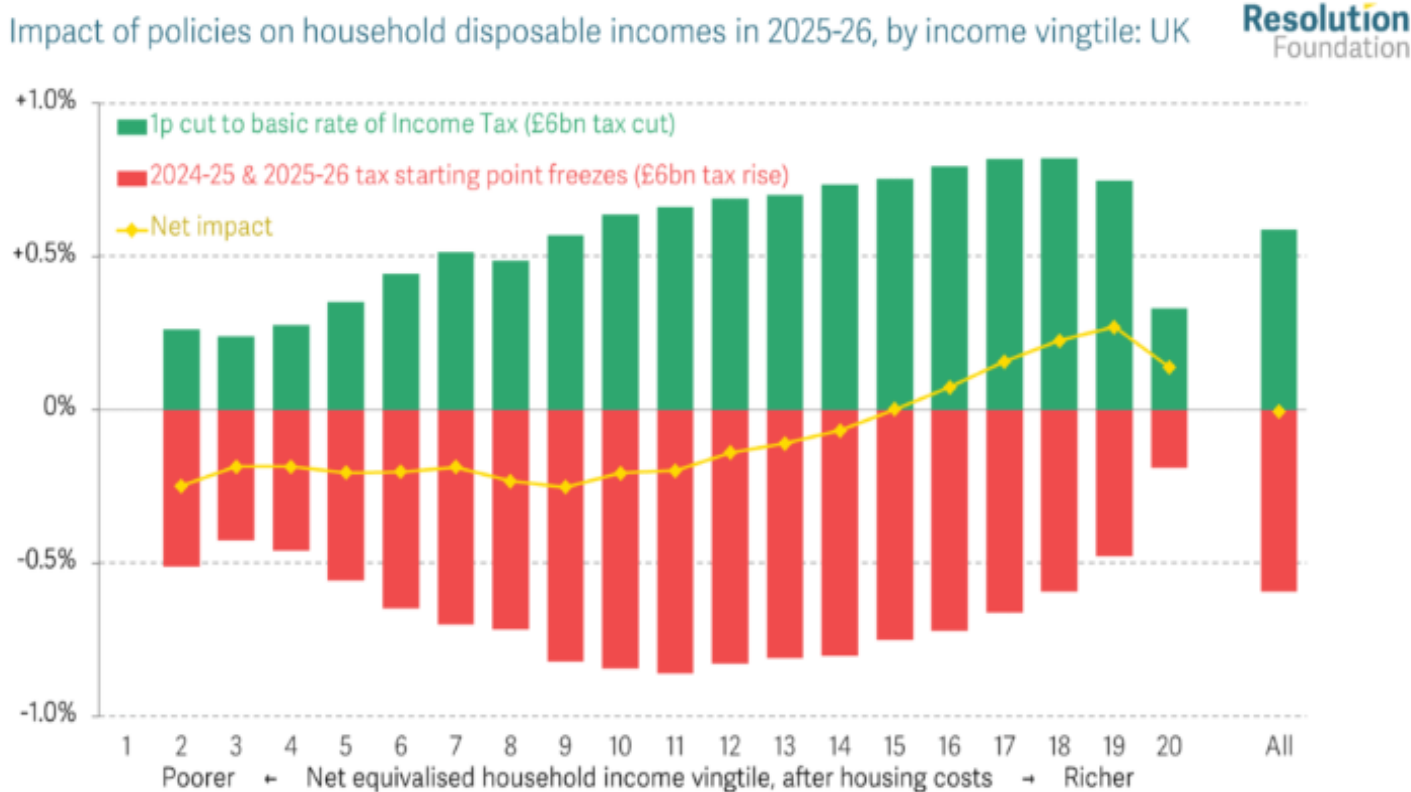
Annual growth in average weekly earnings (regular pay) and CPIH inflation, outturn and projections: GB/UK



Source: Resolution Foundation

Impact of Budget on different income groups

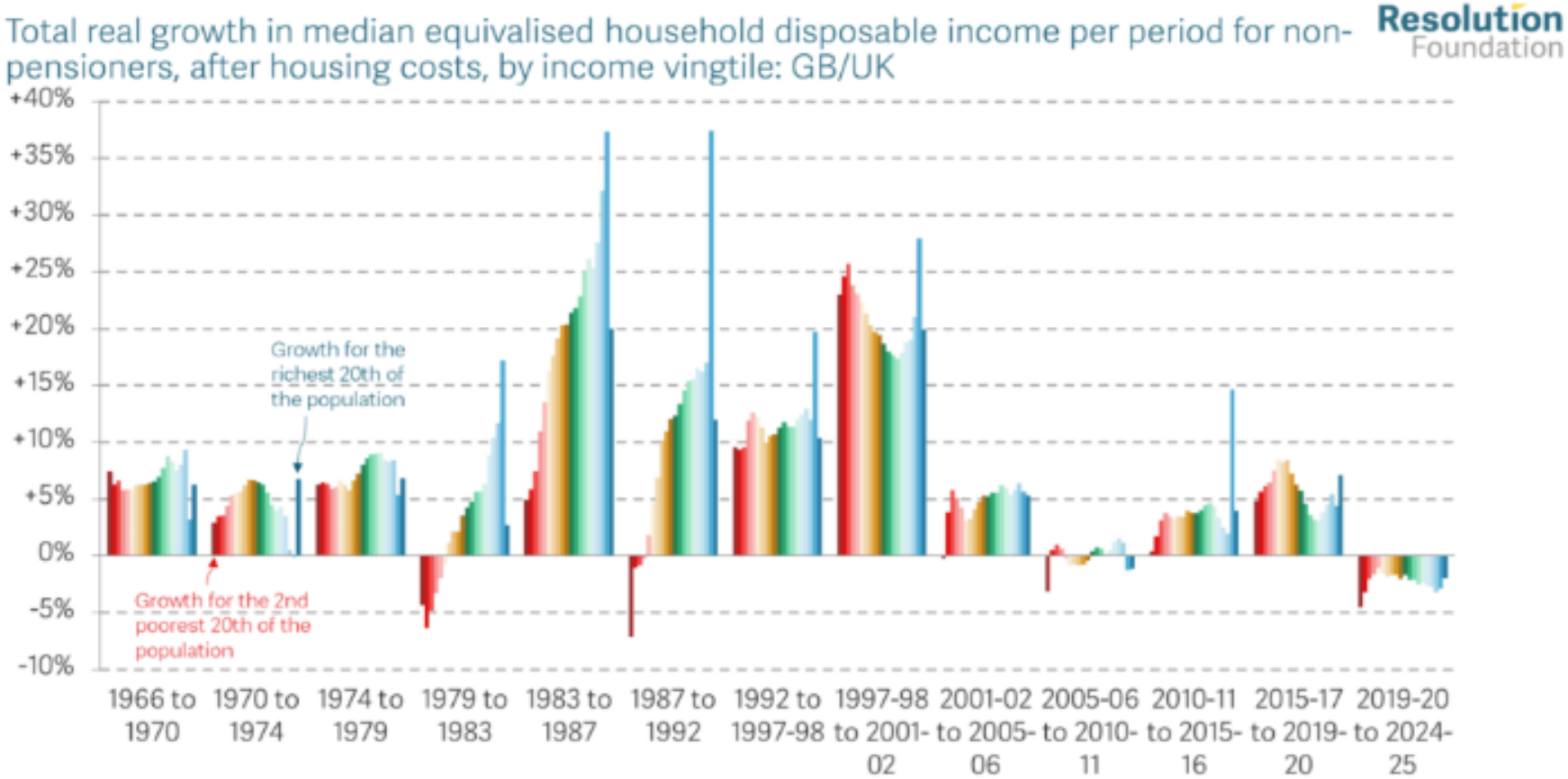
- it was progressive next year and into the future



Notes: We exclude the bottom 5 per cent due to concerns about the reliability of data for this group. Based on the latest OBR CPI forecast, the starting point for Income Tax, personal National Insurance and the Health and Social Care Levy would rise to around £13,220 in 2025-26 (rather than £12,570) if the freeze ended two years early. Source: RF analysis of DWP, Family Resources Survey, using the IPPR Tax Benefit Model. © Resolution Foundation 2022 resolutionfoundation.org

Source: Resolution Foundation

Household income growth to be lowest since 1945



Resolution Foundation

Notes: We exclude the bottom 5 per cent, due to concerns about the reliability of data for this group. See The Living Standards Outlook 2022 for details of our projection methodology. Some periods are four years long and others five years. The chosen time periods correspond to the years of past general elections (plus 2024), but we do not include a division for the 2017 election and nor do we try to estimate growth over the February to October parliament of 1974. Source: RF analysis of DWP & IFS, Households Below Average Income; and RF projection including use of the IPPR Tax Benefit Model, ONS data, and OBR forecasts.

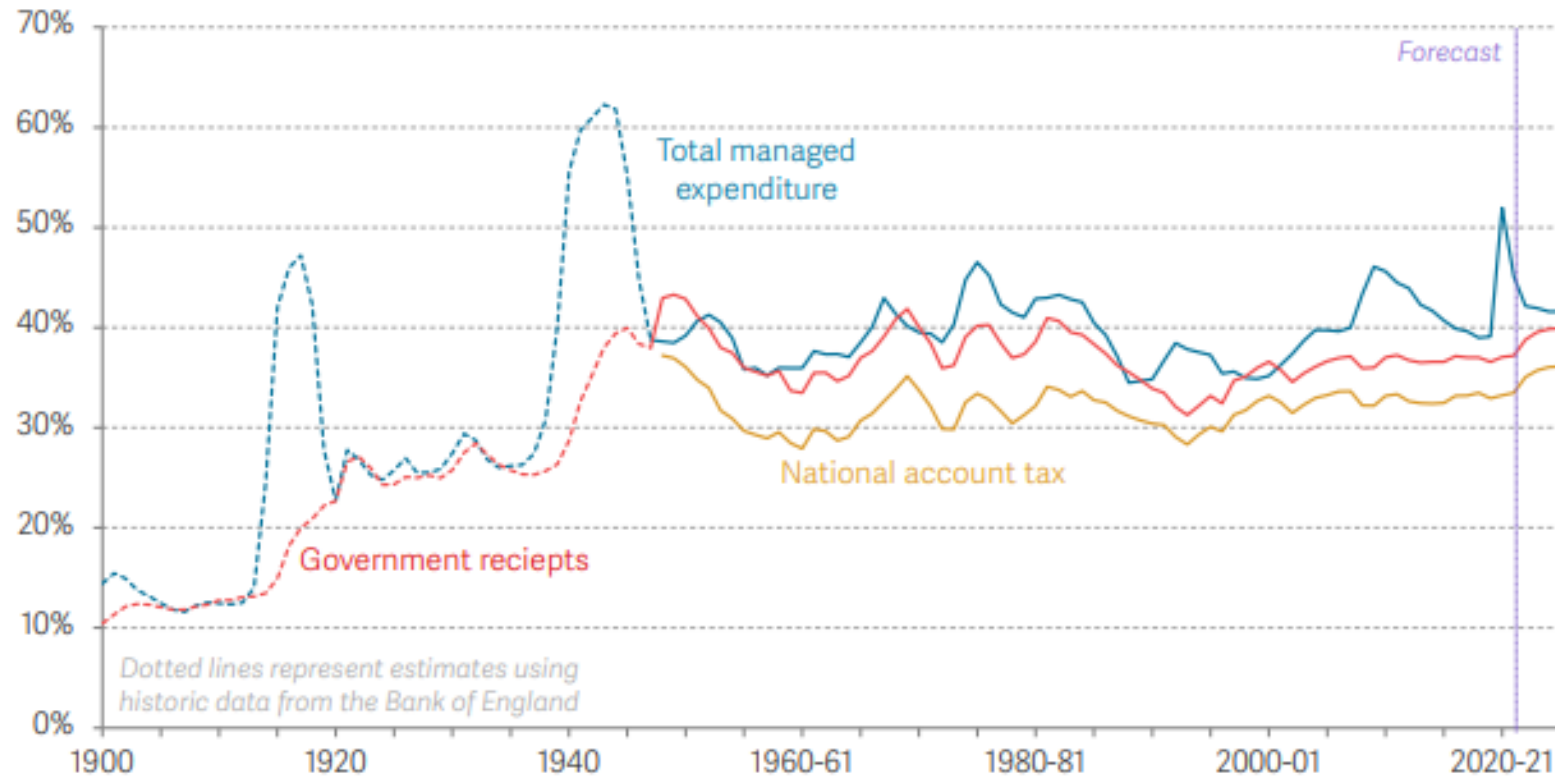
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Taxation and public spending

- Both taxation and public spending to remain at levels higher than before the pandemic
- UK moving towards being a 'bigger State' country with higher taxes
- Distributional effects of the Budget broadly 'progressive'
- Health (and social care – but it is mostly the NHS) rising as a share of all public expenditure
- Local government's settlement is relatively generous by recent standards, but little growth for service apart from adult social care
- Capital expenditure will level off, but embedding recent years' increases

Government spending and borrowing

- tax to reach highest share of GDP since the 1950s/early 1960s

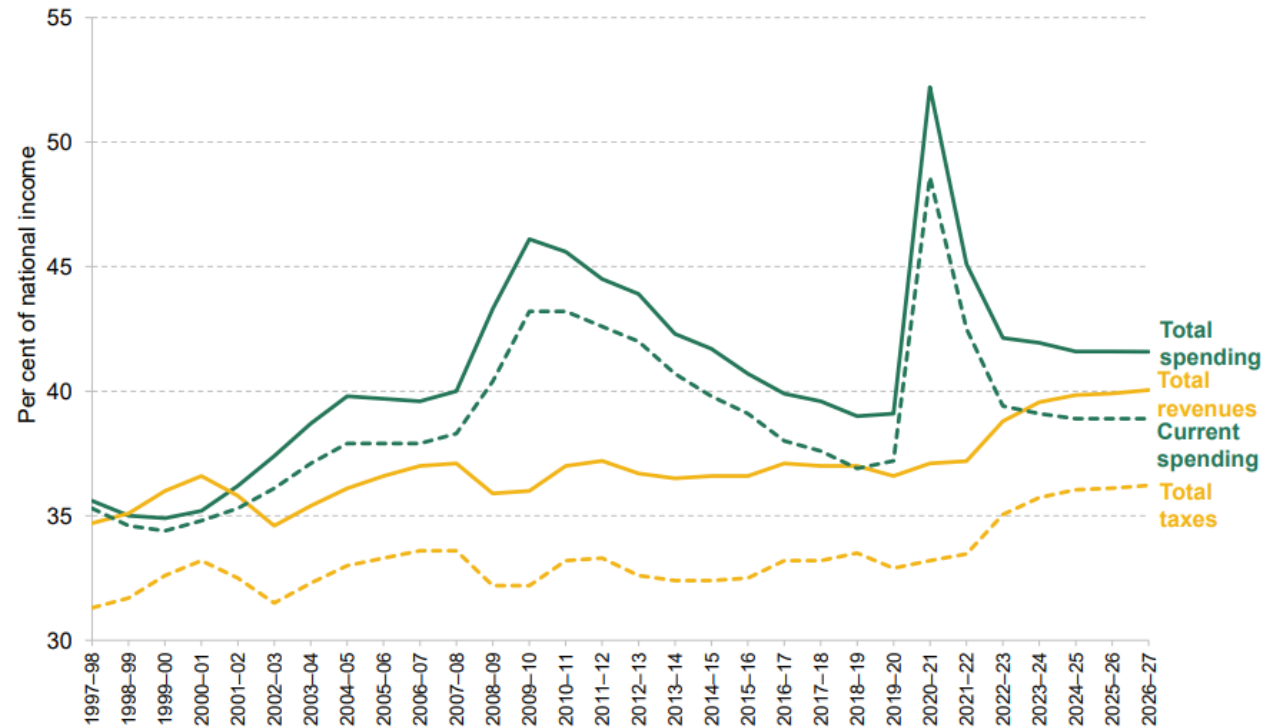


Source: Resolution Foundation

A larger State in future – IFS agree

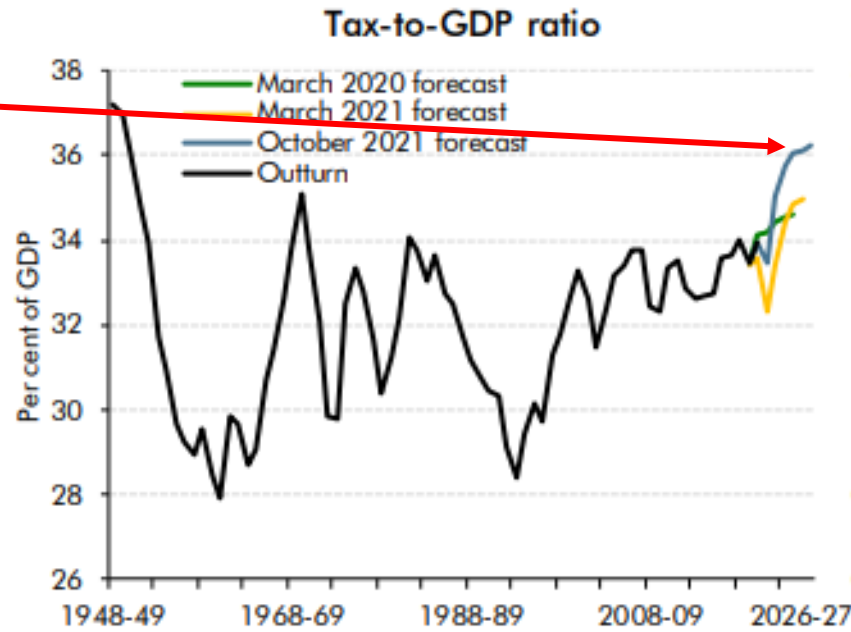
A bigger state post pandemic

IFS

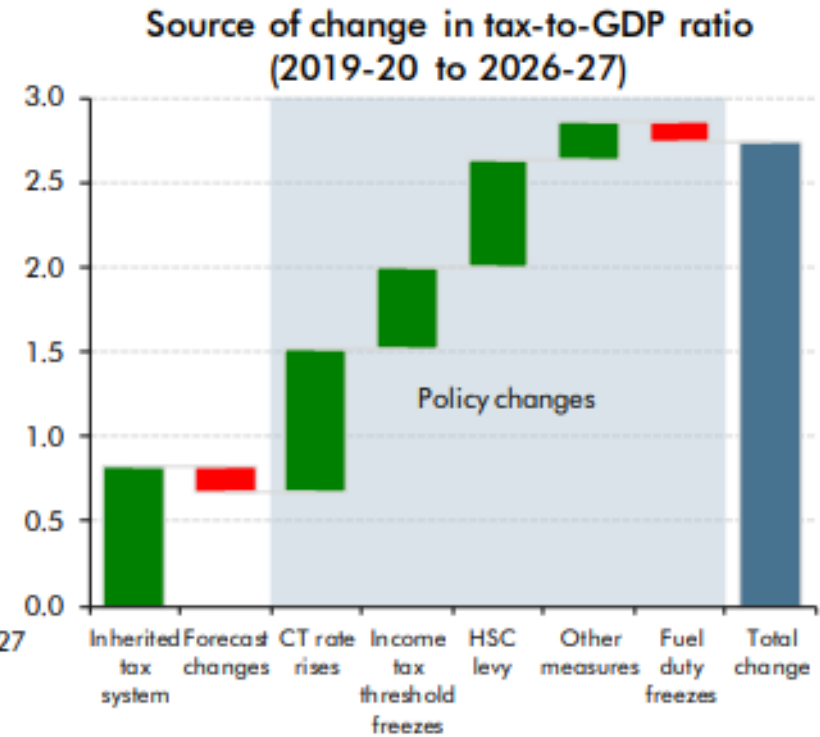


Tax and spend

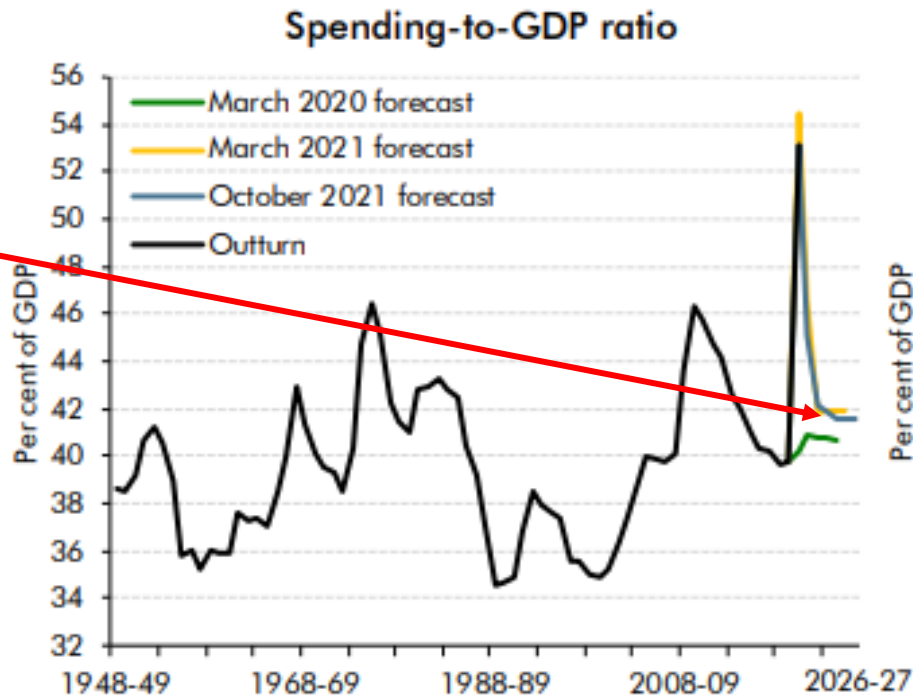
Taxes as a % of GDP



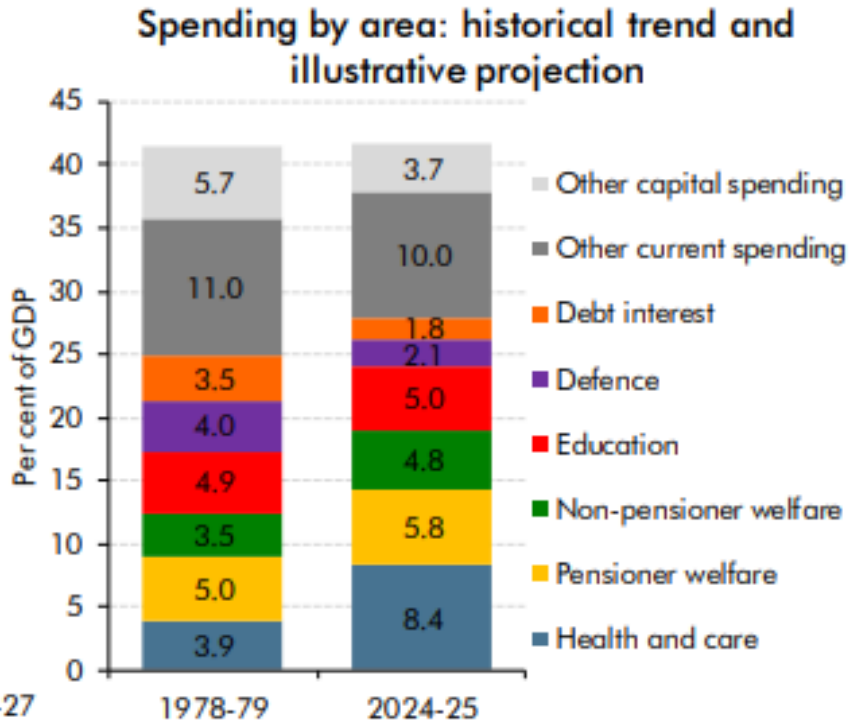
Highest since the 1960s



Spending as a % of GDP

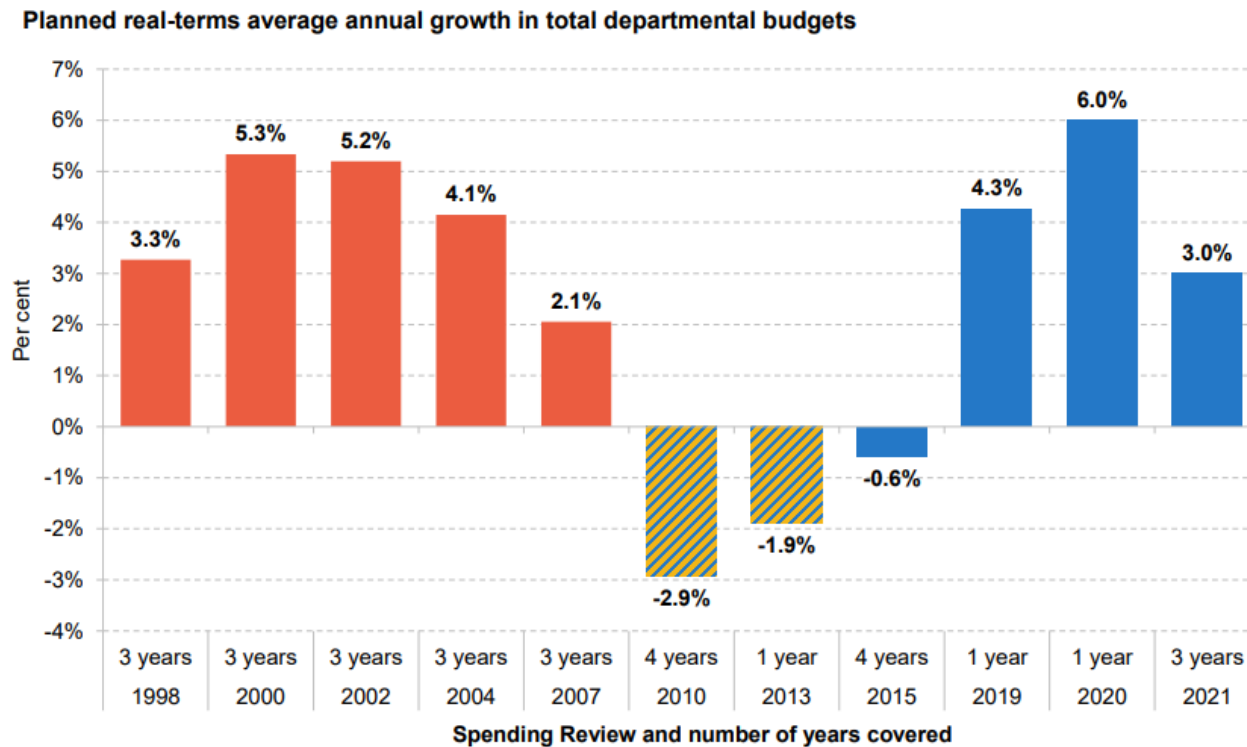


Post-Covid level above pre-Covid



Public spending: real terms increases

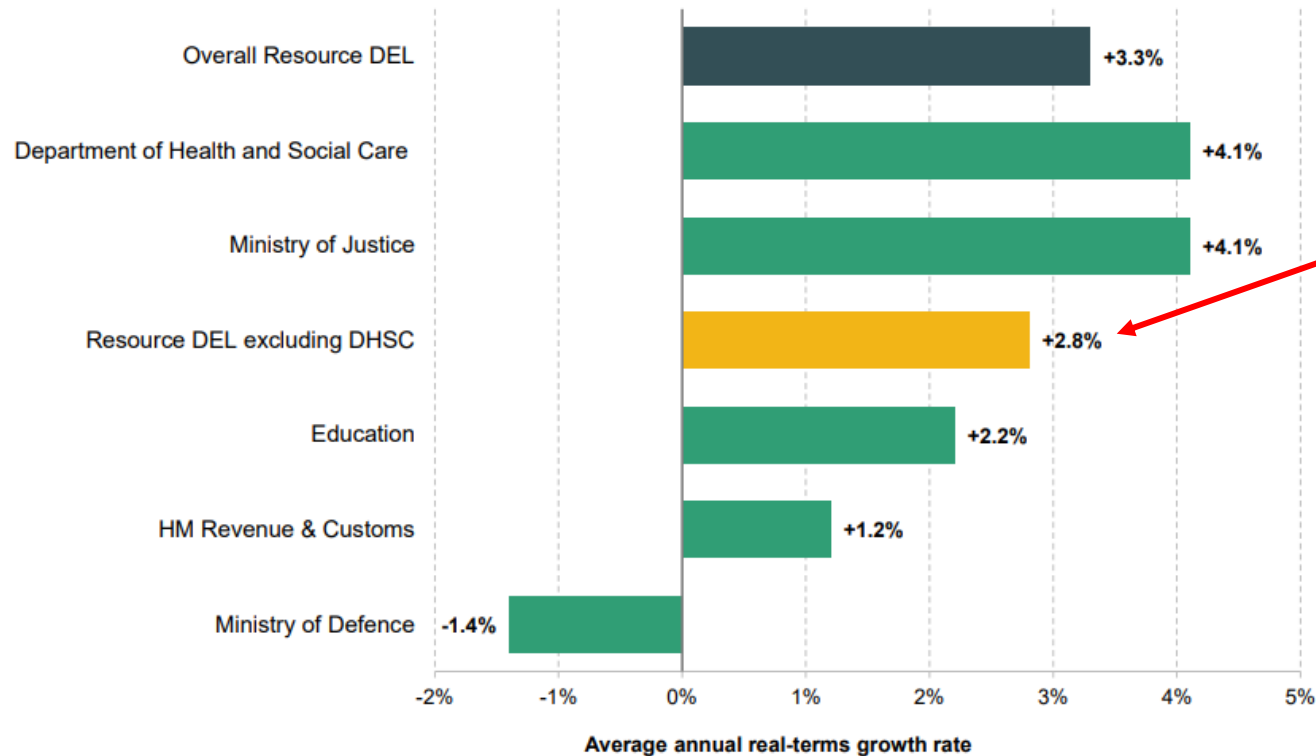
- an end to 'austerity' – sort-of



Note: Figures denote *planned* average real-terms growth rate in TDEL.
Source: HM Treasury Spending Review 2021 and all sources for Figure 5.13 of IFS Green Budget 2021.

Public spending: differences from department to department

Average real % growth in resource budgets over SR 2021 period (2021–22 to 2024–25)

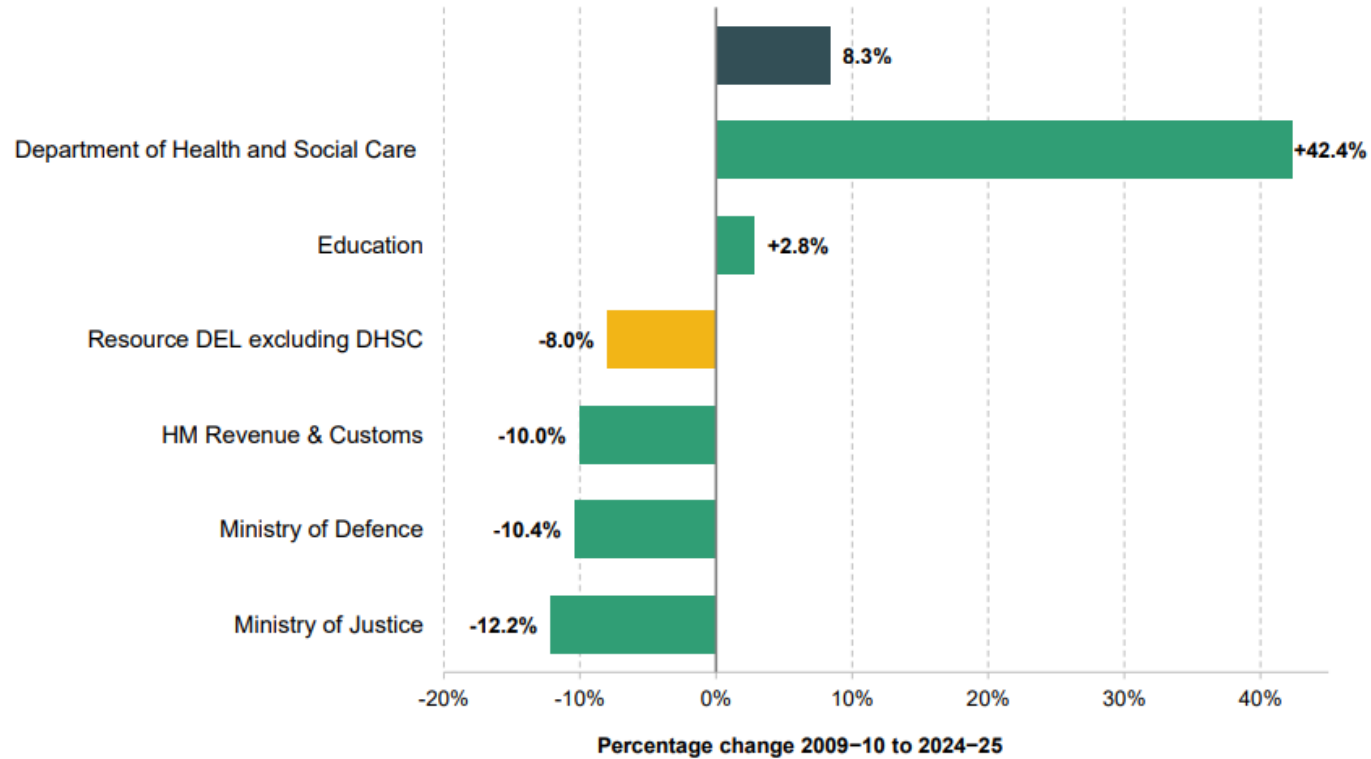


Local
government
within
here

Note: Resource DEL refers to resource departmental expenditure limits, which can be thought of as day-to-day funding for public services.
Source: Author's calculations using HM Treasury, Spending Review 2021 (Table E.3).

The shape of the State is changing

- health takes more and more of public spending



Note: Resource DEL refers to resource departmental expenditure limits, which can be thought of as day-to-day funding for public services. Overall Resource DEL refers is adjusted by the OBR for historical discontinuities and classification changes, and is additionally adjusted for spending changes related to employer pension and NICs.

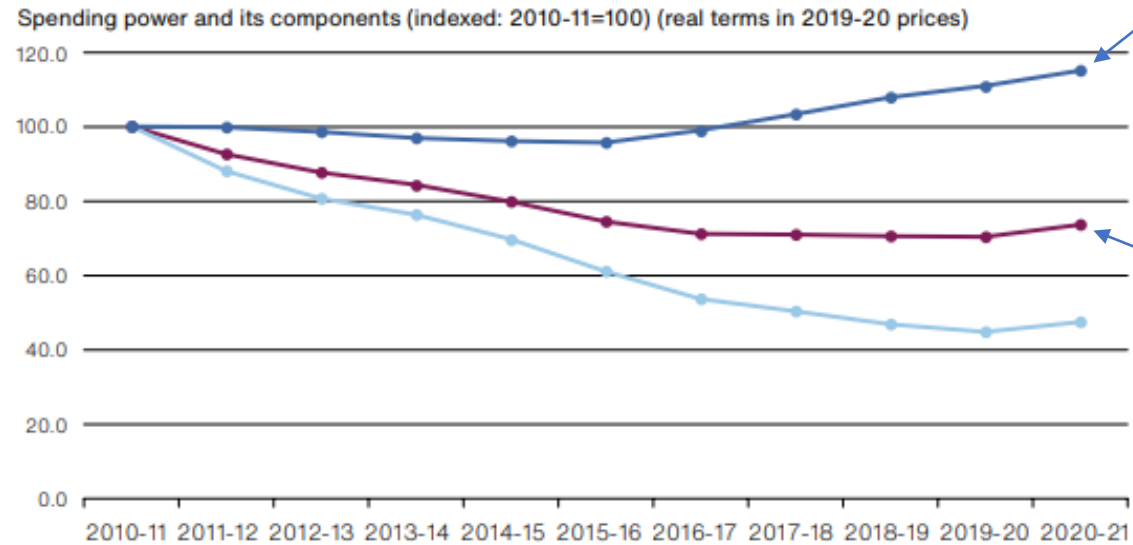
Source: Author's calculations using OBR October 2021 EFO, HM Treasury Spending Review 2021 and PESA (various).

Local government's finances

Figure 1

Change in spending power in English local authorities 2010-11 to 2020-21

Spending power fell rapidly from 2010-11 to 2016-17 at the sector level but has been relatively stable since then, with growth in 2020-21



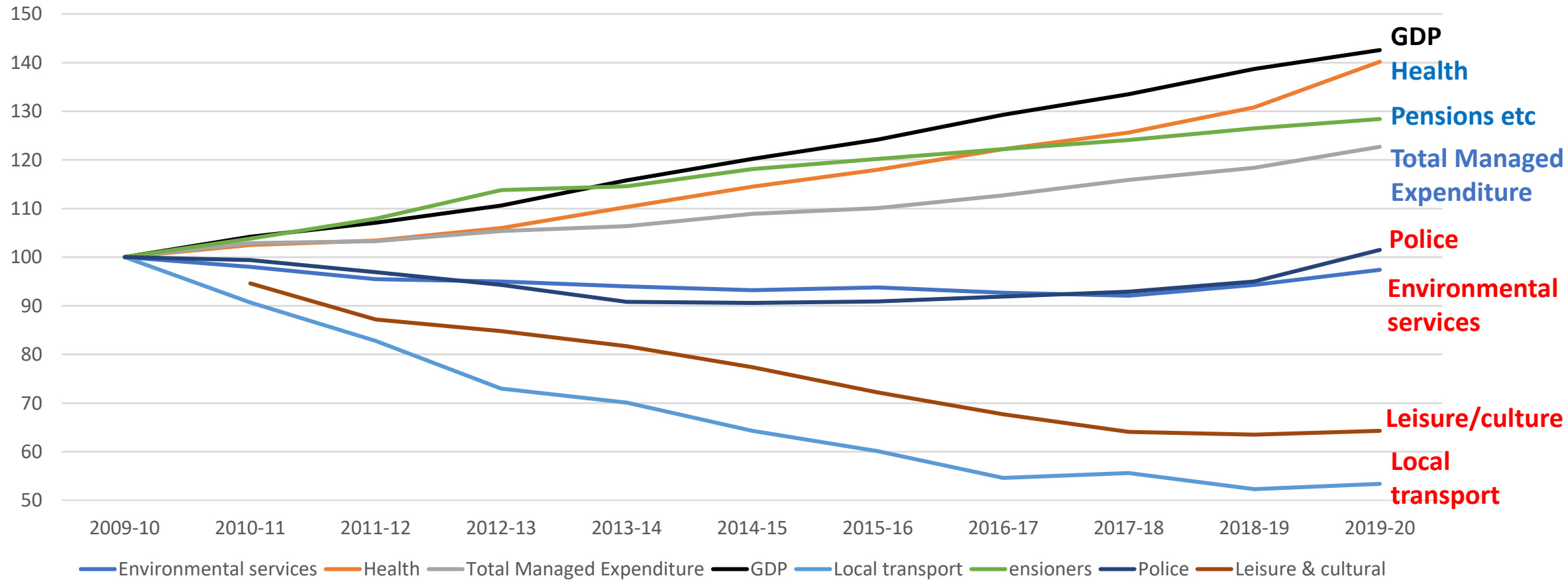
- Spending power
- Government funded spending power
- Council Tax

Council tax rising sharply

Local government spending still c25% below 2010-11 in real terms

Public expenditure priorities

2009-10 to 2019-20 [£, 2009-10 =100, cash]



Sources: ; GDP, 'Health', 'TME' and 'Transport, from *Public Expenditure Statistical Analyses*, various years;

Pensioners from: GOV.UK [outturn-and-forecast-spring-statement-2021.xlsx]

'Environmental' 'local transport' and 'police' from *Local Authority Revenue Expenditure and Financing*, MHCLG, successive years

Blue: central govt

Red: local govt

The visible impact of these policies

- The different treatment of councils' spending and central government/welfare expenditure is visible in the streets outside peoples' homes
- Local government has attempted to protect social services, thus provision such as street cleaning, highways, planning, refuse collection, parks, graffiti removal, rough sleeping, libraries, leisure, transport, youth services, etc have faced reductions of 30-60%
- As incomes rise for many people, there must be a risk that a 'private affluence and public squalor' challenge will become apparent
- In major cities, this kind of visible interface is inevitably more apparent

Percentage change in expenditure 2009-10 to 2019-20

- various household-related services, public and private

	% change, 2009-10 to 2019-20 (cash)
Household expenditure	
Pets and related products	+99
Travel abroad*	+72
Food	+45
Vehicles*	+25
Sport and recreation	+22
Local government expenditure	
Police	+1
Local environment	-2.5
Local transport	-42

Sources: <https://www.statista.com>, except 'Local environment': as previous table

Note: * = 2010-11 to 2018-9 only

Local government

- 'core spending power'

£ billion	Outturn	Outturn	Baseline	Plans	Plans	Plans	Average annual real terms growth	
							2019-20	2020-21
Resource DEL ^{1 2}	7.5	8.6	9.1	10.8	12.1	12.7	9.4%	8.4%
<i>of which: Adult Social Care reform</i>	-	-	-	0.2	1.4	2.0	-	-
Core Spending Power (CSP)	46.2	49.1	50.4	53.7	56.6	58.9	3.0%	2.5%

¹ Excluding ringfenced COVID-19 DEL

² Local Government DEL presented here is not reduced by the switch from DEL to AME for Business Rate Retention Pilots and does not include DEL compensation for new business rates measures announced at Budget 2021. Figures for 2019-20 and 2020-21 also reflect other adjustments for business rates and the New Homes Bonus. Therefore, the figures in this table do not match the outturn figures presented in the total DEL table.

Source: HM Treasury

Council tax has been a robust income source and is set to rise further

- Government revenues fell in 2020-21 and 2021-22 as compared to estimates at the end of 2019-20
- Council tax proved robust
 - Further increases in the yield expected
 - Government has ruled out reform
- NNDR rising more slowly
 - Some additional reliefs for the coming year, but full replacement unlikely
- Inflation/pay increase risks to service volume

	£ billion				
	Outturn	Forecast			
	2020-21	2021-22	2022-23	2023-24	2024-25
Income tax ¹	-9.5	-4.1	2.2	4.0	6.5
of which: Pay as you earn	-6.2	-0.5	3.5	5.9	5.2
Self assessment	-2.4	-4.1	-1.9	-2.7	0.5
Other income tax	-0.8	0.5	0.6	0.8	0.8
National insurance contributions	-6.2	0.0	18.0	-2.3	-5.4
Health and social care levy				18.3	18.7
Value added tax	-22.0	-14.0	4.0	3.3	2.4
Corporation tax ²	-6.3	-8.0	-6.0	10.8	18.0
of which: Onshore	-6.0	-8.7	-7.7	10.1	17.6
Offshore	-0.2	0.7	1.7	0.7	0.4
Petroleum revenue tax	0.0	-0.2	0.0	0.0	0.0
Fuel duties	-6.6	-1.4	-1.7	-1.3	-1.3
Business rates	-12.0	-10.9	-4.5	-1.0	-1.6
Council tax	0.5	1.0	1.4	2.0	2.5
VAT refunds	0.1	0.0	1.1	0.9	-0.1
Capital gains tax	-0.8	-3.4	-1.2	-0.4	-0.3
Inheritance tax	-0.2	0.1	0.1	-0.3	0.4
Property transaction taxes ³	-4.3	0.1	-0.4	-1.0	-1.4
Stamp taxes on shares	0.1	0.5	0.0	0.0	0.0
Tobacco duties	0.8	1.2	1.3	1.3	1.3
Alcohol duties	0.6	0.4	-0.3	-0.3	-0.2
Air passenger duty	-3.7	-3.1	-2.3	-1.4	-0.4
Insurance premium tax	-0.3	-0.2	-0.1	0.0	0.0
Climate change levy	-0.4	-0.1	-0.3	-0.4	-0.5
Bank levy	0.0	0.2	0.2	0.2	0.2
Bank surcharge	-0.4	0.0	-0.4	-1.1	-1.2
Apprenticeship levy	0.0	0.1	0.0	0.0	0.0
Digital services tax	0.0	0.2	0.2	0.2	0.3
Other HMRC taxes ⁴	-0.4	0.4	1.0	1.2	1.2
Vehicle excise duties	-0.2	0.0	0.1	0.1	-0.1
Licence fee receipts	0.1	0.0	0.0	0.0	0.0
Environmental levies	-1.1	-0.4	-0.6	0.0	0.0
Emissions Trading Scheme receipts	0.1	-0.3	3.6	3.0	2.9
Other taxes	-1.2	-0.6	0.3	0.3	0.2
National Accounts taxes	-73.2	-42.6	15.8	36.1	41.3
Less own resources contribution to EU	0.2	-	-	-	-
Interest and dividends	-4.3	-4.5	-2.8	-1.7	-2.6
Gross operating surplus	0.6	-0.2	0.2	0.6	0.5
Other receipts	-0.9	-1.4	-0.1	0.0	-0.1
Current receipts	-77.7	-48.8	13.2	35.1	39.0

Current receipts

- change since 2019-20

Council tax yield increased by more (in cash) in 2020-21 and 2021-22 than any revenue apart from tobacco duty

	£ billion							
	Outturn			Forecast				
	2019-20	2020-21	2021-22	2022-23	2023-24	2024-25	2025-26	2026-27
Income tax ¹	193.6	198.1	213.2	229.6	240.5	253.0	268.4	284.3
of which: Pay as you earn	165.2	169.3	183.8	196.9	206.9	214.9	227.7	239.7
Self assessment	32.0	31.9	31.8	35.3	36.3	40.9	43.5	47.2
Other income tax	-3.7	-3.1	-2.3	-2.6	-2.6	-2.8	-2.8	-2.6
National insurance contributions	144.6	144.0	157.0	182.0	168.1	171.7	176.5	183.4
Health and social care levy					18.3	18.7	19.3	20.1
Value added tax	133.8	118.6	131.9	155.0	159.1	163.1	167.4	172.1
Corporation tax ²	49.8	51.8	52.0	56.6	75.6	85.2	89.3	91.5
of which: Onshore	48.8	51.1	50.2	53.8	73.7	83.6	87.7	90.1
Offshore	1.0	0.7	1.8	2.8	1.9	1.6	1.6	1.5
Petroleum revenue tax	-0.4	-0.3	-0.4	-0.3	-0.2	-0.2	-0.1	-0.1
Fuel duties	27.6	20.9	26.8	28.8	29.9	30.4	30.7	31.1
Business rates	31.3	19.5	22.5	29.8	34.0	34.7	35.2	36.0
Council tax	36.3	38.4	40.1	41.8	43.6	45.4	46.9	48.4
VAT refunds	19.0	20.2	21.0	22.9	23.4	23.6	24.6	25.9
Capital gains tax	9.8	10.6	9.2	13.0	15.2	16.7	18.1	19.7
Inheritance tax	5.1	5.4	6.0	6.4	6.5	6.8	7.2	7.6
Property transaction taxes ³	12.5	9.5	14.8	15.8	16.5	17.2	18.2	19.4
Stamp taxes on shares	3.6	3.7	4.2	3.9	4.0	4.1	4.3	4.5
Tobacco duties	9.7	9.8	10.1	10.1	10.0	10.0	9.9	9.8
Alcohol duties	11.5	12.4	12.8	12.6	13.0	13.7	14.2	14.8
Air passenger duty	3.7	0.3	1.1	2.1	3.2	4.4	4.5	4.8
Insurance premium tax	6.5	6.3	6.5	6.8	7.0	7.1	7.2	7.4
Climate change levy	2.1	1.8	2.0	1.9	2.0	2.0	2.1	2.2
Bank levy	2.5	1.9	1.3	1.2	1.2	1.2	1.2	1.2
Bank surcharge	1.5	1.1	1.6	1.2	0.6	0.5	0.5	0.5
Apprenticeship levy	2.8	3.0	3.2	3.2	3.3	3.4	3.6	3.7
Digital services tax	0.1	0.3	0.6	0.6	0.7	0.8	0.9	1.1
Other HMRC taxes ⁴	7.5	7.4	8.4	9.1	9.3	9.4	9.5	9.7
Vehicle excise duties	6.8	6.9	7.1	7.3	7.5	7.6	7.7	7.8
Licence fee receipts	3.3	3.7	3.7	3.9	3.9	4.0	4.0	4.1
Environmental levies	8.0	8.5	9.5	9.2	10.4	10.9	11.2	12.4
Emissions Trading Scheme	1.6	1.3	0.9	4.9	4.3	4.3	4.2	4.2
Other taxes	10.2	7.8	8.8	10.0	10.1	10.2	10.3	10.4
National Accounts taxes	744.4	713.0	775.7	869.4	921.1	959.8	996.9	1,038
Less own resources contribution to EU	-3.2	-2.2	-	-	-	-	-	-
Interest and dividends	23.4	23.3	24.3	27.8	30.7	31.2	32.2	33.7
Gross operating surplus	57.7	57.6	58.5	61.5	64.1	66.6	69.1	72.1
Other receipts	4.8	3.6	3.5	3.7	3.8	3.6	3.8	3.9
Current receipts	827.0	795.3	862.0	962.4	1,020	1,061	1,102	1,148

Current receipts

Business rates up £4.7bn (15%)
in cash terms between 2019-20 and
2026-27

Council tax yield up £12.1bn (33%)
in cash terms between 2019-20 and
2026-27

Fuel duty: 13%
Alcohol duties: 29%
Vehicle excise duty: 15%
Air passenger duty: 30%

NB 'Property transaction taxes' will have risen from 24% of
council tax to 40% between 2010-11 and 2026-27

Levelling up main funds/ initiatives

Policy	Description
Levelling Up Fund*	A £4.8 billion fund for 'shovel-ready' infrastructure projects across the UK. This money will be spent up to 2024/25. Bids for the first round of funding were submitted between March and June 2021, and final decisions will be made in autumn 2021.
Towns Fund*	A £3.6 billion fund for towns in England, including money for the regeneration of high streets. A total of 101 towns were eligible to bid for up to £25 million each for Town Deals, with the allocation of funding announced in July 2021. ⁹ Funding will predominantly be for investment, focusing on: <ul style="list-style-type: none"> • Urban regeneration, planning and land use • Skills and enterprise infrastructure • Connectivity.
Community Renewal Fund*	A £220 million fund for the whole of the UK in 2021/22, which aims to provide a bridge between EU structural funds and the planned new UK Shared Prosperity Fund (UKSPF). The majority of the funding is revenue funding, with a small amount of capital funding. Projects must align with at least one of the following priorities: <ul style="list-style-type: none"> • Skills • Supporting people into employment • Local business • Communities and place.
Skills Fund	A £2.5 billion fund for adult skills, including a guarantee of free access to level 3 qualifications and funding for skills boot-camps.
Freeports*	Low-tax and low-tariff business zones. Locations bid to become freeports and eight were selected and announced at the March 2021 budget.
UK Infrastructure Bank	A new government-owned bank that will be able to finance infrastructure projects. The bank will have £12 billion of capital for lending and investment, and the authority to issue up to £10 billion of guarantees.
Civil service relocation	Movement of civil service jobs away from London and the south-east of England, with a target to move 22,000 jobs by 2030.

* Denotes centrally managed funds or projects where places bid for selection.

A longer list of local funding pots [1]

- subject to central allocation decisions

- Levelling-up Fund
- UK Shared Prosperity Fund
- Towns Fund
- Transforming Cities Fund
- Better Care Fund
- Brownfield Land Release Fund
- National Home Building Fund
- Housing Infrastructure Fund
- Cultural Investment Fund
- Discover England Fund
- Shared Outcomes Fund
- Air Quality Grant
- Green Jobs Challenge Fund

A longer list of local funding pots [2]

- subject to central allocation decisions

Contain Outbreak Management Fund

Nature for Climate Fund

Green Recovery Challenge Fund

Flexible Childcare Fund

Care and Support Specialised Housing Fund

National Skills Fund

National Security Strategic Investment Fund

Cultural Investment Fund

Museums Infrastructure Fund

Refugee Transitions Outcomes Fund

Local Sustainable Transport Fund

Potholes Fund

Natural Environment Investment Readiness Fund

Restart Fund

Conclusions

- The UK economic situation is self-evidently rather better than expected a year (or even six months) ago
 - But, Ukraine...
- Both Covid-19 and Brexit will have long-term 'scarring' effects
- 'Austerity' appears to be over, but the NHS is again the big winner
- Local government appears to have benefited from having a more powerful Secretary of State
- Council tax and NNDR are here to stay and probably will not be reformed much
- Fair Funding Review? Levelling Up/Devolution?

The economic and political horizon Implications for the UK's public finances

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