Foreign & Commonwealth Office

UK Fiscal Consolidation

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Presentation to EUIJ Waseda Symposium

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Background facts

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1. UK– sixth largest global economy
2. Diverse economy
3. Member of the EU, but we have not adopted the Euro
4. Coalition government – elected May 2010

UK Government spending

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1. Social protection £200bn
2. Health £126 bn
3. Education £89bn
4. Debt interest £50bn
5. Defence £40 bn
6. Public order and safety £33bn
7. Personal social services £32bn
8. Housing and environment £24 bn
9. Transport £23 bn
10. Industry, agriculture and employment £20bn
11. Other expenditure £74 bn

UK Government receipts

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1. Income tax £158bn
2. National insurance £101 bn
3. VAT £100bn
4. Corporation tax £48bn
5. Excise duties £46bn
6. Council tax £26bn
7. Business rates £25bn
8. Other £85 bn

The UK fiscal challenge…

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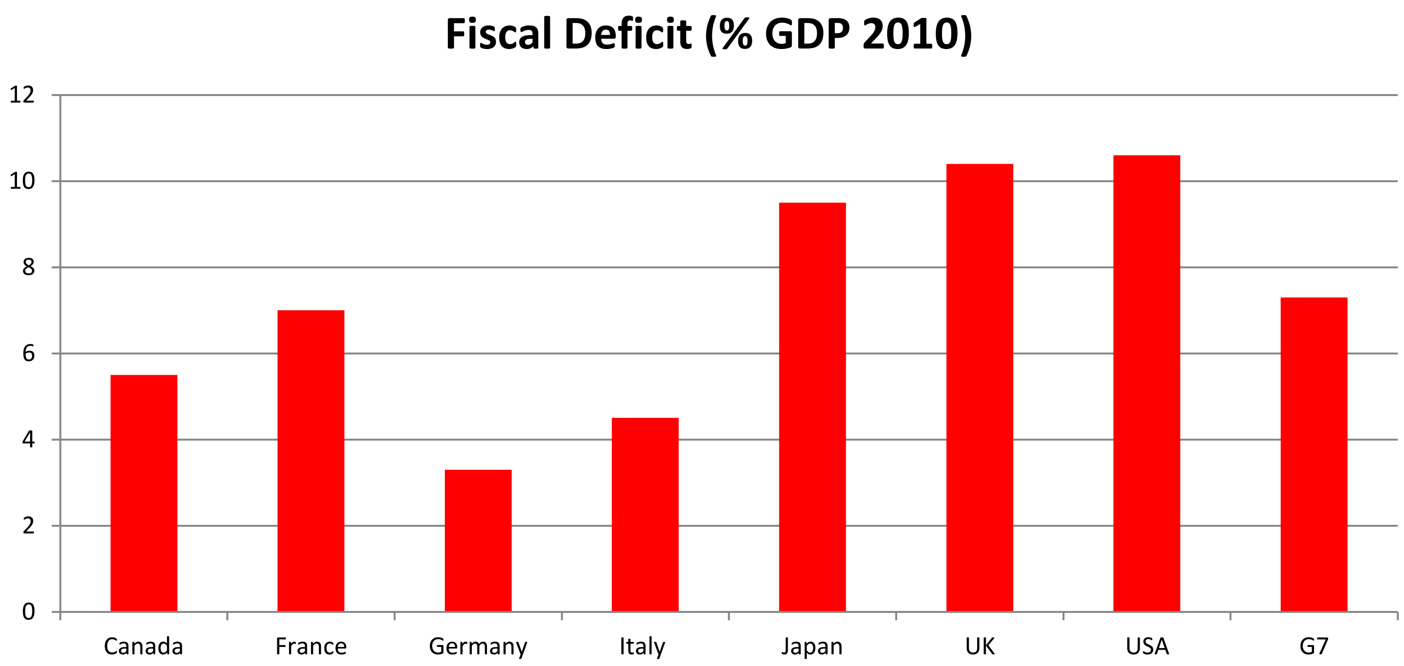

Source data: IMF

➢ The **second largest fiscal deficit as a percentage of GDP in the G7 (and G20)**. Latest official outturn figures shows borrowing reached £143.2 billion in 2010/11.

… but our net debt is low by G7 standards and we have the longest maturity of debt

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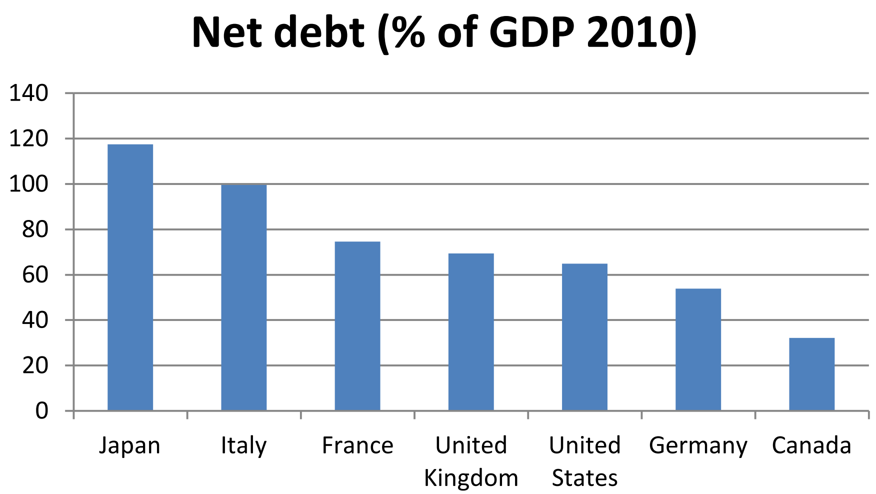
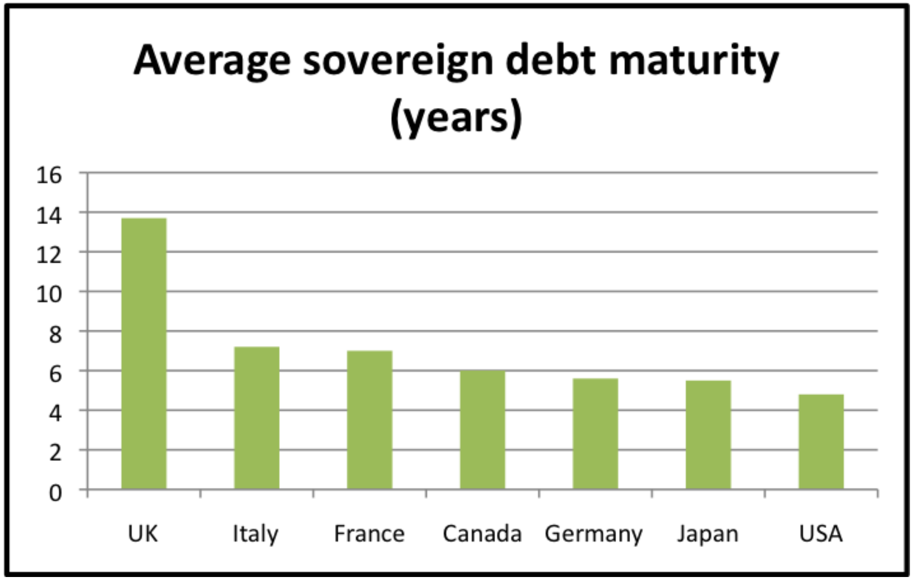


Source : IMF World Economic Outlook Projections ,Apr 2011



Source : The Economist

Low net debt means lower interest payments. Net debt in the UK was around 69% of GDP in 2010 according to latest IMF estimates.

According to the IMF, between 2008 and 2010 the UK saw the largest increase in net debt of all G7 economies.

The average maturity of UK debt is 13.5 years, meaning we need to issue less debt in the near-term, resulting in **less rollover risk**.

UK Government debt is AAA rated, with a "stable" outlook.

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2. The UK Fiscal Framework and the Spending Review

UK fiscal framework is based on a clear and measurable mandate

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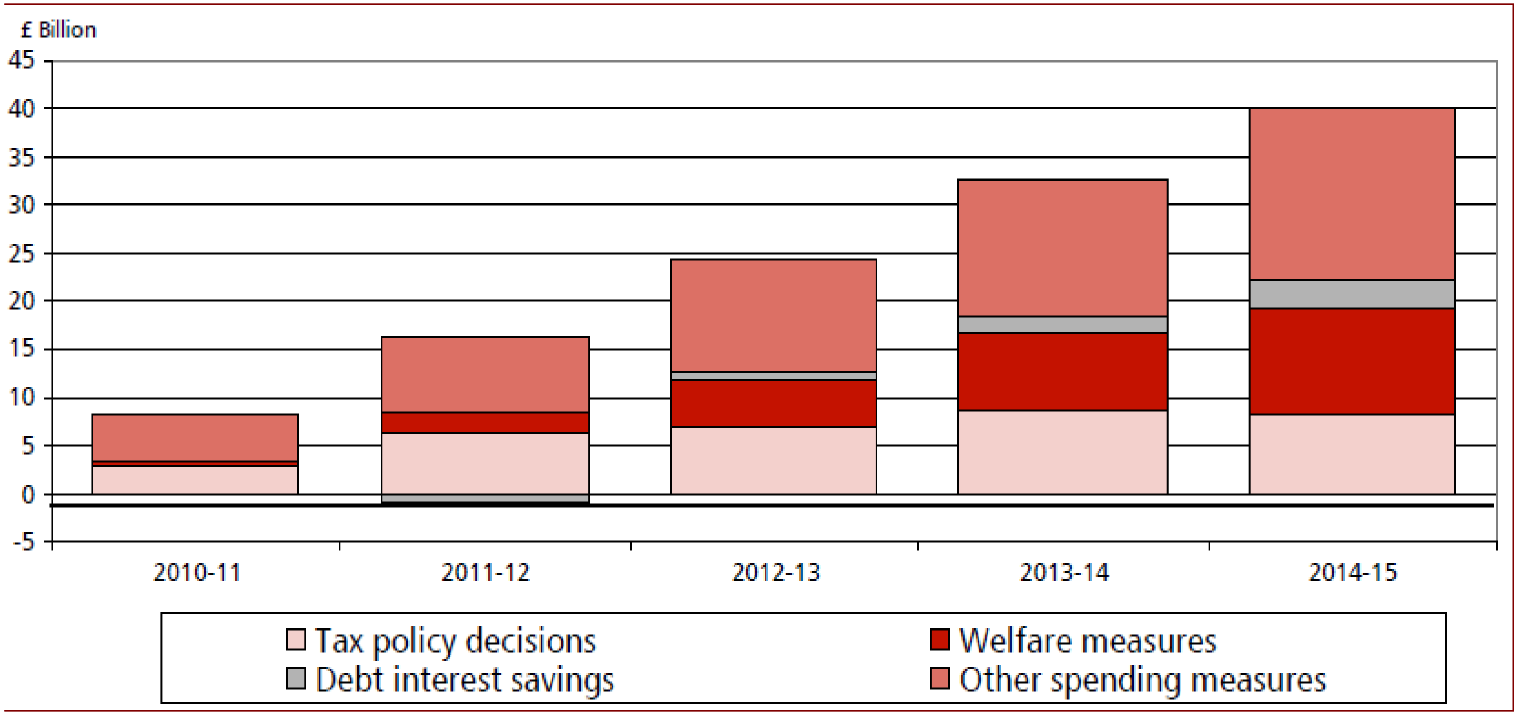
1. **Deficit target:**
   - To achieve cyclically-adjusted current balance by 2015-16
2. **Debt target:**
   - Net debt as a share of GDP to be falling by 2015-16

The independent Office of Budget Responsibility (OBR) is responsible for forecasts and judgement on achieving fiscal mandate

Creation of the OBR puts the UK at the **forefront of international best practice**, exceeding the IMF's recommendations on fiscal transparency. The UK is one of the few advanced economies with an independent fiscal agency producing the official fiscal and economic forecasts on which budget decisions are made.

The greatest contribution to fiscal consolidation will come from lower spending rather than tax increases

- By 2014-15, 80% of the additional consolidation measures set out in the Budget will be achieved through spending restraint
- The approach is consistent with advice from the OECD and the IMF, that consolidations which largely rely on spending constraints promote growth more than consolidation via tax increases.



Source: HM Treasury

Comprehensive spending review (1)

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1. Growth

> Review of all capital spending plans undertaken to identify which areas of spend generate the highest economic returns - analysed around 250 projects and programmes

> - Decision to prioritise investment that can underpin the transition to a high-tech, low-carbon economy including:

- Transport capital investment , higher in 2014-15 than in 2005-06 (Road, rail and metro)
- Science
- Regional Growth Fund
- Digital infrastructure
- Low carbon, inc carbon capture and storage, and green investment bank

> - Investment in skills: apprenticeships; school

> Business environment

- Reductions in corporate tax (from 28% in 2010, now 26% and will move to 23% by 2014 – lowest in the G7).

UK: a business friendly enviornment

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- According to the Economist Intelligence Unit, the UK is forecast to have the **strongest business environment** (institutional environment; macroeconomic stability; tax and enterprise policies; labour market; infrastructure; etc) of all major European economies up to 2012.

- The UK is the **easiest place to set up and run a business** in Europe. According to the World Bank, it takes just 13 days to set up a business in the UK, compared to the European average of 32 days.

- According to the Organisation for Economic Co-operation and Development (OECD), the UK has the **fewest barriers to entrepreneurship** in the world.

- Transparency International says that the UK is one of the **most transparent countries in the world**.

Economist Intelligence Unit

World Bank

ORGANISATION FOR ECONOMIC CO-OPERATION AND DEVELOPMENT OECD

TRANSPARENCY INTERNATIONAL the global coalition against corruption

"The UK is the number one location for European headquarters: more overseas companies set up their European headquarters in the UK than anywhere else." UKTI

Comprehensive spending review (2)

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2. Fairness
   - Withdrawal of universal child benefits from higher rate tax payers
   - Capping household benefits
   - Reforming social housing
   - Maintain benefits for the elderly
   - ODA will reach 0.7% of National Income in 2013

Comprehensive spending review (3)

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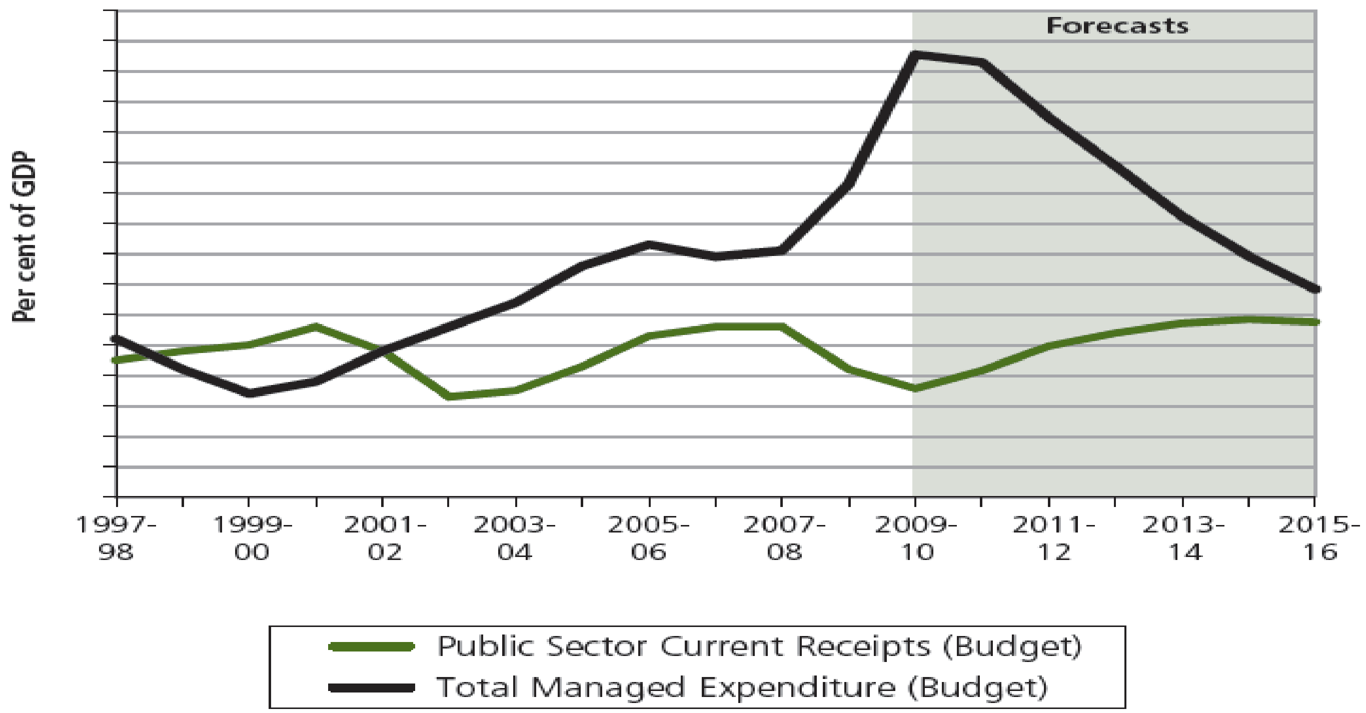
Consumption tax raised from 17.5%- 20% January 2011

3. Public Sector reform

- More responsibility from centre to local decision makers
- Government efficiency – administration budgets reduced by 34% (£5.9bn).
  - Reduction in central government staff by 330,000 staff over four years
  - Greater Efficiency e.g. by central procurement

The Spending Review outlines how the government is tackling the budget deficit

> The OBR forecasts that the Spending Review consolidation plan will:
  - reduce public sector net borrowing from a peak of 11.0 per cent of GDP in 2009-10 to 1.1 per cent of GDP in 2015-16;
  - eliminate the cyclically adjusted current deficit by 2014-15;
  - place net borrowing on a downward path from 2014-15.



Source: HM Treasury, based on OBR forecasts

The UK recovery is likely to be choppy

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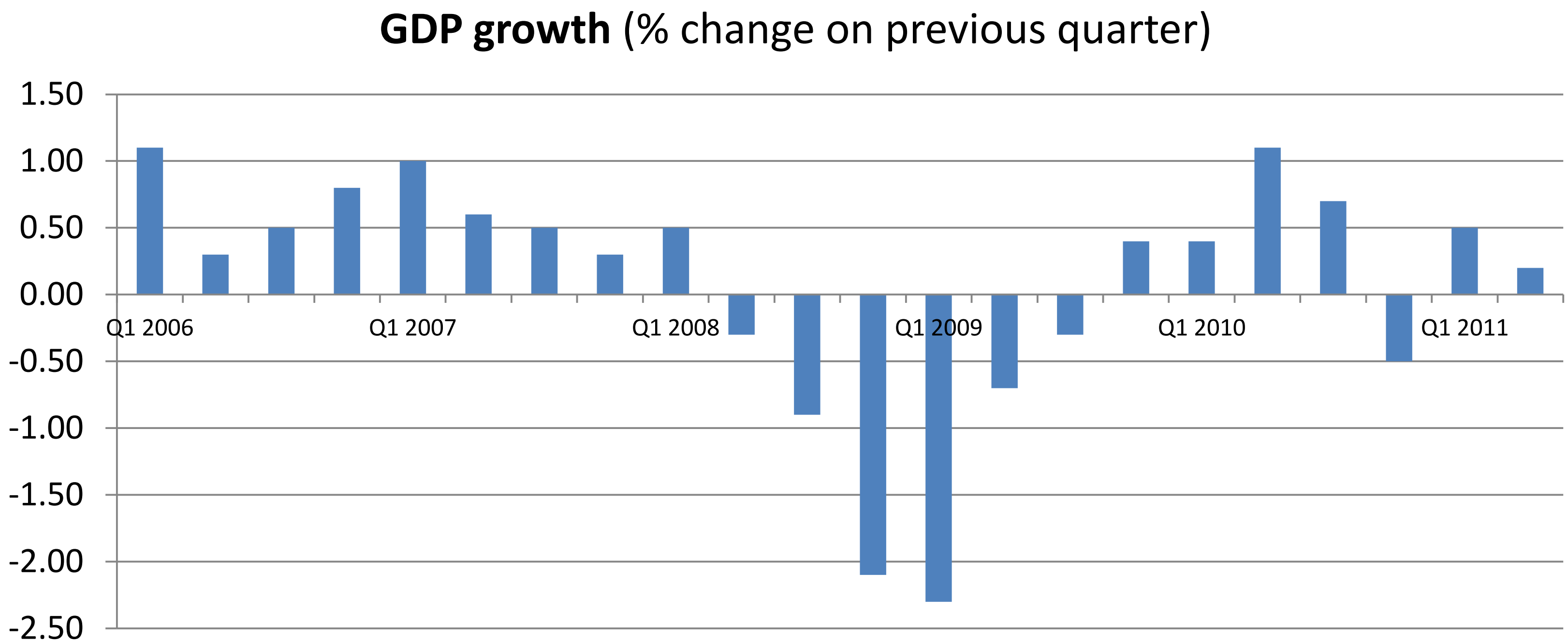

Source: ONS

- After 6 quarters of contraction in 2008 and 2009, GDP growth recommenced in 2010.
- **Growth was 0.2% in Q2 2011,** following an expansion of 0.5% the previous quarter.

Steady growth is predicted for after 2011

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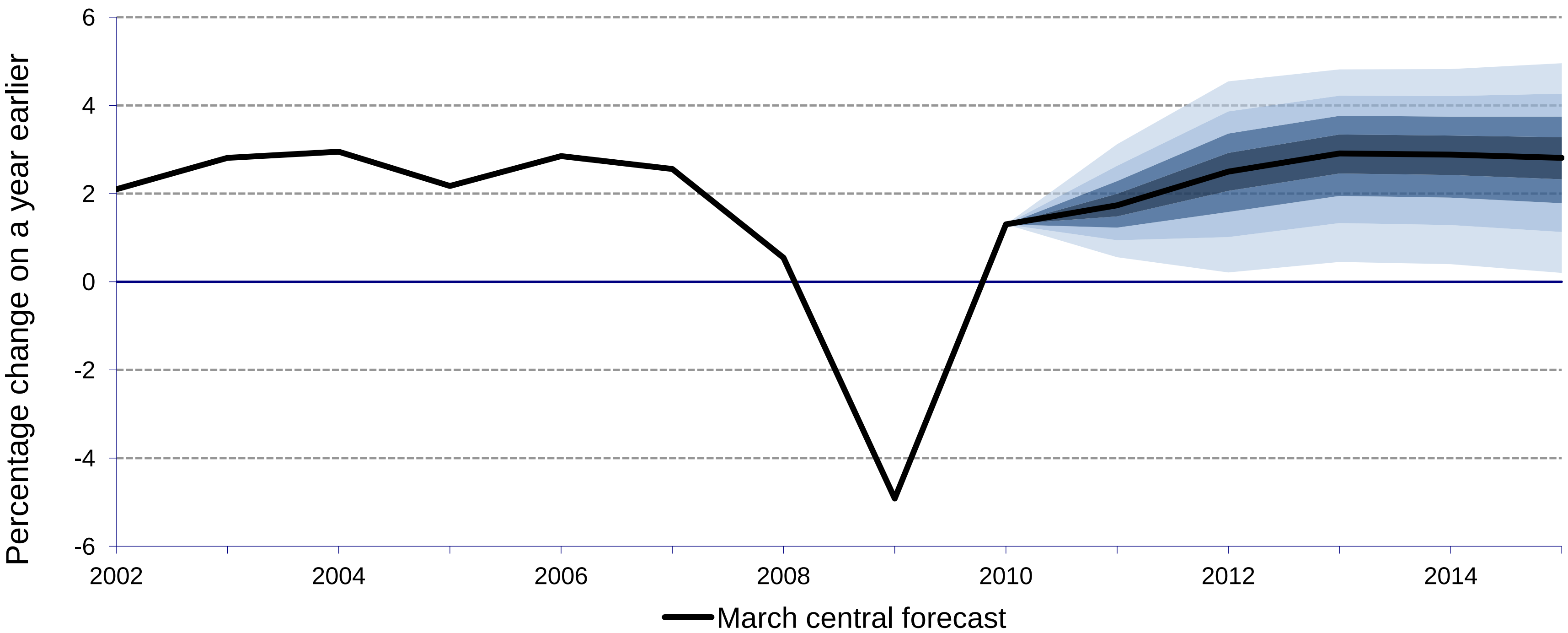
➢ The independent Office for Budget Responsibility (OBR) forecasts **GDP to grow at above-trend rates after 2011** as the private-sector led recovery takes hold and the economy rebalances towards business investment and net trade.

	2011	2012	2013	2014	2015
GDP growth %	1.7	2.5	2.9	2.9	2.8

Source: OBR, Mar 2011



Source: OBR, Mar 2011

Growth forecast strong by G7 comparison

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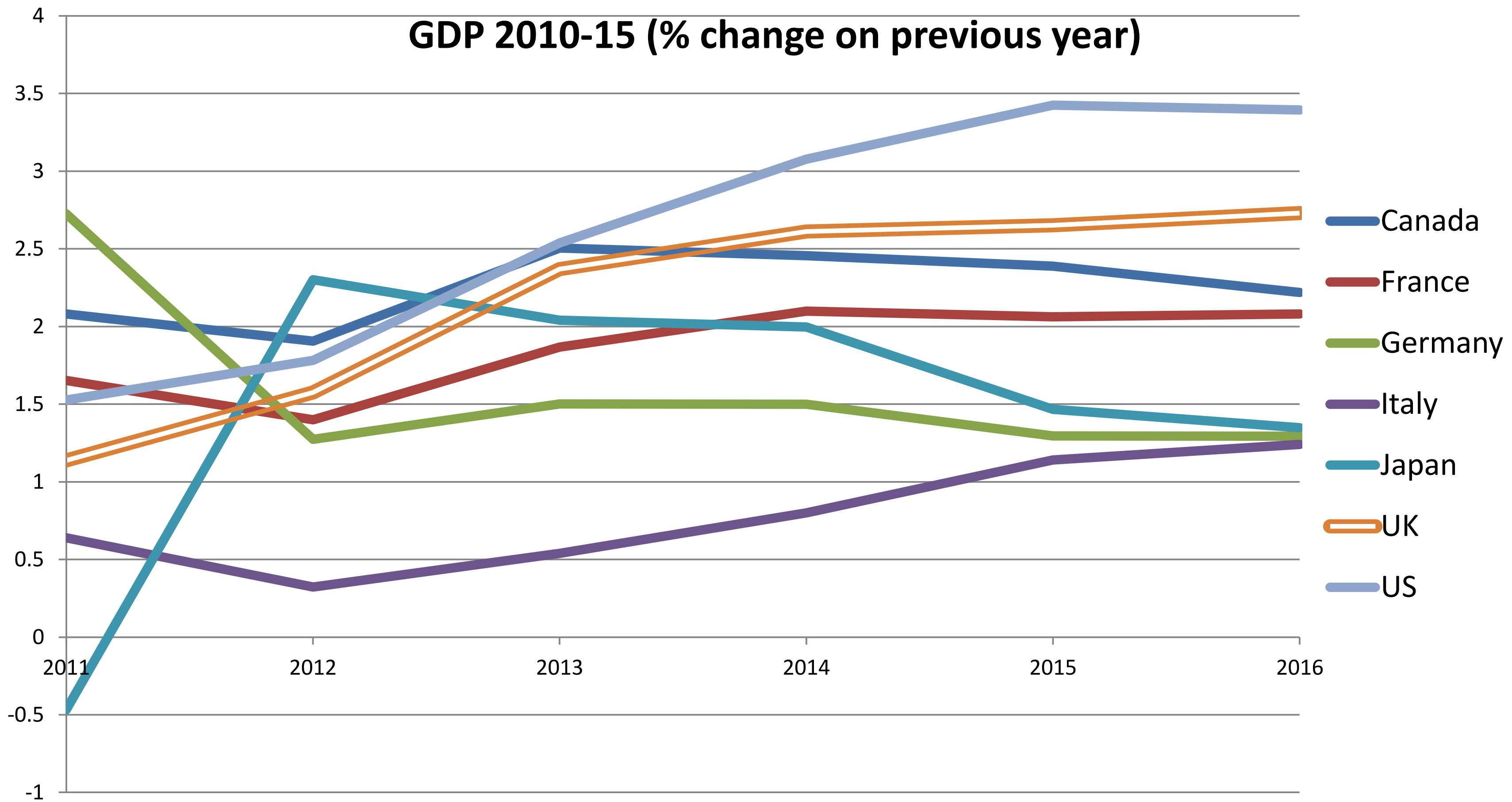
- The IMF expects the UK to grow above 2% from 2013 and to be the second fastest-growing G7 economy from 2014.



Source: IMF World Economic Outlook, September 2011

Lessons

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- Sound public finances are essential for sustainable growth

- We recognised we had a problem with our fiscal deficit and have put in place a credible plan - swift and resolute actions.
  - *Welcomed by markets, IMF, rating agencies etc*
  - It will not be pain free but taking action now will put us on a better footing for the future to enhance our prosperity

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