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Still five more years of austerity to go?

Paul Johnson

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Big picture

- Deficit of around £90 billion this year
  - As a fraction of national income that is half its post crisis peak
- But very much higher than planned in 2010
  - As a result of poor economic performance 2010-12
- Debt approaching 80% of national income
- Substantial additional "austerity" will be required
  - With significant differences between the parties

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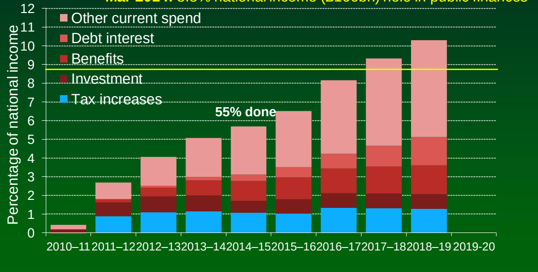
The cure (March 2014): 10.3% national income consolidation over 9 years (£194bn)



Notes: All monetary figures are expressed in 2015–16 terms.
Sources: HM Treasury; OBR; Author's calculations.

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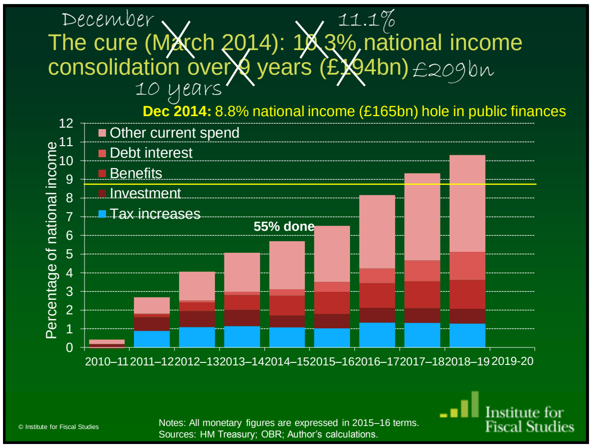
December
11.1%
The cure (March 2014): 10.3% national income consolidation over 9 years (£194bn) £209bn
10 years
Dec 2014: 8.8% national income (£165bn) hole in public finances
Percentage of national income
Other current spend
Debt interest
Benefits
Investment
Tax increases
55% done
2010–11 2011–12 2012–13 2013–14 2014–15 2015–16 2016–17 2017–18 2018–19 2019-20
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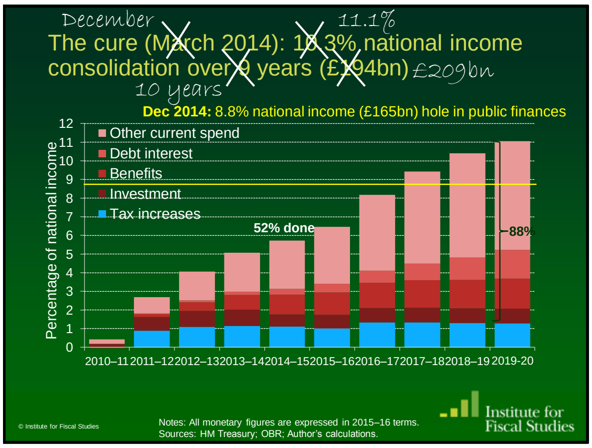
December
11.1%
The cure (March 2014): 10.3% national income consolidation over 9 years (£194bn) £209bn
10 years
Dec 2014: 8.8% national income (£165bn) hole in public finances
Percentage of national income
Other current spend
Debt interest
Benefits
Investment
Tax increases
52% done
88%
2010–11 2011–12 2012–13 2013–14 2014–15 2015–16 2016–17 2017–18 2018–19 2019-20
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Notes: All monetary figures are expressed in 2015–16 terms.
Sources: HM Treasury; OBR; Author's calculations.
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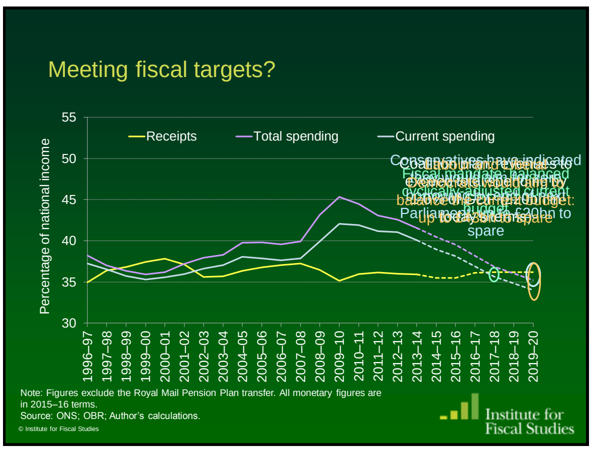
Meeting fiscal targets?
Percentage of national income
Receipts
Total spending
Current spending
Note: Figures exclude the Royal Mail Pension Plan transfer. All monetary figures are in 2015–16 terms.
Source: ONS; OBR; Author's calculations.
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Progress on spending to date

- How much of the planning spending cut has been achieved to date depends on the definition used
- Prime Minister has favoured "Total spending less debt interest" focussing on a £25bn cut over 2016–17 and 2017–18
  - on the same basis now a £30bn cut over those two years
  - more importantly a £38bn cut over five years to 2019–20
  - compares to £11bn cut over four years to 2014–15, so only 23% of the planned 2010–11 to 2019–20 cut done by end 2014–15
  - Partly due to faster growth in pension benefits over the earlier period
- Focus here on "Departmental Expenditure Limits" (DEL)
  - spending by Whitehall departments on admin and services
  - 39% of the planned 2010–11 to 2019–20 cut done by end 2014–15

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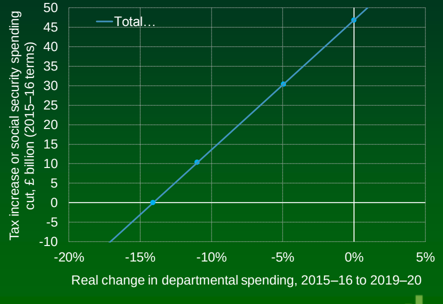
How could future tax increases/welfare spending cuts change the picture?



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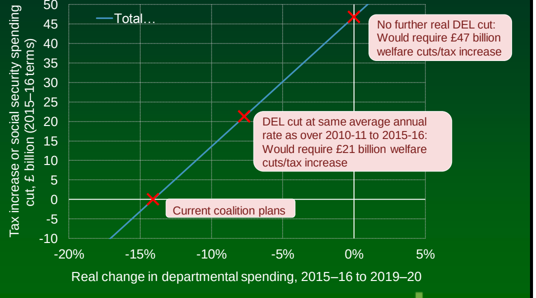
How could future tax increases/welfare spending cuts change the picture?



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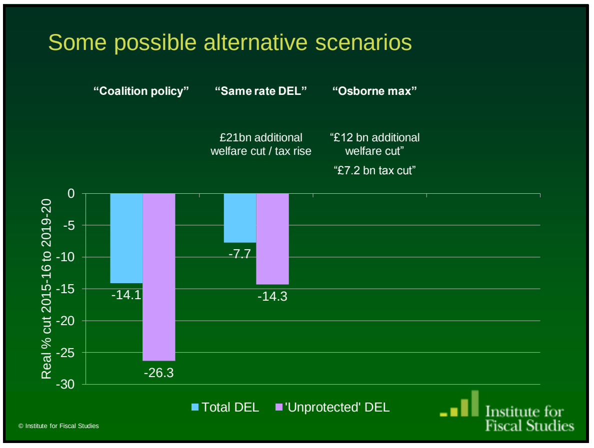
Some possible alternative scenarios
“Coalition policy”
“Same rate DEL”
“Osborne max”
£21bn additional welfare cut / tax rise
“£12 bn additional welfare cut”
“£7.2 bn tax cut”
Real % cut 2015-16 to 2019-20
0
-5
-10
-15
-20
-25
-30
-14.1
-26.3
-7.7
-14.3
Total DEL
'Unprotected' DEL
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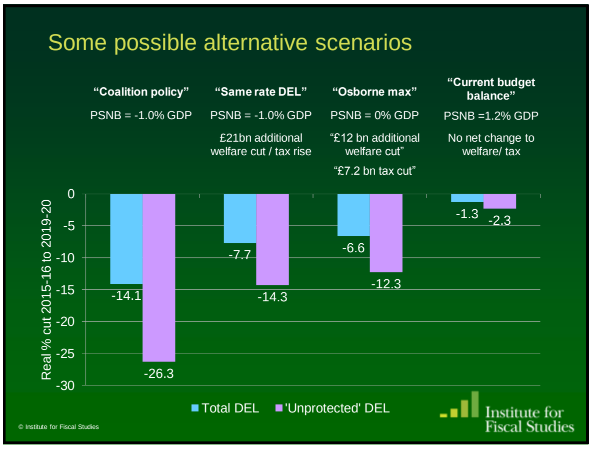
Some possible alternative scenarios
“Coalition policy”
PSNB = -1.0% GDP
“Same rate DEL”
PSNB = -1.0% GDP
£21bn additional welfare cut / tax rise
“Osborne max”
PSNB = 0% GDP
“£12 bn additional welfare cut”
“£7.2 bn tax cut”
“Current budget balance”
PSNB =1.2% GDP
No net change to welfare/ tax
Real % cut 2015-16 to 2019-20
0
-5
-10
-15
-20
-25
-30
-14.1
-26.3
-7.7
-14.3
-6.6
-12.3
-1.3
-2.3
Total DEL
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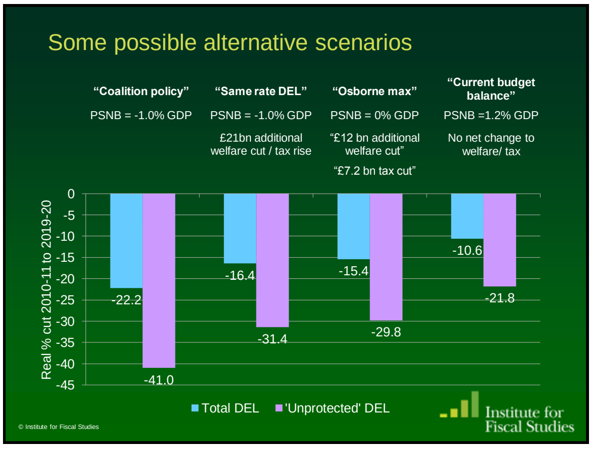
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PSNB =1.2% GDP
No net change to welfare/ tax
Real % cut 2010-11 to 2019-20
0
-5
-10
-15
-20
-25
-30
-35
-40
-45
-22.2
-41.0
-16.4
-31.4
-15.4
-29.8
-10.6
-21.8
Total DEL
'Unprotected' DEL
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The cost of higher borrowing

- Any additional spending financed from higher borrowing would result in higher debt and a greater proportion of spending going on debt interest spending
- Running a current budget surplus (borrowing 1.2% GDP) from 2017-18 onwards rather than coalition plans and zero borrowing in 2019-20 would result in:
  - 2.4% national income higher debt in 2020-21
  - £1.5 billion higher debt interest payments (2015-16 terms)
- Impact would be larger if higher levels of borrowing are maintained in the longer term
  - E.g. see HMT projections in chart 1.9 (p27) of Autumn Statement

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Summary

- Current coalition plans imply large cuts to departmental spending still to come
  - Cumulative cuts over whole consolidation could reach 22% for all departmental spending, and 41% for unprotected areas
- Cuts beyond 2015-16 could be reduced by further welfare spending cuts, tax increases and/or higher borrowing
- Tory, Labour and Lib Dem fiscal rules all allow for greater borrowing than currently forecast under coalition policy
  - Tories to a lesser extent than Labour/Lib Dems as aiming for zero borrowing rather than borrowing up to amount spent on investment
- Any additional spending financed from higher borrowing would result in higher debt and a greater proportion of spending going on debt interest spending
  - Impact would be relatively small up to 2019-20; would be larger if higher levels of borrowing are maintained in the longer term

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