Our fiscal future

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• The spending review period and medium term outlook
• The long term outlook
The hole in the public finances

Permanent damage = 7.5% of GDP (£114bn)

Notes and sources: see Figure 3.6 of The IFS Green Budget: February 2012.
The cure (November 2011): 8.1% national income consolidation over 7 years

**Nov 2011**: 7.5% national income (£114bn) hole in public finances

Notes and sources: see Figure 3.5 of *The IFS Green Budget: February 2012*. © Institute for Fiscal Studies
Spending and revenues brought back to pre-crisis levels

Notes and sources: see Figure 3.6 of The IFS Green Budget: February 2012.
6-year squeeze on public service spending

Note: Figure shows total public spending less spending on welfare benefits and debt interest.
Pattern of DEL changes 2010-11 to 2014-15

- International Development: 37.8%
- Energy and Climate Change: 6.5%
- NHS (England): 1.0%
- Defence: -8.2%
- Education: -11.9%
- Total: -11.5%
- Transport: -14.5%
- CLG: Local Government: -20.7%
- Home Office: -22.0%
- Justice: -27.2%
- Environment, Food and Rural Affairs: -27.6%
- Business, Innovation and Skills: -31.2%
- Culture, Media and Sport: -46.1%
- CLG: Communities: -71.3%

Percentage real increase, 2010–11 to 2014–15

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Similar priorities (in different directions)

Notes and sources: see Figure 3.12 of The IFS Green Budget: February 2012.
Household incomes falling to unprecedented degree

Sources: Department for Work and Pensions’ HBAI series; IFS calculations and projections using Family Resources Survey.
Continuing change in the shape of the state

- Health, social protection and education account for two thirds of public spending
- Up from less than half in 1979
- Increase results from health and social protection
  - Education has merely maintained its share
- Defence, housing and support for business and industry have taken the strain
Public spending in 2010-11

- Social protection: 29%
- Personal social services: 10%
- Health: 6%
- Education: 6%
- Transport: 5%
- Defence: 5%
- Public order and safety: 4%
- Gross debt interest: 3%
- Housing: 3%
- Other: 2%
- TIEEEE: 2%
- AFF: 1%
Public spending in 1978-79

- Social security: 23%
- Personal social services: 9%
- Health: 9%
- Education: 9%
- Transport: 6%
- Defence: 4%
- Law, order & protection: 4%
- Gross debt interest: 2%
- Housing: 2%
- TIEEE: 1%
- AFFF: 1%
- Other: 10%
Going forward state is set to change further

- Demographics will drive further change
- OBR projections suggest that health and pensions alone could account for more than a half of non-interest spending by 2060
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- OBR projections suggest that health and pensions alone could account for more than a half of non-interest spending by 2060
- And there are additional pressures on tax receipts
  - Notably on petrol and from north sea oil
  - Perhaps from corporation tax
This creates some major pressures

• At least another £100 billion in tax rises or spending cuts will need to be found over a – relatively long – period from 2020

• Three core drivers:
  – Demographics
  – Structure of spending commitments
  – Stability of tax base
This creates some major pressures

- At least another £100 billion in tax rises or spending cuts will need to be found over a – relatively long – period from 2020
- Three core drivers:
  - Demographics
  - Structure of spending commitments
  - Stability of tax base
- There are only three choices:
  - Increase total taxes to accommodate pressures
  - Reform and rein in health and pension spending
  - Cut other areas of spending
Conclusions

• £114 billion hole in public finances
• Planned fiscal consolidation: 8.1% of national income
  – Most of the spending cuts are still to come
• Long term squeeze on household incomes
  – Real increases in energy prices a big issue for those on low incomes
• The longer term outlook is daunting too
  – Continued move to the “welfare state” offers challenges
  – Main sources of “environmental” taxation are falling