



Ben Zaranko, Institute for Fiscal Studies

2 December 2025

@TheIFS

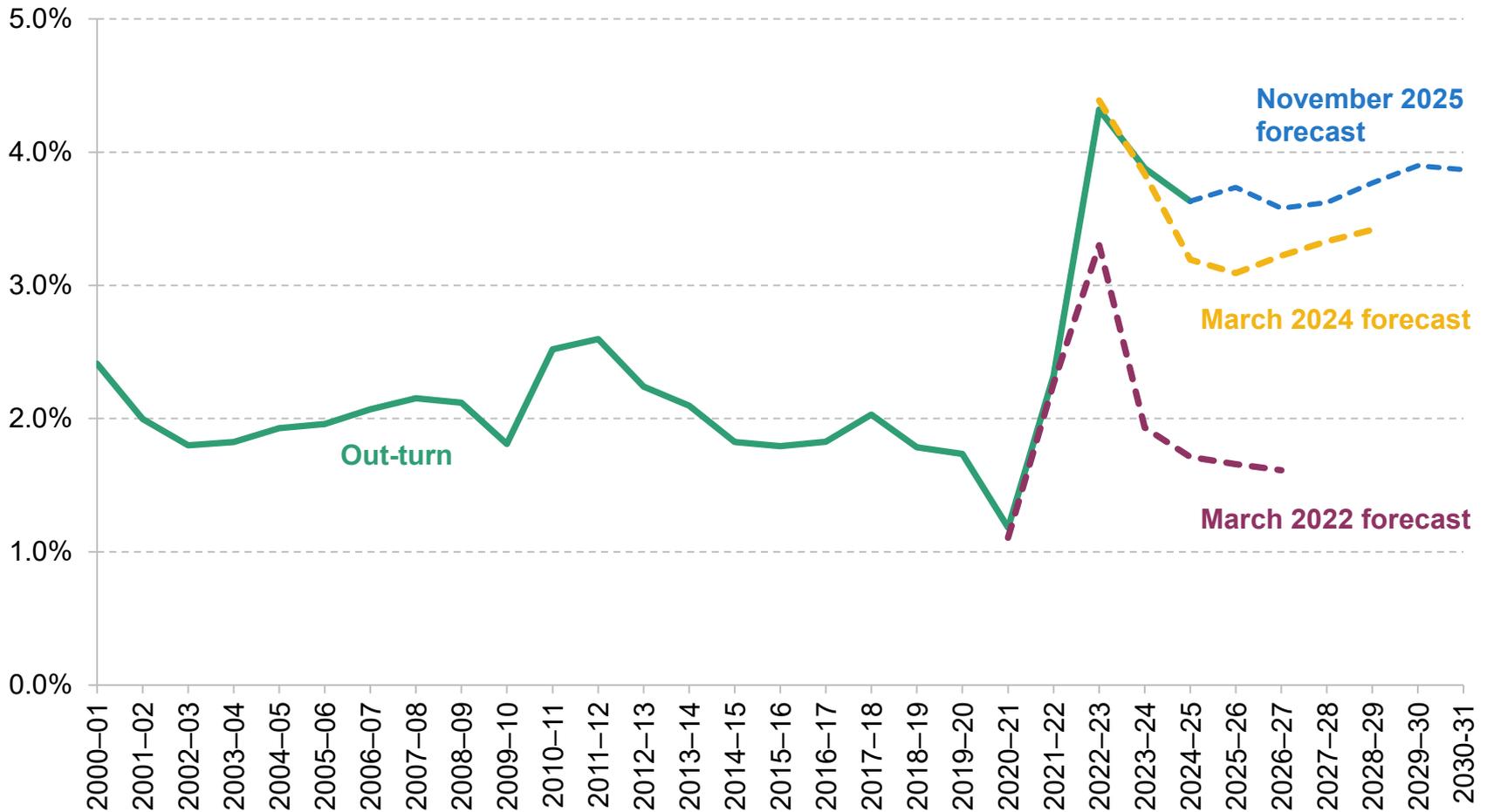
Making sense of the Budget



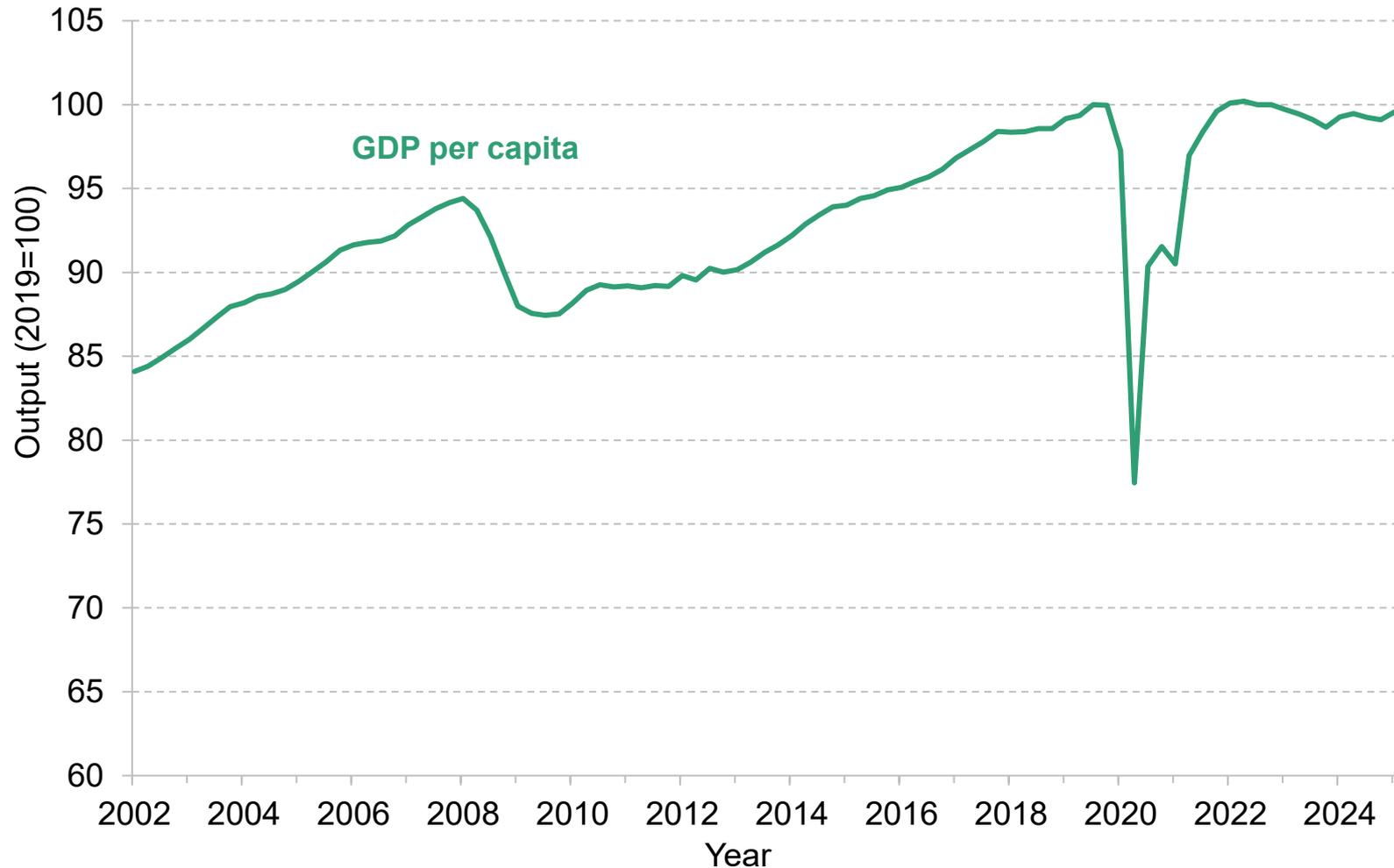
Why the Budget was gloomy

A toxic combination of high debt interest costs...

Debt interest spending as a percentage of national income

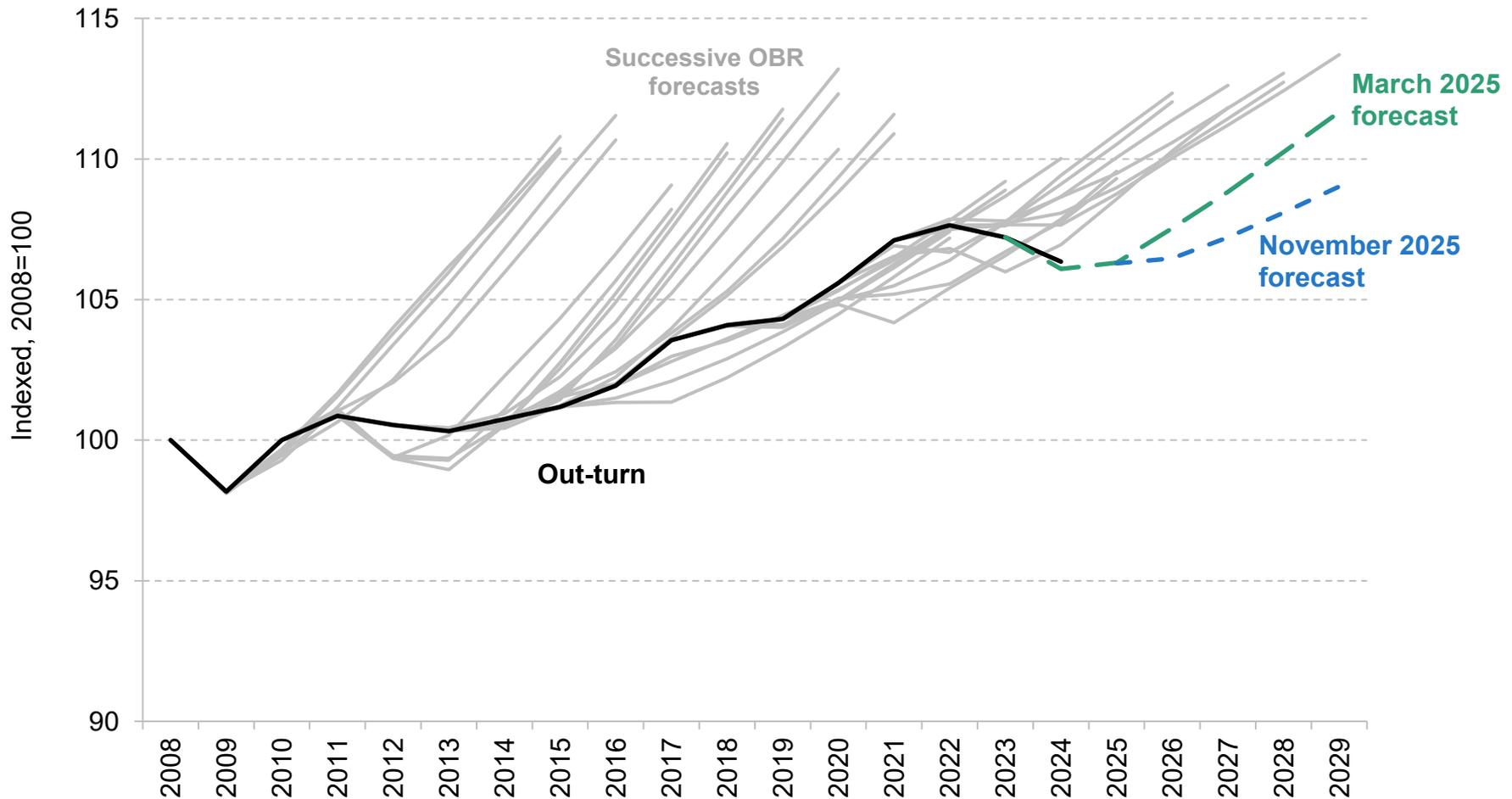


... and abysmal growth performance



The productivity hedgehog

Successive OBR forecasts for productivity since 2010



Source: Office for Budget Responsibility, reproduced and adapted from IFS Green Budget 2025, 'Risks and challenges for the public finances', <https://ifs.org.uk/publications/risks-and-challenges-public-finances>

Living standards are stagnating

Annualised growth in real-terms disposable housing income per person, by parliament



Note: 2015 to 2017 and 2017 to 2019 parliaments have been combined



What actually happened at the Budget?

Big Budget decisions

The outlook for the economy and the public finances got a bit worse (but not by as much as was generally expected)

- Productivity growth down, lots of extra spending pressures, but tax receipts up for other reason: the overall forecast didn't move much
- This matters because we set policy based on a forecast for the future

In the face of that, the Chancellor decided to raise taxes by ~£26 billion

- The biggest measure: a 3-year extension in the freeze in personal tax thresholds, which raises around **£8 billion** ('fiscal drag')
 - (on top of the **£52 billion** already raised via previous threshold freezes)
- Lots of smaller measures, mainly targeting high earners / expensive houses
 - e.g. taxing pension contributions, dividend income, property income, ...
- One particularly interesting tax change worth dwelling on...

Taxing electric vehicles

Background: driving creates negative externalities (pollution, congestion, wear and tear on the roads) – that’s why we tax it

- Government charges fuel duties on petrol and diesel
- As drivers shift to electric cars, creates two problems:
 - Fiscal problem: revenue is shrinking, need to raise other taxes
 - Economic problem: leaves driving under-taxed

The Budget: finally, some effort to tackle the issue

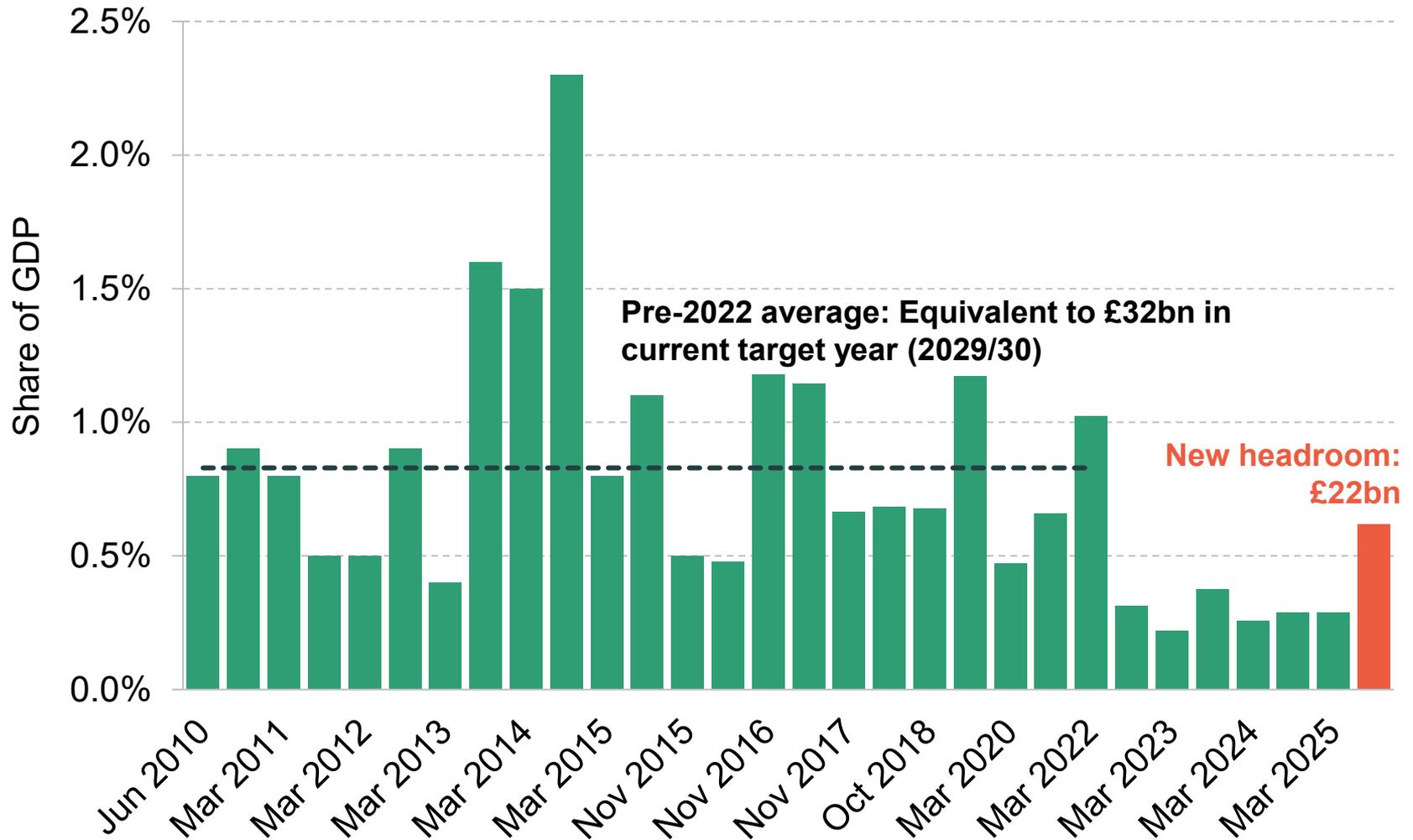
- A new 3p per mile charge for battery electric cars
- Better than nothing! Raises £2 billion by 2030. But...
- The biggest negative externality from driving is congestion – **this tax bears no relation to the congestion a journey creates**
 - We could have done better – the technology exists!

Why raise taxes?

The Chancellor raised taxes for two main reasons:

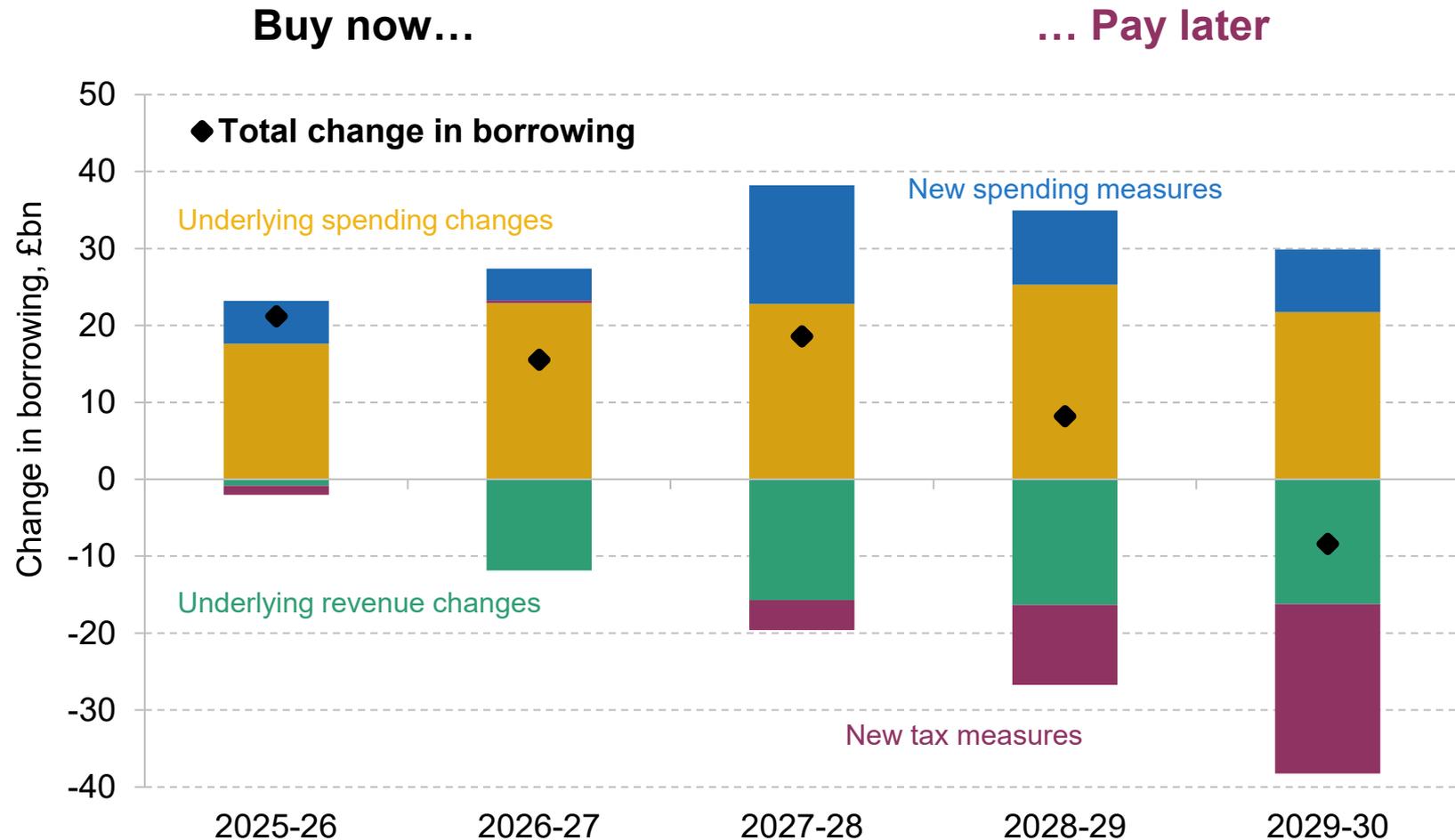
1. To spend more, mainly on social security benefits (£9 billion)
 - Scrapping two child limit (lifts 450,000 children out of poverty)
 - Reversing previous failed attempts to cut other benefits
2. To build a bigger buffer against her fiscal rules
 - The Chancellor has set herself a limit on borrowing
 - She was previously meeting this limit with £10 billion to spare (often called 'headroom') – that has been increased to £22 billion

Fiscal headroom over time



The big risk in the Budget

Change in public sector net borrowing since March by year



Final thoughts

- The Budget was far from a disaster – it had some bright spots
- But it was also a ‘safety first’ Budget, not especially ambitious
 - The UK’s fiscal problems haven’t gone away, and the extra ‘headroom’ is based on some chunky pre-election tax rises
 - Identified lots of problems but stopped short of trying to solve them
 - More of the same on economic growth strategy – will it be enough?
 - Talked a lot about ‘backing working people’ ... but pensioners were some of the biggest beneficiaries
- And the way the whole Budget process was conducted was bonkers

The Institute for Fiscal Studies
2 Marylebone Road
London
NW1 4DF

www.ifs.org.uk

