July 2026 *Fiscal risks and sustainability report*

Transcript of Presentation by:

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1. Opening slide

- Thanks, Laura.

- Good morning, everyone.

- In this report we examine long-term pressures on public spending and revenues, and their implications for fiscal sustainability.

2. International government borrowing and debt

- It is important to first put this analysis in the context of the challenging current fiscal position in the UK. These two charts show that:

    - On the left, UK government borrowing, shown in the green line, has been consistently higher than averages of comparable countries for the past 20 years, and has been at around 5 per cent of GDP since Covid, a relatively high level historically and internationally, though it fell to 4.3 per cent of GDP last year.

    - On the right, as a result of this high borrowing, UK debt has tripled over the past 20 years, taking it from close to the advanced-economy average, to 45 per cent of GDP above.

- The Government's current fiscal plans would bring borrowing down to around 2 per cent of GDP by 2030, which would be enough to stabilise debt.

- But there are short- and medium-term risks to this, not least from the impact of the conflict in the Middle East, which we will assess in our next medium-term forecast.

- Given these challenges, it is more important than ever that there is also an understanding of the longer-term pressures on the public finances.

3. Assessing long-term fiscal sustainability

- We illustrate this through a series of 50-year fiscal projections.

- Long-term analysis such as this is clearly highly uncertain – to address this we produce multiple different scenarios to show the impact of varying key assumptions.

- In almost all of these scenarios the public finances move on to an unsustainable path – and if this started to happen future governments would in reality have to take action to prevent it.

- So these scenarios should not be seen as precise forecasts. They are illustrations of long-term fiscal pressures and whether the public finances are sustainable under current policy settings.

- To represent current government policy settings over the long term, in some cases there are clear long-term policy commitments that we can use.

- But typically this is not the case, so we have to make assumptions – and when these are material we produce scenarios showing the impact of alternative choices.

4. Population projections

- The basis for the scenarios is the ONS's latest long-term projections for the UK population.

- In these, the population rises from nearly 70 million now to around 73 million in the mid-2050s before starting to fall.

- And the age structure becomes older, shown by the rightward shift from the green to yellow line in the chart, with the median age of the population rising from 40 now to 49 in 2075.

5. Tax and spending age profiles

- This matters for the public finances as demand for public services and tax revenue per person varies considerably by age. This chart shows tax and spending age profiles that we have updated for this report. It shows that:

    - Tax revenue, shown in blue, peaks during working age.

    - Public spending is higher at younger ages, mainly due to education, shown in green…

    - …But public spending is particularly higher at older ages, due to the costs of health, shown in yellow, and pensions, shown in purple.

6. Baseline long-term public spending scenario

- These demographic trends are an important driver of long-term pressures on public spending.

- In our baseline scenario, these and other pressures would push public spending up by around 9 per cent of GDP, from 40 per cent of GDP in 2030 to 49 per cent by 2075. The main upward pressures are:

    - The older population increasing demand for **health**, but also, an assumption that health spending will increase further due to wider cost pressures, shown in purple.

    - The older population also increases the cost of the **state pension**, shown in blue.

    - But there are also non-demographic upward pressures on spending: the largest, outside health, is the commitment for **defence spending** to reach 3.5 per cent of GDP by 2035, shown in yellow.

7. Baseline long-term tax scenario

- The main long-term pressure that we identify on taxation comes from the loss of fuel duty and other emissions-related taxes due to the transition to net zero. There is also a small loss of revenue from the ban on tobacco purchases for those born from 2009. Together these would act to push revenue down slightly over the long term, shown in the yellow line.

- The demographic changes which push up on spending are expected to have a much more muted upward effect on tax receipts, and combining these with the net zero pressures produces the green line.

- So overall, these long-term trends leave receipts relatively stable over the 50-year period.

- Both these and the spending projections I outlined previously are based on our main assumptions for unchanged government policy. I will set out the impact of using different policy assumptions later.

8. Baseline fiscal scenario

- In our baseline fiscal scenario, using these tax and spending scenarios, a gap opens up between the two over the next 50 years, shown in the left chart, primarily due to the upward pressures on spending that I have described.

- As a result, government borrowing would rise and debt would move onto what would be an unsustainable ever-upward path from around the 2040s, shown in the chart on the right.

9. Net debt: sensitivity in debt dynamics scenarios

- However, there are plausible alternative scenarios where this upward path for debt starts earlier and is steeper:

    - The starting point for the baseline scenario is the latest medium-term forecast for the primary deficit – which is a measure of borrowing that excludes interest costs. This is forecast to improve to reach a *surplus* of 1.5 per cent of GDP in 2030, driven by the Government's current fiscal consolidation plan. This would be the largest primary surplus since 2000.

    - However, successive recent governments have set out similar medium-term plans to consolidate the public finances, which have subsequently been pushed back. If the projections were to instead start from a **primary deficit at the 2026 level**, of a 1.4 per cent *deficit*, the unsustainable upward trajectory in debt starts in the 2030s, shown in the yellow line.

    - The baseline scenario also assumes steady economic growth across all 50 years. But it is almost inevitable that the economy will be hit by **major shocks** in the future, and recent experience is that these are very costly for the public finances. If we additionally assume the UK is hit by major negative shock every 10 years, as has happened in the recent past, then the upward path for debt steepens further, shown in the blue line.

    - Finally, if we assume that there is also feedback from higher debt levels to **higher interest rates** on government borrowing, then debt moves on to an explosive path which would very quickly be unsustainable, shown in the purple line.

10. Net debt: sensitivity to economic and demographic assumptions

- We also look at the sensitivity to other key economic and demographic assumptions.

- This includes a scenario with higher **population** growth than in the baseline due to more assumed births and fewer deaths.

- This leads to slightly more pressure on the public finances due to higher spending on education, health and pensions, which is not fully offset by higher tax revenues from a larger working-age population, shown in the yellow line.

- We also consider scenarios around our baseline assumption of 1 per cent average annual total factor **productivity** growth across the 50 years, which is a highly uncertain assumption:

    - If we instead assume the much lower post-financial crisis average of 0.3 per cent total factor productivity growth, then debt would move much more quickly onto a path which is clearly unsustainable, shown in the blue line.

    - But, if we assume a return to the much higher pre-crisis average of 1.3 per cent annual total factor productivity growth, then, assuming governments use some of the proceeds of this higher growth to improve the fiscal position, the increase in debt would be much delayed and shallower, shown in the purple line.

    - In practice, past governments have often spent the upside from economic growth – so maintaining a broadly constant spending-to-GDP ratio even when economic growth has been strong. In a scenario where this continues, there would be a much more limited fiscal benefit from higher productivity, shown in the dashed purple line.

11. Net debt: sensitivity to long-term policy assumptions

- Finally, we look at the impact of using alternative assumptions for unchanged long-term government policy.

- In the baseline scenario we assume that the **state pension** is uprated by the triple lock – the highest of earnings, CPI inflation, or 2.5 per cent. If instead we assume that the state pension is uprated with earnings, which is the main assumption we use for the rest of tax and spending upratings, this would reduce debt by 2075 by around one-tenth compared to the baseline, shown in the yellow line.

- The policy variant with the largest impact on the projections relates to the uprating of **personal tax thresholds**. Our baseline assumption is that these are uprated each year with earnings. This is consistent with most of our wider assumptions on unchanged policy across tax and spending, and would leave the effective tax rate on labour broadly constant over the 50 years.

- However, medium-term policy is to uprate with inflation, and governments have in fact chosen to freeze thresholds in the 10 years from 2021 to 2031. If we assume inflation uprating of personal tax thresholds over 50 years this would reduce debt in 2075 by around half compared to the baseline, shown in the red line. This is because large numbers of taxpayers would be pulled into paying higher tax rates as their earnings rise more quickly than the thresholds.

- However, this only reflects the direct fiscal effect of this assumption – it does not take account of the likely substantial impact this would have on the labour market, given:
    - it would be equivalent to a 50 per cent increase in the effective tax rate on labour;
    - around two-thirds of taxpayers would pay at least the 40 per cent higher rate of tax; and
    - a full-time worker on the minimum wage would start to pay the higher rate from around the 2060s.
- We also look at two further policy variants: one where we assume **non-pension welfare payments** are uprated by inflation rather than our main assumptions of earnings; and one where governments constrain wider growth in **health costs**. In both these scenarios, debt is around a third lower than in the baseline scenario by 2075.

12. Primary balance adjustment paths

- Overall, in nearly all of these scenarios, debt eventually moves on to an ever-upward path that would be unsustainable.
- If these paths were to start to materialise, it is almost certain that future governments would have to take action to put the public finances back on a sustainable path.
- Doing this earlier would be less costly than delaying the required fiscal adjustment. This chart shows three illustrative scenarios for adjusting the primary deficit to keep debt at the current level of 95 per cent of GDP in the baseline scenario.
- Taking immediate action, shown in the green line, requires a smaller overall permanent adjustment than one that is either phased, shown in yellow, or delayed, shown in blue.

13. Conclusions

- What are the main conclusions that we draw from all these scenarios?
- First, it is important to underline again that these scenarios should not be seen as forecasts – they are illustrations of the possible fiscal implications of long-term pressures on public spending and revenue, in the unlikely event that future governments do not take action to address them.

- But they all generally point in the same direction – in nearly all of the scenarios, with our assumptions for unchanged government policy, public debt at some point in the future would move on to an ever-upward trajectory that would be unsustainable.

- This point is in the 2040s in the baseline scenario. But there are plausible scenarios where it happens as early as the 2030s – for example if the level of borrowing does not fall as planned over the next few years and the economy is hit by another major shock.

- There are also some scenarios where the upward trajectory for debt is delayed and much shallower. For example, this is the case where we assume sustained higher productivity growth than in the baseline. Although this is only if future governments choose to use the proceeds of higher growth to maintain fiscal sustainability, rather than simply to increase spending further.

- However higher population growth – though it could lead to higher aggregate GDP – may not improve the fiscal outlook because of the pressures on education and health spending from more younger and older people.

- Choosing to address these fiscal challenges over the long term primarily through higher tax – for example as in the scenario where personal tax thresholds are uprated with inflation over 50 years – is likely to generate rising economic distortions and costs. So it is likely that action over the long term would need to be spread across many different policy areas.

- And an important conclusion is that earlier action reduces risk and is likely to be less costly over the long term:

    - The required reduction in the deficit to maintain debt at current levels relative to GDP could be twice as large if implemented in the middle of the century, rather than in the early 2030s.

    - And the longer debt is allowed to rise, the greater the risk of higher interest rates compounding the challenge, or a sudden adverse investor reaction taking place.

- Overall, the significant uncertainty around these projections should not be used as an excuse for inaction – unsustainable fiscal outcomes that may not occur for some years are today's challenge not just tomorrow's.