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BRIEFING

Help today, squeeze tomorrow

Putting the 2022 Autumn Statement in context

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Summary

Yesterday, Jeremy Hunt delivered an Autumn Statement that combined the 'tough choices' rhetoric of George Osborne and the policies of Gordon Brown. In the face of grim economic – and grimmer fiscal – forecasts, he announced energy support today but tough times tomorrow, with huge stealth tax rises for the middle and top of the income distribution followed by far less concrete spending cuts pencilled in for after the next election.

The new Office for Budget Responsibility (OBR) forecasts for an energy shock-driven recession are much more optimistic than those of the Bank of England, but still point to unemployment rising by 500,000 in the short term and the economy being no bigger at the end of this parliament than its start – the first time that has happened in 40 years. But the fast-rising debt interest bill doing more fiscal damage than the weaker economic outlook. Overall, these changes leave borrowing £270 billion higher cumulatively over the coming five years than was expected in March this year.

The Chancellor's short-term response was to give details of the support for household energy bills next year, combining a slightly more generous repeat of Sunak's lump-sum Cost of Living Payments for vulnerable groups with a less generous form of Truss' Energy Price Guarantee (EPG - which will see a typical bill rise to £3,000 next April). The latter may make a limited difference to energy bills in 2023-24 overall because they are currently set to average £3,300.

Together, this energy support will be less generous than the current year but more progressive, as the EPG rises and other fully or nearly universal support (i.e. bill discounts and council tax rebates) falls away. The average energy-specific support falls from £1,800 in 2022-23 to £700 next year, a 61 per cent reduction. Those with harder-to-heat homes or larger families will be particularly hard hit by rising energy bills, with almost one-quarter (23 per cent) of households facing bills of over £4,000 next year.

That said, two-thirds of next year's support will go to the poorest half of households, compared to half of the support this year. However, the reliance on the benefits system to passport support creates a major cliff edge and plenty of rough justice – particularly for the 2.3 million households who are in the poorest fifth of the population but do not receive means-tested benefits and so will not qualify for lump-sum payments. Someone earning £1 too much to qualify for Universal Credit could potentially miss out on £900 of support – a powerful disincentive for some to increase their earnings next year.

Looking further ahead, the Chancellor announced a £55 billion a year fiscal tightening in order to meet his (considerably loosened) fiscal target of getting debt falling as a share of GDP by 2027-28. A change of Chancellor has seen the Government swing from

announcing the biggest tax cuts in 50 years, to implementing biggest fiscal tightening since 2010 in just a few weeks.

Looking through those recent seesaws in economic policy, three-quarters of the fiscal tightening announced since the Spring is focused on spending cuts. This reflects that the £25 billion of new tax increases announced yesterday – including top-heavy tax rises to reduce the amounts people can make before paying capital gains tax, dividend tax, and the 45p rate of tax – largely fill the revenue hole caused by the remaining tax cuts from Liz Truss' tenure.

However, the overall fiscal consolidation announced since the pandemic began is much more tax-rise heavy. The spending cuts announced yesterday largely reverse spending increases previously announced, but overall Chancellors since the pandemic have raised taxes by 2.3 per cent of GDP (£68 billion or £2,300 per household in 2027-28), including freezing all major tax thresholds during the current period of high inflation and sharply increasing corporation tax. On this basis, the consolidation is entirely driven by tax rises, in sharp contrast to the post-financial crisis fiscal tightening, when almost 80 per cent came from spending cuts.

These tax rises will amount to a significant hit to household incomes that is broadly progressive across the income distribution, with higher-income households generally facing higher tax hikes as a proportion of their income. 70 per cent of the new taxes for individuals announced yesterday will be paid by the richest fifth of households.

However, the specific policy choices – especially relying to such an extent on stealthy threshold freezes rather than more visible rate rises – does raise some fairness questions. While the top 20 per cent and middle face tax rises of around 3.7 per cent of income (£3,600 and £1,400 respectively) from all measures announced in this Parliament, compared to 1.8 per cent or £350 for the poorest fifth, the very top 5 per cent pay less proportionally with tax rises only worth 3 per cent of income. This reflects the largely flat cash tax rise for anyone affected by each frozen tax threshold. For example, someone on £62,000 loses as much from threshold freezes as someone on £124,000 in cash terms (£1,600) but twice as much as a share of income (2.6 versus 1.3 per cent). The decision to raise almost £5 billion through higher Council Tax is also very poorly targeted at those with higher incomes.

The sheer scale of tax rises and focus on threshold freezes also reinforces the extent to which these tax rises are a departure from the post-financial crisis fiscal tightening. Tax as a share of GDP is rising steeply, reaching its highest level since the Second World War (37.5 per cent by 2024-25), while the six-year personal allowance freeze is set to undo around half of George Osborne's flagship increases to it over the 2010s, and will take it back to around its 2013-14 real-terms level.

While some tax rises have already been introduced, spending reductions announced yesterday are much more backloaded than those announced in 2010, and none are due to be implemented during the current spending review period that extends to 2024-25. Indeed, the Chancellor announced modest top-ups to departmental spending over the next two years, notably for the health service and schools. Beyond 2024-25, although public spending as a share of GDP is set to rise to 43.4 per cent in 2027-28, that reflects fast-rising debt interest costs that are masking significant cuts to investment and public service spending pencilled in from 2025-26; notably, after the next general election.

Public investment cuts have played a major role in every recent fiscal consolidation. Despite the current Prime Minister having announced significant investment increases recently, this time is no exception, with Public Sector Net Investment (PSNI) being frozen in cash terms from 2025-26. This £15 billion cut will see it fall from 2.5 per cent of GDP this year to 2.2 per cent in 2027-28, undoing over 80 per cent of the increase in PSNI originally planned by Rishi Sunak, but leaving it around 0.2 percentage points of GDP above the average for this century.

A £22 billion reduction in day-to-day public services, combined with existing protections for health, defence and education, implies cuts to unprotected departments like transport, policing and local government of around 0.8 per cent per year between 2024-25 and 2027-28. This will take real per capita spending for these departments back to the level they were at in 2014-15, or below it if inflation in the middle of this decade comes in higher than the OBR's very low forecast. Such cuts are likely to be undeliverable, requiring years of holding down public sector wages relative to the private sector.

Whether spending cuts on this scale come to be implemented will depend on whether the economy performs as badly, and – crucially – on whether debt interest costs rise as fast, as forecast. But while the UK's economic outlook is highly uncertain, the outlook for living standards is certainly bleak.

Average real household disposable incomes are forecast to fall by 7.1 per cent over this year and next – equivalent to £1,700 per household – by which time average incomes will have fallen back to 2014 levels. That is despite government policy offering significant support, with measures announced since the spring providing an average £1,300 boost to the lowest income households (mainly via targeted Cost of Living Payments) and highest income households (driven by the scrapping of the Health and Social Care Levy, partially offset by the lowering of threshold for the 45p rate of income tax to £125,000). The squeezed middle will receive less support, at an average £950 per household.

The government confirmed it will proceed with the uprating of all benefits in line with inflation (10.1 per cent) next year reflecting pre-existing policy, and making a huge difference to those on low-to-middle incomes - the biggest rise since 1991. Compared to the widespread suggestion of an earnings-related uprating (5.5 per cent), this will see households on Universal Credit receive £244 extra on average from April next year. The welcome 9.7 per cent rise in the National Living Wage from April 2023 will also see the earnings of the lowest earners rise significantly above average next year.

Looking to the longer term, and accounting for all announcements this Parliament, policy decisions – and the freeze to personal tax thresholds in particular – are deepening the squeeze for all but the poorest quarter of the population (who gain more from increases to Universal Credit generosity than they lose from tax rises). While the poorest fifth will be £350 better off on average, typical households see their incomes reduced by £1,100 in 2027-28, rising to a £4,200 loss for the top decile.

This leaves the outlook for living standards during the 2020s in a truly dreadful place. Real household disposable incomes are forecast to remain lower at the start of 2028 than they were before the pandemic hit in 2019. The outlook for real wages is even worse, with the value of workers' pay packets not expected to return to their 2008 level until 2027. This unprecedented 19-year pay downturn has cost workers £15,000 a year compared to a world where their wages had instead continued to grow at their pre-financial crisis rate.

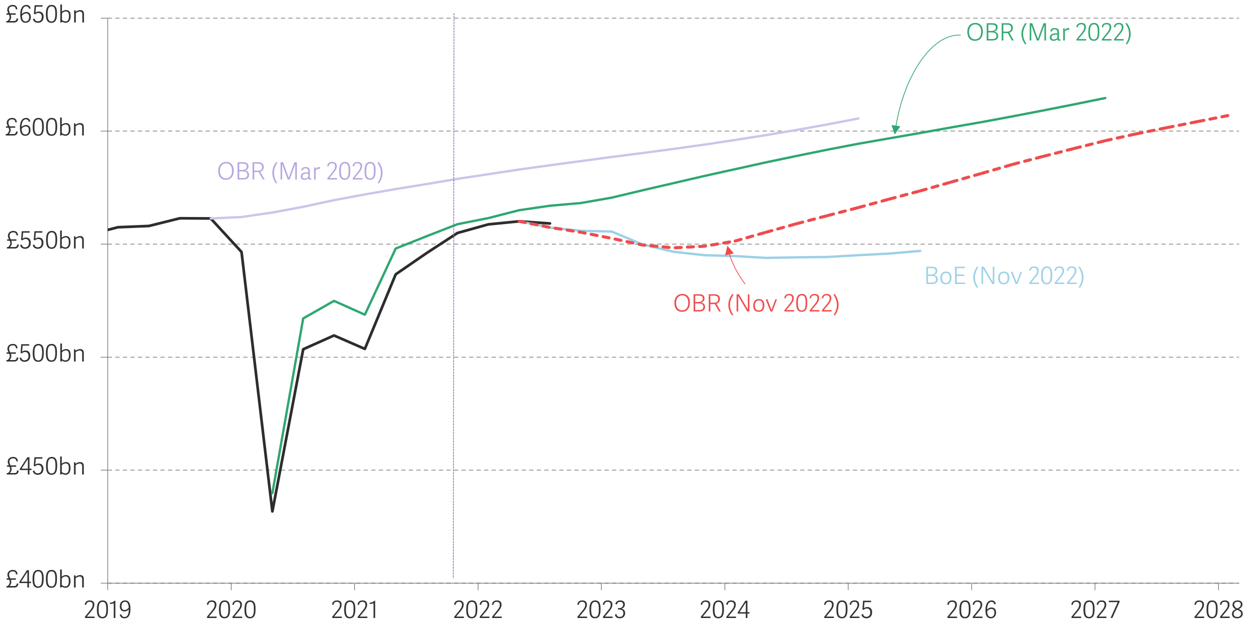
As an energy importer during an energy price shock, Britain is getting poorer. Deciding how we do so was, to a significant extent, the choice facing the Chancellor. He has decided that households will do so with higher energy bills, higher taxes, and worse public services than previously expected. Making the choices may have been tough, but the reality of living through the next few years will be tougher.

The economic outlook is grim, despite the OBR being much more optimistic than the Bank of England

The Office for Budget Responsibility (OBR) has slashed its forecasts for economic growth over the near term. The economy has already started to shrink, and the OBR forecasts a contraction of a cumulative 2.1 per cent in GDP over the five quarters between Q2 2022 and Q3 2023 (Figure 1). The economy will not regain its pre-pandemic size until Q4 2024. This is five years with no GDP growth: the economy is set to end this Parliament no bigger than it started, something not seen since the early 1980s.

FIGURE 1: **The OBR now forecasts a recession for the UK**

Real GDP outturns and forecasts: UK



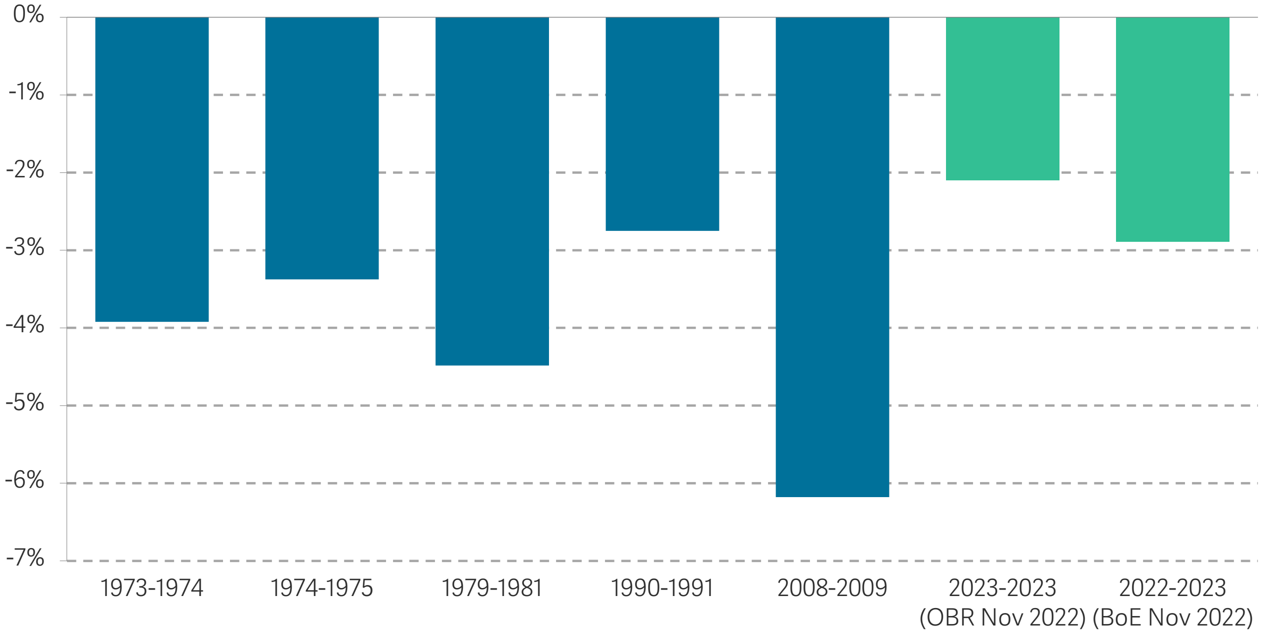
SOURCE: OBR, Economic and Fiscal Outlook, various; Bank of England, Monetary Policy Report, November 2022.

This is weaker than the 2.1 per cent growth the OBR expected over the same period back in March, but, as Figure 1 shows, more optimistic than the Bank of England's latest forecast. It would also be a notably smaller contraction than in the any of the technical recessions of the past 50 years (Figure 2).

Both private investment and private consumption are expected to contract even more sharply than GDP over the next five quarters: private domestic demand is accordingly expected to shrink by 3.4 per cent. Government spending and trade are expected to cushion the blow: public sector demand is expected to grow by nearly 10 per cent in real terms, and net trade is expected to contribute 1.4 percentage points to cumulative growth. This is a picture of a weak private sector over the near term being supported by demand from the government and overseas.

FIGURE 2: **The OBR forecasts a relatively shallow recession compared to past recessions**

Falls in real GDP from peak to trough in previous recessions and the November 2022 OBR and Bank of England forecasts: UK



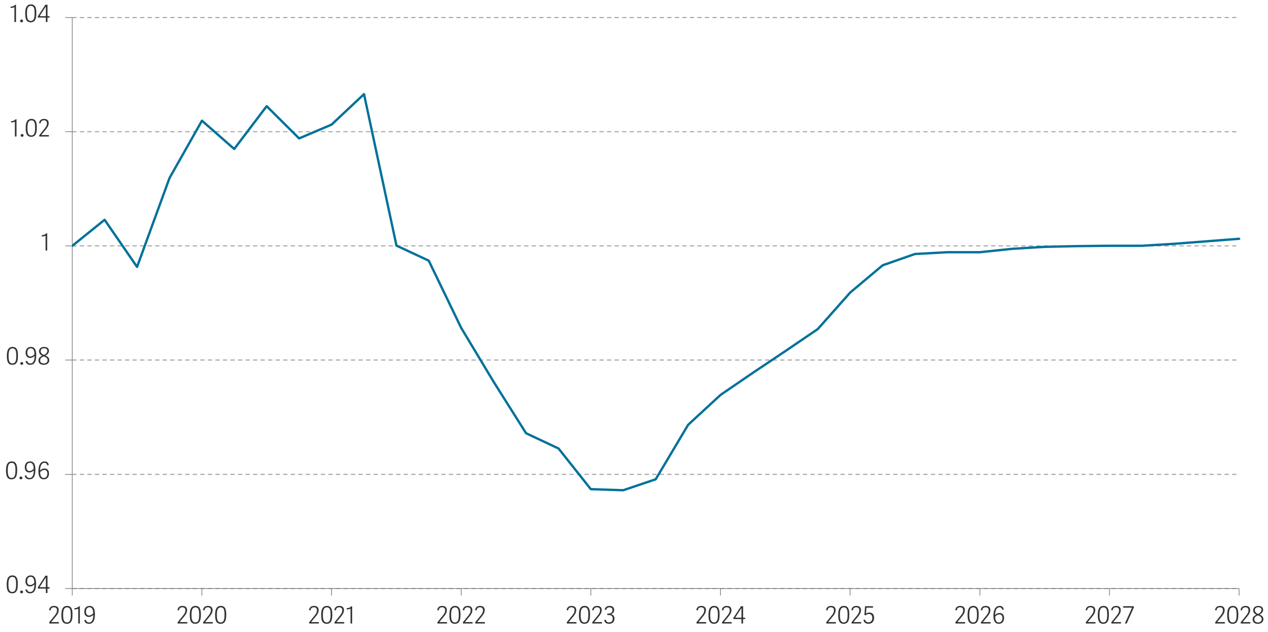
SOURCE: OBR, Economic and Fiscal Outlook, various; Bank of England, Monetary Policy Report, November 2022.

The main underlying cause of this weak economic performance over the near term is the sharp rise in the prices of energy and other goods that the UK imports, relative to the price of what we sell on world markets – the 'terms of trade'. The OBR is expecting the terms of trade to bottom out in the middle of next year at around 5 per cent below its pre-pandemic level. The OBR then forecasts a strong terms of trade recovery, as energy and food prices fall back again (Figure 3).

The key difference between the OBR and the Bank of England is that the OBR is notably more optimistic about the economy's ability to grow without generating inflation, forecasting that the price level will rise by only 2.3 per cent in total in the three years to end-2025, compared to the Bank's forecast of 6.7 per cent (Figure 4). Over the same period, GDP grows by 4 per cent in the OBR forecast, whereas in the Bank of England's it grows by only 1.4 per cent. This reflects a much more optimistic assumption within the OBR about the growth in the productive potential of the economy (see Box 1), as well as how disinflation is generated by the recession. As discussed below, these assumptions are material for the fiscal outlook, as they mean tax revenues hold up in the medium term despite the recession, and departmental spending limits set in cash terms go further given very weak inflation.

FIGURE 3: **The economic headwinds from high world prices are expected to abate**

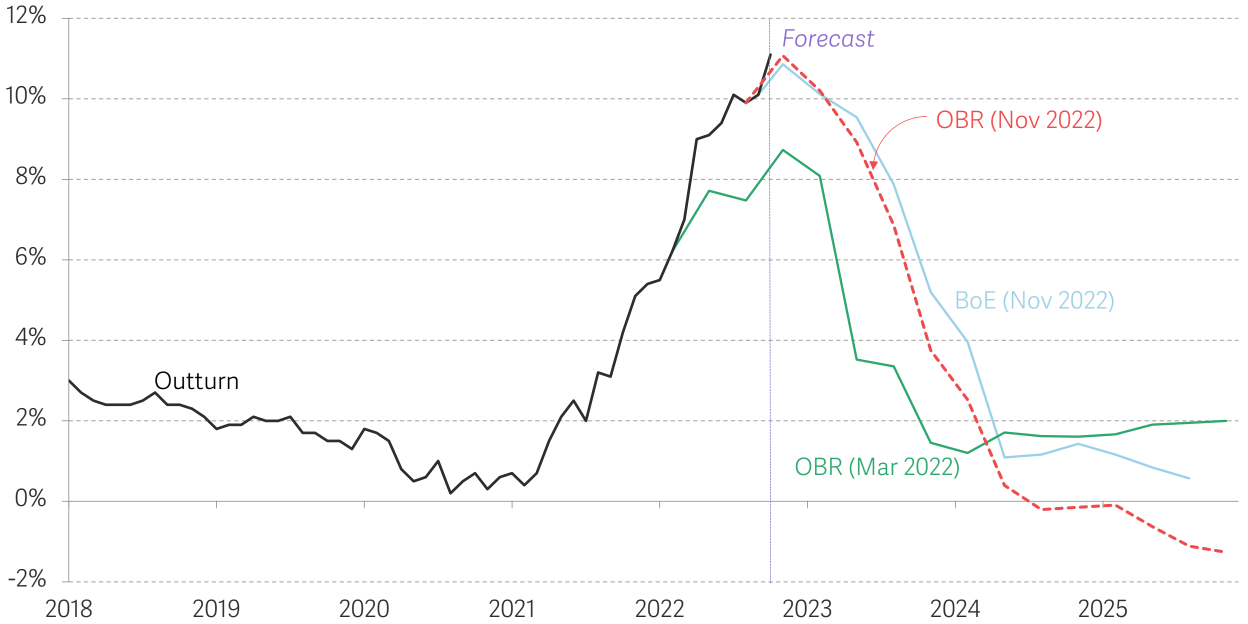
Price of UK exports relative to price of UK imports (Q1 2019 = 1), outturn and OBR forecast



SOURCE: OBR, Economic and Fiscal Outlook, November 2022.

FIGURE 4: **The OBR forecasts that inflation will turn negative for nearly two years**

CPI inflation, outturn and forecasts from the OBR and Bank of England: UK



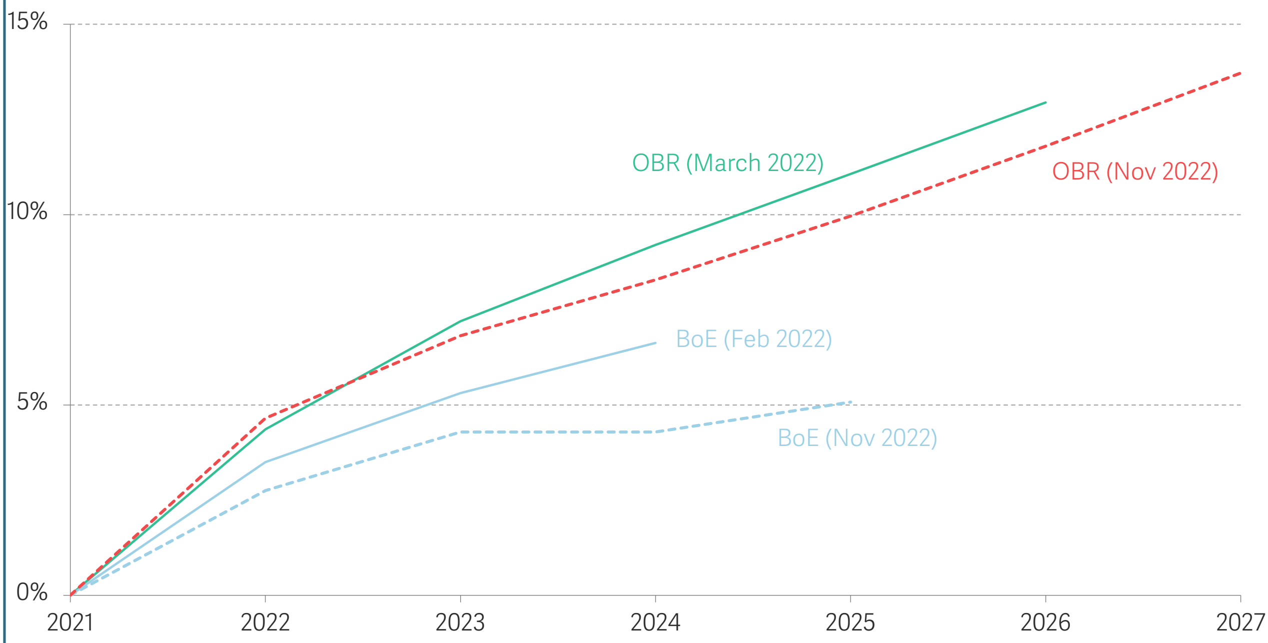
SOURCE: OBR, Economic and Fiscal Outlook, November 2022; Bank of England, Monetary Policy Report, November 2022.

BOX 1: The OBR has become more pessimistic about longer-term growth, but remains much more optimistic than the Bank of England

A key determinant of tax revenues over the medium term is the rate at which the economy can grow without generating inflation. The OBR has downgraded its estimate of growth in potential supply between 2021 and 2026 by 1.4 percentage points to 11.8 per cent. But they remain notably more optimistic than the Bank of England (see Figure 5).

FIGURE 5: **The OBR has downgraded growth in potential supply but remains much more optimistic than the Bank of England**

Cumulative growth in potential GDP from 2021, OBR and Bank of England: UK



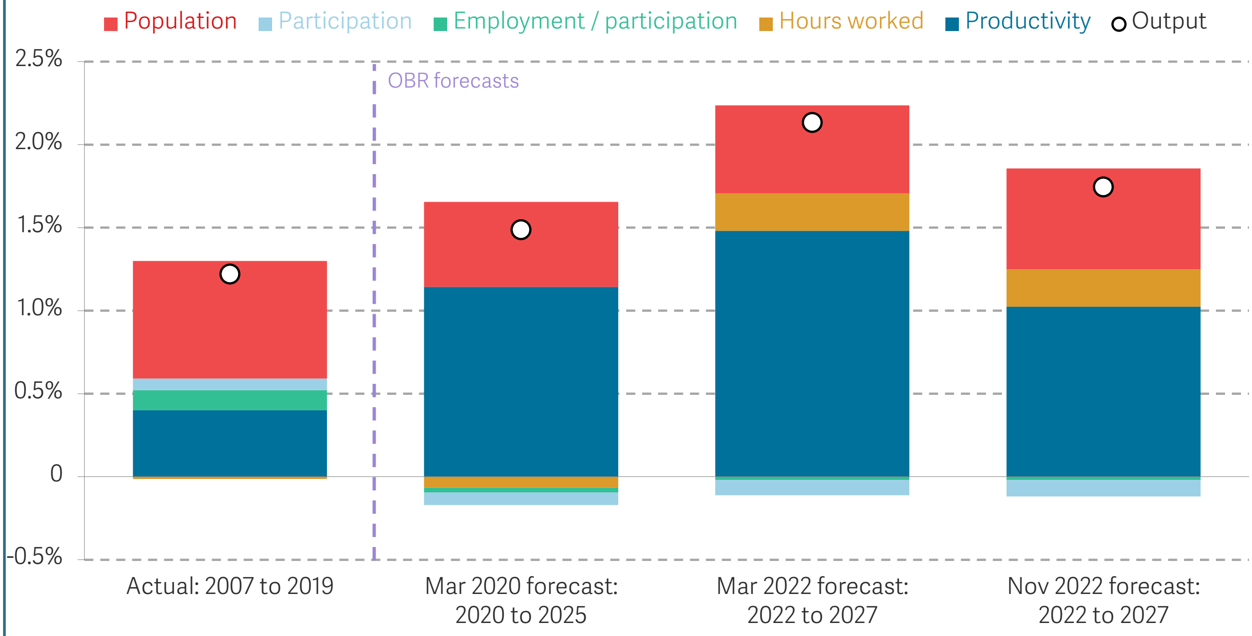
NOTES: OBR potential supply refers to non-oil GVA and Bank of England projections for potential supply are for whole-economy GDP. Bank of England potential supply is backed out by comparing the projection for GDP with (quarter-point-rounded) output gap.
SOURCE: OBR, Economic and Fiscal Outlook, November 2022; Bank of England, Monetary Policy Report, November 2022

The OBR's optimism is also clear in comparison to the UK's recent past. They are expecting potential GDP to grow faster over the next 5 years (1.7 per cent at an annualised rate) than the average growth rate of actual GDP over the 12 years leading up to the pandemic (1.2 per cent) (see Figure 6). Growth in population and productivity are the main drivers of potential supply in the long term. The OBR is expecting population growth to decelerate to 0.6 per cent per year, albeit somewhat faster than their expectation in March

2022, while it is expecting annualised productivity growth to accelerate markedly from 0.4 (2007 to 2019) to 1.0 per cent (in 2027).

FIGURE 6: **The OBR expect relatively fast growth in labour productivity over the medium term**

Annualised growth in output and components, outturn growth and OBR forecasts of potential supply growth: UK



NOTES: Historical data are outturns. Population is 16+ population. Forecasts relate to potential rather than actual supply, and are for non-oil GVA.
SOURCE: ONS; OBR, Economic and Fiscal Outlook, various

One of the most persistent economic impacts of Covid-19 has been the hit to labour supply, with participation still down by 396,000 as of September 2022 compared to February 2020. This has largely come from lower participation among older workers, with signs of earlier retirements and a rise in ill-health among this group. The OBR have now factored persistently lower labour supply into their forecasts: it thinks that the 16+ participation rate will remain at 63 per cent (roughly a percentage point lower than the 2019 level), slightly lower than expected in March.

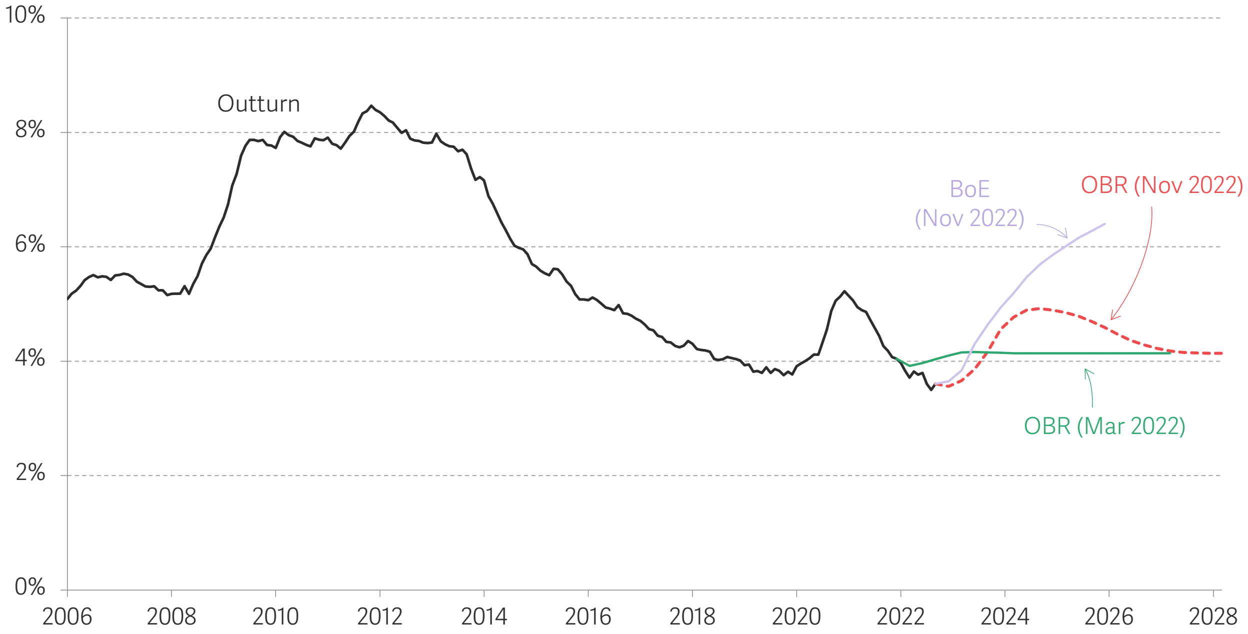
A looming recession means unemployment is set to rise sharply

The weaker near-term economic outlook is reflected in the OBR's expectations for the labour market. As a result, unemployment is set to rise throughout 2022 to 2024, peaking at 4.9 per cent in 2024 (Figure 7), an increase of 500,000 people. Here, again, while this is a grim forecast in absolute terms, the OBR remains significantly more optimistic than the Bank of England's projection of a rise to 6.4 per cent in 2025. The flip-side is that this shows up as weaker wage growth: the OBR's forecast is for the current wage squeeze to be longer and deeper than in March – continuing the disastrous period for real pay growth since the financial crisis. Indeed, inflation-adjusted pay won't return to 2008 levels until 2027. This would amount to 19 years of zero cumulative growth.

In a counterfactual world where real wages had continued growing at their 2000-08 pace (of 2.2 per cent per year) they would instead have risen 35 per cent by 2027, equal to £292 per week in 2022 prices, or around £15,000 a year. As discussed below, this is a key driver of the broader weak outlook for household incomes. More positively on wages, the Chancellor announced the National Living Wage is set to rise from £9.50 to £10.42 next April – a 9.7 per cent increase. This will mean that unlike average earners, the two million workers who earn the minimum wage will see their wages keeping pace with inflation (the OBR expect CPI inflation to be 8.9 per cent in Q2 2023).

FIGURE 7: **Unemployment is set to rise over the next two years – but the two official forecasters disagree about the extent and length of the increase**

16+ unemployment rate, outturn and forecasts from the OBR and the Bank of England: UK



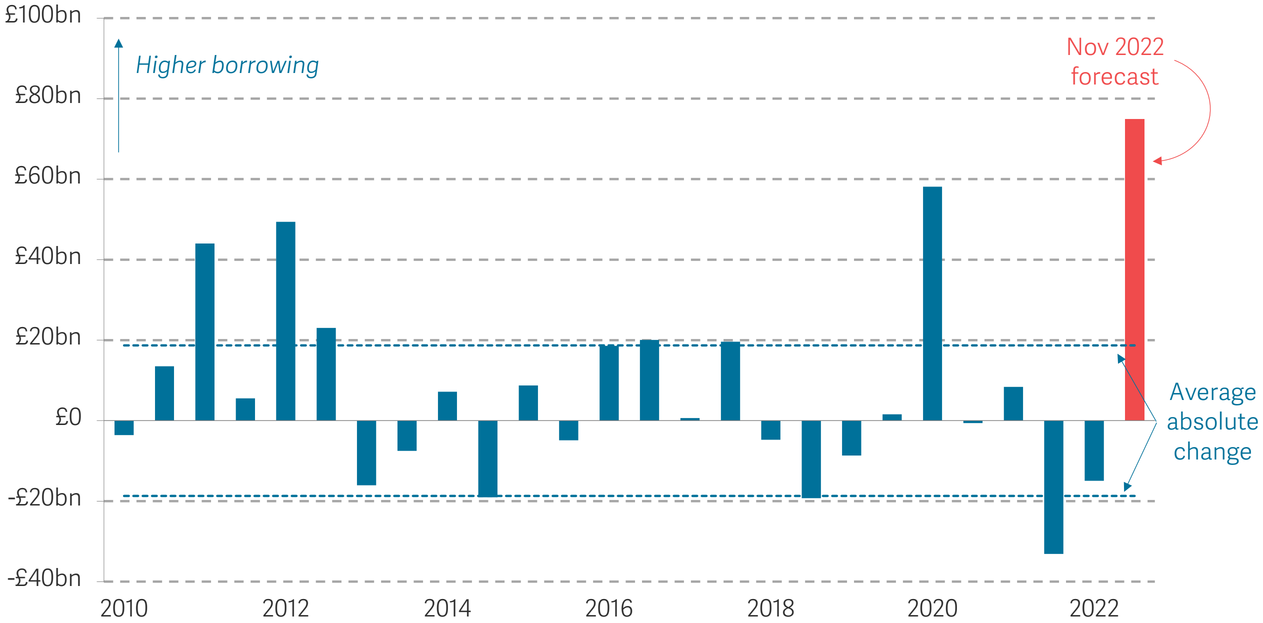
SOURCE: OBR, Economic and Fiscal Outlook, various; Bank of England, Monetary Policy Report, November 2022.

If the economic forecasts are grim, the fiscal forecasts are grimmer

The public finances have not just been hit by a weaker economy, but higher interest rates too. The OBR estimates that combination has added £75 billion to the deficit in 2026-27 (Figure 8) and £270 billion cumulatively over the five-year forecast period (with higher debt interest costs doing the majority of the damage). This is the biggest upward revision to borrowing due to economic changes since at least 2010, larger than that during the pandemic, and is over four times the average change between OBR forecasts.

FIGURE 8: **The economic deterioration has caused the largest rise in borrowing since at least 2010**

Economy-driven changes to the fifth year of the OBR borrowing forecasts (reflecting the economy and related changes to the performance of the public finances), 2022-23 prices: UK

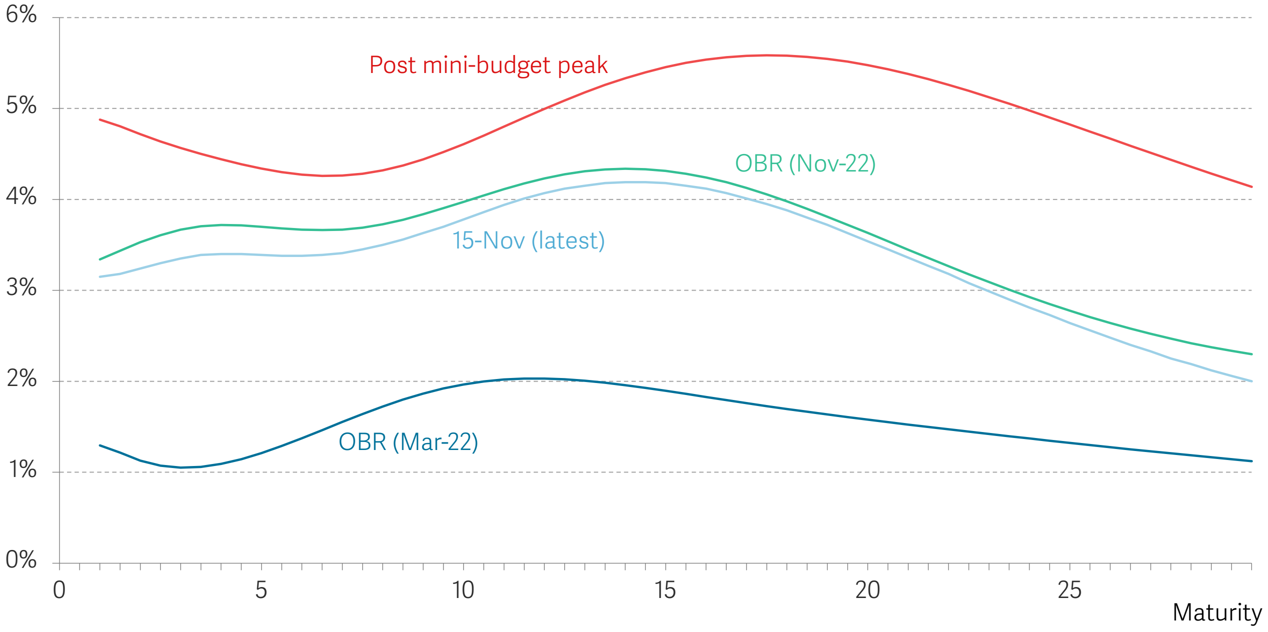


NOTES: Totals are adjusted for GDP deflator inflation. Underlying forecast changes include the impact of changes in outturn data, revisions to the economic forecast and judgements about the performance of the public finances.
SOURCE: RF analysis of OBR, Forecast revisions database; OBR, Economic and Fiscal Outlook - November 2022.

The key factor in this deterioration is the huge rise in interest rates – both in the UK and globally – over recent months (Figure 9). Although there have been sizeable falls since the peak of the market dysfunction following September's mini-budget, borrowing rates are expected to be up to 2 percentage points higher in the coming years than was expected back in March. This represents an ongoing fiscal cost as the Government must spend more to service its debt every year.

FIGURE 9: **Although interest rate expectations have fallen over recent weeks, they are up by around 2 percentage points since March 2022**

Nominal sterling gilt forward rates: UK



SOURCE: RF analysis of Bank of England, Yield curves.

Higher interest rates are the biggest driver of the grim fiscal outlook, but it has been amplified by the permanent tax cuts announced in the mini-budget. Despite significant U-turns before the Autumn Statement, the OBR estimates that there was a remaining net increase in borrowing from mini-budget policies of £18 billion by 2027-28.

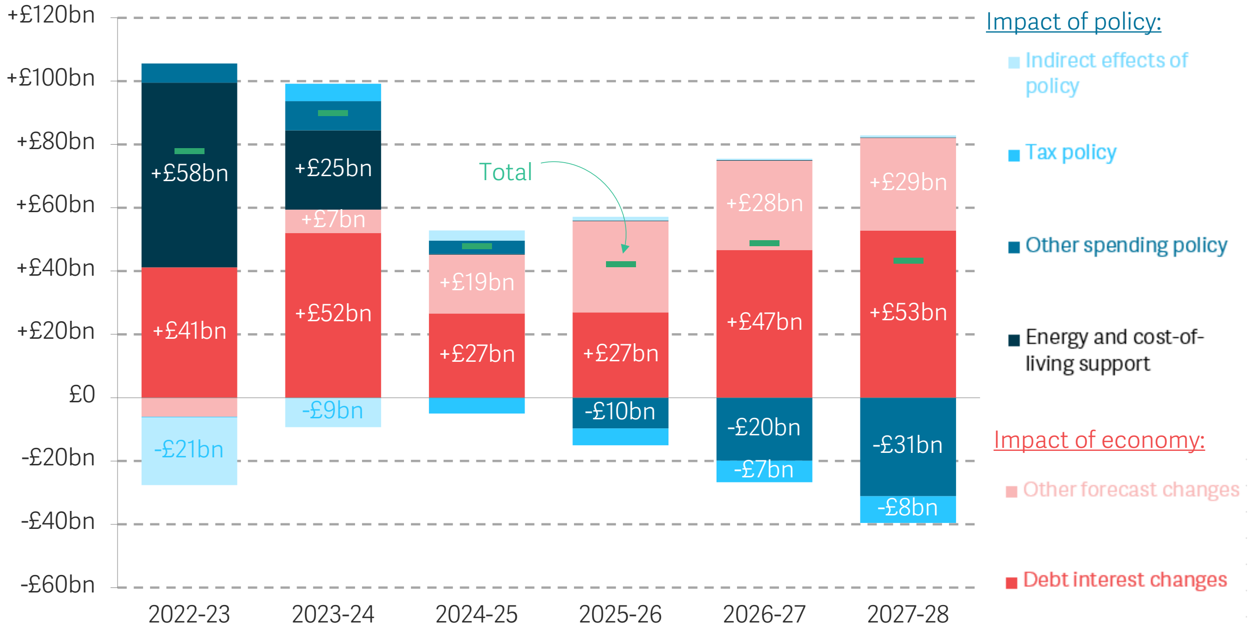
The Chancellor announced more energy support for the short term, and £55 billion of tightening in the medium term

In the face of these grim forecasts, the Chancellor has used the Autumn Statement to ease the adjustment to higher energy prices in the near term before turning to putting the public finances on a sustainable footing beyond the middle of this decade. As Figure 10 shows, both of these have a major impact on the public finances. Since March, around £80 billion of measures to deal with the cost-of-living crisis have been announced.[1] And in the longer-term, the Autumn Statement announced plans to cut spending and raise taxes to reduce borrowing by around £55 billion a year by 2027-28 – which amounts to a net £40 billion change since the March 2022 Spring Statement given the remaining taxes cuts inherited from Liz Truss. Below, we take each of these two big policy decisions in turn.

1 These costings depend heavily on the wholesale price of energy, which we discuss in more detail below.

FIGURE 10: **Although the economic deterioration is the most significant factor pushing up borrowing, energy cost measures and mini-Budget decisions are also important**

Change in public sector net borrowing forecast, by driver: UK



SOURCE: OBR, Economic and Fiscal Outlook – November 2022.

The short-term fiscal outlook is dominated by spending on energy support, which is being reduced next year. The Chancellor has followed his swift curtailment of Liz Truss's Energy Price Guarantee (EPG) with his own support package, which shares the same name and consists of a £3,000 ceiling on the energy bill for a typical household for the 2023-24 financial year. This is a rise of £500 a year on the current regime, or £900 when accounting for the expiry of £400 Energy Bill Support Scheme rebate. As a result, as Figure 11 shows, energy bills in 2023-24 will be at least 40 per cent higher than in 2022-23, with monthly bills peaking at £400 in January 2024 for a typical household on a pre-payment meter.[2]

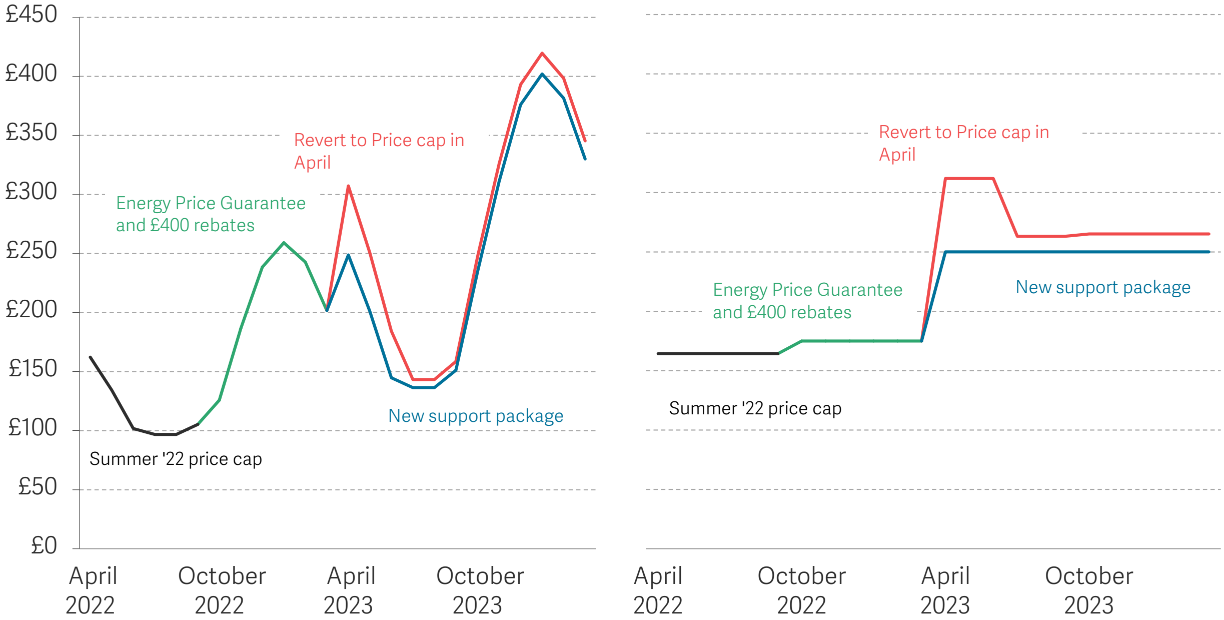
The amount of protection this offers to households compared with the default of reverting to Ofgem's formula driven price cap depends entirely on energy prices next year. The Government has suggested that the new EPG would save the typical household £500 a year, but the most recent estimates from Cornwall Insight imply a series of quarterly

2 The Government also announced that they will double support to those using alternative fuels such as heating oil, increasing the one-off payment to £200. This will benefit approximately 1.9m households across the UK, especially those in Northern Ireland where all households will receive the payment to account for the high prevalence of non-gas-heated properties.

price caps that put the typical (no-EPG-applied) energy bill at £3,300 across 2023-24, which would mean the second coming of the EPG saves the typical household only £300.[3]

FIGURE 11: **The less generous Energy Price Guarantee means energy bills in 2023-24 will be around 40 per cent higher than in 2022-23**

Historical and forecast monthly energy bills for a typical household paying via a pre-payment meter (left hand panel) and direct debit (right hand panel): April 2022-March 2024



NOTES: Figures net of £400 Energy Bills Support Scheme rebates but no other cost of living payments such as those delivered through the benefits or council tax system. Costs based on forecasts for Cornwall Insight resulting in a typical energy bill of £3,300 in 2023-24.
SOURCE: RF analysis of Ofgem price cap methodology, Government Energy Price Guarantee, Cornwall Insight, UCL SERL data.

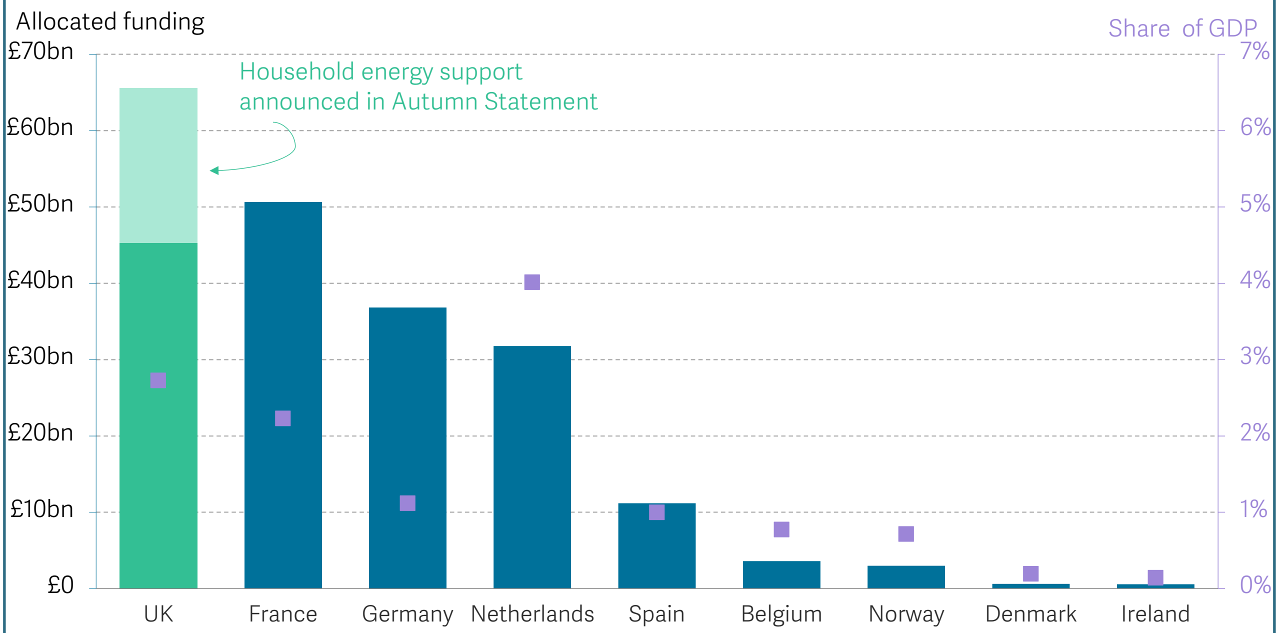
Using the Government's assumptions, the EPG extension is estimated to cost £12.8 billion; this would push the UK into top spot among peer nations in costs devoted to supporting households with energy bills (see Box 1). But supporting all 28 million UK households with a £300 bill discount (in line with the most recent Cornwall Insights estimates) would cost £8 billion, around £5 billion less than the Government is budgeting for, and around one third of the cost of the EPG during the winter of 2022-23. These costings are of course highly uncertain, being based on future commodity market prices, which the previous year has shown are far from easy to anticipate.

3 The latest Cornwall Insight price cap for Q2 2023 is £3,739 per year, and those for Q3 and Q4 2023 are £3,157 and £3,182, respectively. Weighted by monthly household gas and electricity consumption, and rolling the Q4 2023 price over to Q1 2024 (for which no forecasts are available) yields a typical household bill of £3,300. For more, see: November 17 Tweet by Cornwall Insight and Predicted fall in the April 2023 Price Cap but prices remain significantly above the EPG, Cornwall Insight, November 2022.

The invasion of Ukraine means that the UK is not the only European nation acutely exposed to high gas prices. Many European countries have announced support for households to weather this energy crisis, but the new support for households announced in the Autumn Statement takes the total commitment by the UK government to £66 billion (at least, using the estimates published in the Autumn Statement), the highest in cash terms among European comparators including France and Germany (Figure 12), and the second highest as a percentage of GDP (the UK's support amounts to 2.7 per cent of GDP, below only the Netherlands whose support is 4 per cent of GDP).

FIGURE 12: **The UK now leads peer nations in terms of household support announced during the energy crisis**

Allocated funding to shield households from rising energy costs announced since September 2021, and as share of national GDP: selected European countries

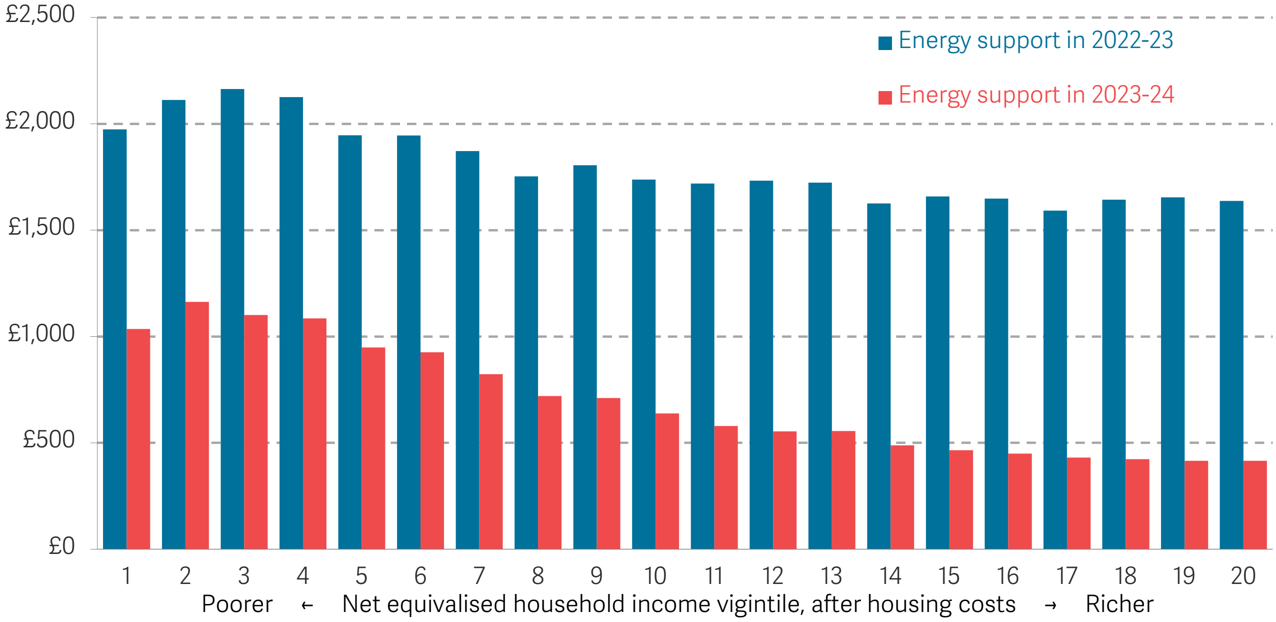


NOTES: Data includes energy specific grant support for households weathering the cost-of-living crisis in Europe. Spending calculated as a proportion of GDP for the year between Q3 2021 and Q2 2022. Some costs include support for small businesses where this could not be disaggregated from households. Where packages had multiple purposes, these were divided into business, household and general cost of living support based on the best available evidence. Support for petrol and diesel costs not included. UK support includes cost of living payments in 2022-23 and 2023-24, Energy Price Guarantee in 2022-23 and 2023-24, and universal £400 payment in 2022-23. Figures do not yet account for Germany's €200-billion energy relief plan which was backed by Germany's parliament on October 21 2022, will be financed through new borrowing under an Economic Stabilisation Fund. The package will be reviewed by the European Commission and the breakdown of support for households versus for business or general cost of living at the time of writing is uncertain.
SOURCE: RF analysis of Bruegel, Eurostat, ONS, Bank of England.

Reflecting the fact that poorer households are far more exposed to the impacts of rising energy bills, accompanying the continuation of the universal price cap is a repeat of the targeted Cost of Living payments introduced when Rishi Sunak was Chancellor. In 2023-24, households on Universal Credit and other means-tested benefits will receive £900 (up from £650 this year), pensioners will again receive £300, and those in receipt of various disability benefits will receive a repeat of the £150 they received this year.[4]

FIGURE 13: **The poorest households will get twice as much energy support in 2023-24 as the richest**

Total value of energy support in 2022-23 and 2023-24 by income vigintile, in nominal prices: UK



NOTES: Energy support in 2022-23 includes the £2,500 Energy Price Guarantee, £400 energy bills payment, £150 Council Tax payment, £650 means-tested benefit payment, £300 pensioner payment, and £150 disability payment. Energy support in 2023-24 includes the £3,000 Energy Price Guarantee, £900 means-tested benefit payment, £300 pensioner payment, and £150 disability payment. Chart assumes Cornwall Insight energy bill forecasts as of 17/11/2022.
SOURCE: RF analysis of DWP, Family Resources Survey using the IPPR tax-benefit model; DWP, Households Below Average Income; ONS, Living Costs and Food Survey.

The new package of support for 2023-24 – i.e. the combination of the savings from the EPG and the Cost of Living Payments – amounts to £700 on average across all households, but its more targeted nature means that it is worth £1,100 for the poorest fifth of households, and just £420 for the richest fifth– see Figure 13. Indeed, 60 per cent of household support in 2023-24 will be targeted, a notable increase on the 20 per cent in the current year. As a result, two-thirds (66 per cent) of support goes to those in the bottom half of the income distribution in 2023-24, compared to just over half (54 per cent)

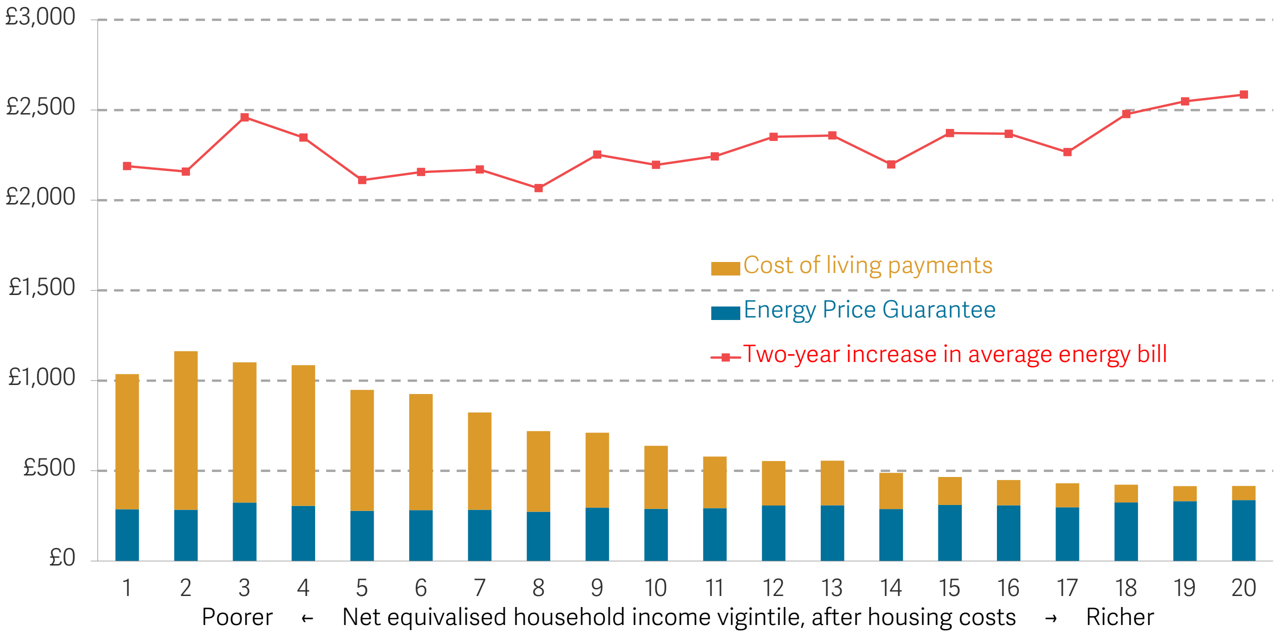
4 The Government has not yet said how many payments there will be or when in 2023-24 payments will be made. For more on the 2022-23 payments, see: T Bell et al, Back on Target, Resolution Foundation, May 2022.

in 2022-23. On the other hand, the amount of support was far more generous in 2022-23: on average, households are being supported by £1,800 of support in 2022-23, compared to £700 next year, a 61 per cent reduction.[5]

As Figure 14 shows, the level of support in 2023-24 is set to be significantly less than the rise in energy bills that households will have experienced since 2021-22 (bills are forecast to be more than three-times their 2021-22 levels in 2023-24, an increase of £2,300). The new package offsets just 30 per cent of this increase to energy bills on average, and just under half (48 per cent) for an average household in the lowest-income quintile.

FIGURE 14: **Next year's new energy support package offsets a third of the rise in energy bills since 2021-22**

Distribution of average support from new energy support package in 2023-24, and increase in average energy bill since 2021-22: UK



NOTES: Cash values in 2023-24 prices. Two-year increase in average energy bill refers to change in energy bills between 2021-22 and 2023-24, and excludes the effect of the Energy Price Guarantee. Cost of living payments refers to the £900 means-tested benefit payment, £300 pensioner payment, and £150 disability payment. Average energy bill assumes Cornwall Insight energy bill forecasts as of 17/11/2022.
SOURCE: RF analysis of DWP, Family Resources Survey using the IPPR tax-benefit model; DWP, Households Below Average Income; ONS, Living Costs and Food Survey.

These averages hide huge variations in how households are experiencing the energy crisis, which boils down to three targeting problems. First, targeting payments at those receiving means-tested benefits is not a perfect way of targeting those in need, as four-in-ten (or 2.4 million) of the poorest fifth of households do not receive means-tested

5 Energy support in 2022-23 includes the £2,500 Energy Price Guarantee, £400 energy bills payment, £150 Council Tax payment, £650 means-tested benefit payment, £300 pensioner payment, and £150 disability payment. Energy support in 2023-24 includes the £3,000 Energy Price Guarantee, £900 means-tested benefit payment, £300 pensioner payment, and £150 disability payment.

benefits.[6] Second, conditioning the payment on receipt of means-tested benefits creates a cliff edge for support where earning £1 more can mean a family missing out on the payments (although this risk is reduced by spreading the £900 over several payments). Third, energy use varies considerably between households in the same part of the income distribution, driven by factors such as having a large family or living in a poorly insulated rental property. This variation is significant, with higher-energy-use households consuming over 50 per cent more than lower-energy-use households, even when controlling for household income.[7] Based on current forecasts, we expect almost one-quarter of households (23 per cent) to face energy bills of over £4,000 in 2023-24.

Figure 15 illustrates this variation by showing by how much households will be worse off (or better off) if we compare their net energy bills in 2023-24 under the EPG and after netting off the Cost of Living Payments with the energy bills the same households were facing in 2021-22.[8] Overall, fewer than one-in-ten (8 per cent) of households are set to be better off in 2023-24 (rising to 16 per cent for the poorest fifth of households) because the value of the Cost of Living Payments outweighs the rise in their energy costs (for example, someone receiving Pension Credit will get at least £1,200 in Cost of Living Payments in 2023-24, which could well exceed the rise in their energy bill).[9] However, around a quarter (26 per cent) of households are set to be worse off by up to £1,000, a third (34 per cent) worse off by between £1,000 to £2,000, and another third of households (8.9 million households) worse-off by more than £2,000 next year. To give an example of someone losing: a single person not in receipt of benefits will on average be paying £1,900 more for their energy in 2023-24 compared to two years previously (even accounting for the EPG). If they earned £20,000 per year, this effectively represents an 11 per cent cut in their disposable income.[10]

6 M Brewer et al., A chilling crisis: Policy options to deal with soaring energy prices, The Resolution Foundation, August 2022. In fact, new research has shown that some missed out on the £326 cost of living payments in July this year when they worked a couple of additional hours in June, enough to remove their entitlement to Universal Credit and miss out on the payment, leaving them worse off overall, for more see: R Griffiths, Universal Credit, Working Claimants and the Government's Cost of Living Support, IPR Policy Brief, November 2022.

7 M Brewer et al., A chilling crisis: Policy options to deal with soaring energy prices, The Resolution Foundation, August 2022. The Government also announced that it plans to consult on amending the EPG so that households who use very large amounts of energy will have their support capped, while ensuring that vulnerable high energy users, such as those with medical conditions, are not put at risk.

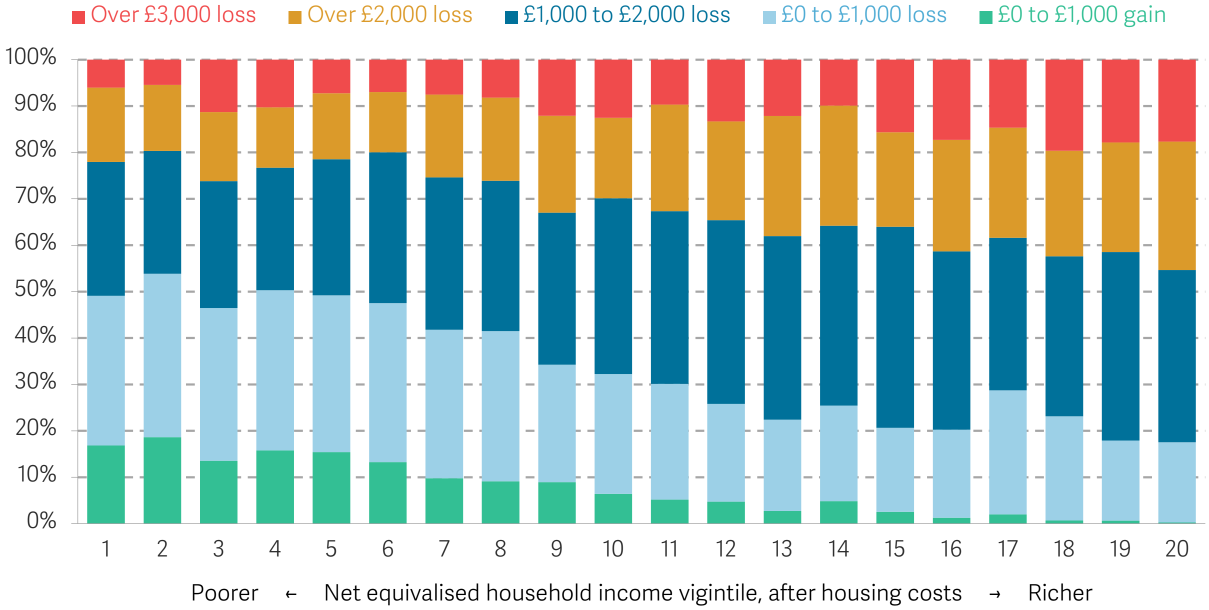
8 To do this, we matched each household in the HBAI dataset set with one in the LCFS data, allowing us to impute values of energy consumption into the HBAI dataset. We have assumed that higher energy prices do not reduce energy use.

9 The Government has not yet announced the timing of the 2023-24 cost of living payments, but it is important to note that the majority of energy consumption takes place during the winter months (78 per cent of gas consumption takes place during October to March). Lessons from the 2022-23 payments in July and November suggest that recipients were largely unable to save payments for future energy bills: instead, they said they would use the November payment for current energy bills, to pay off arrears, or to afford Christmas. Spreading the payments out has the advantage of reducing the cliff edge problems, and making the payments when most energy is consumed will be of greatest help to those who are unable to smooth bills through direct debits. For more, see: M Brewer et al., A chilling crisis: Policy options to deal with soaring energy prices, The Resolution Foundation, August 2022 and R Griffiths, Universal Credit, Working Claimants and the Government's Cost of Living Support, IPR Policy Brief, November 2022.

10 Calculated based on a post-tax income of £17,520, and assumes energy spending based on an average single person living alone.

FIGURE 15: **A third of households will worse off by more than £2,000 as a result of higher energy bills in 2023-24 despite Government support**

Combined annual impact of the increase in energy bills from 2021-22 to 2023-24, and the energy bills support in 2023-24: UK



NOTES: Chart assumes Cornwall Insight energy bill forecasts as of 17/11/2022. Energy support in 2023-24 includes the £3,000 Energy Price Guarantee, £900 means-tested benefit payment, £300 pensioner payment, and £150 disability payment.
SOURCE: RF analysis of DWP, Family Resources Survey using the IPPR tax-benefit model; DWP, Households Below Average Income; ONS, Living Costs and Food Survey.

While the Chancellor has confirmed the details of support for households' energy bills in 2023-24, he has merely committed to do so for the non-household sector by the end of the year: see Box 3.

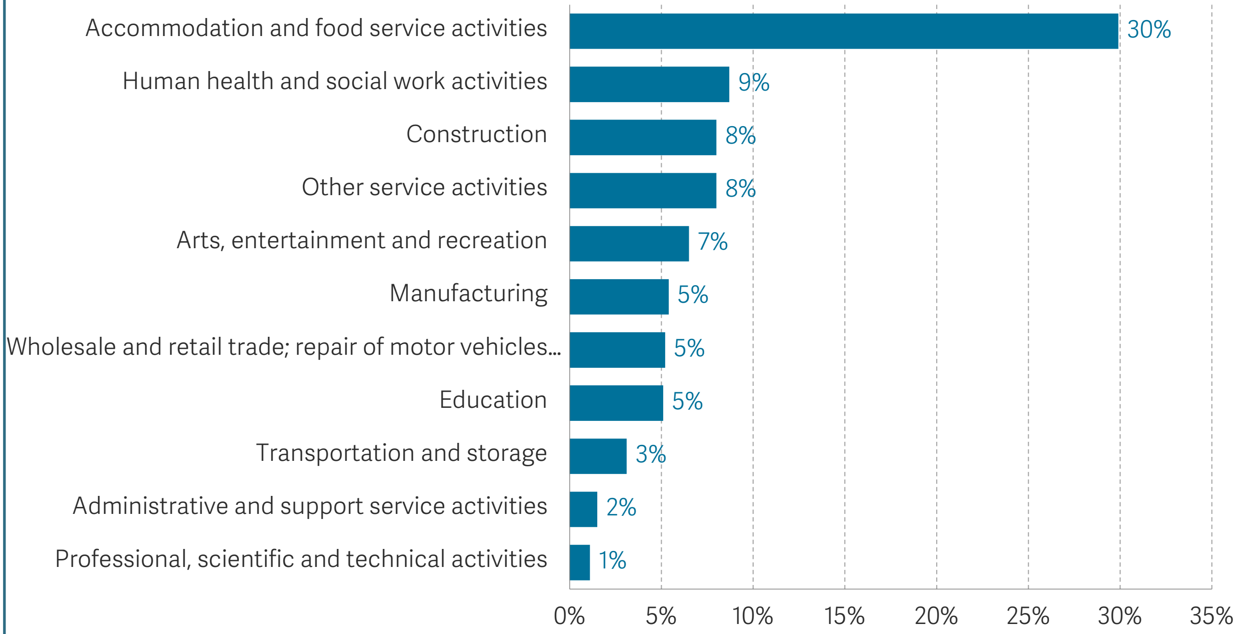
BOX 3: **Hospitality businesses are closing more often in the face of high energy bills**

The government has provided £18.4 billion of support for businesses energy bills this winter, but any support beyond March is subject to an HM Treasury review, due to report at the end of 2022. This review includes examining which business are most acutely affected by rising energy costs.

Despite existing support, it is hospitality businesses that are struggling in the face of rising energy bills with 57 per cent of accommodation and food services businesses reporting that energy bills were their main concern in November compared with 22 per cent of all businesses. To cope, 30 per cent of hospitality businesses reported that they are closing more to reduce energy costs compared with 6 per cent of all businesses (Figure 16).

FIGURE 16: **Hospitality businesses are closing more due to pressures from energy bills**

Businesses reporting that they have cut back on energy use by reducing trading hours or days over the past 3 months by industry: UK, October 2022



NOTES: Businesses responding that they have taken any of the following three actions in the past three months: Reduced the number of days the business trades in a week by two or more days, Reduced the number of days the business trades in a week by one day, Reduced the number of hours the business trades in a week, but the number of days the business trades in a week remained as usual.
SOURCE: RF analysis of BICS, 17 October 2022 to 30 October 2022.

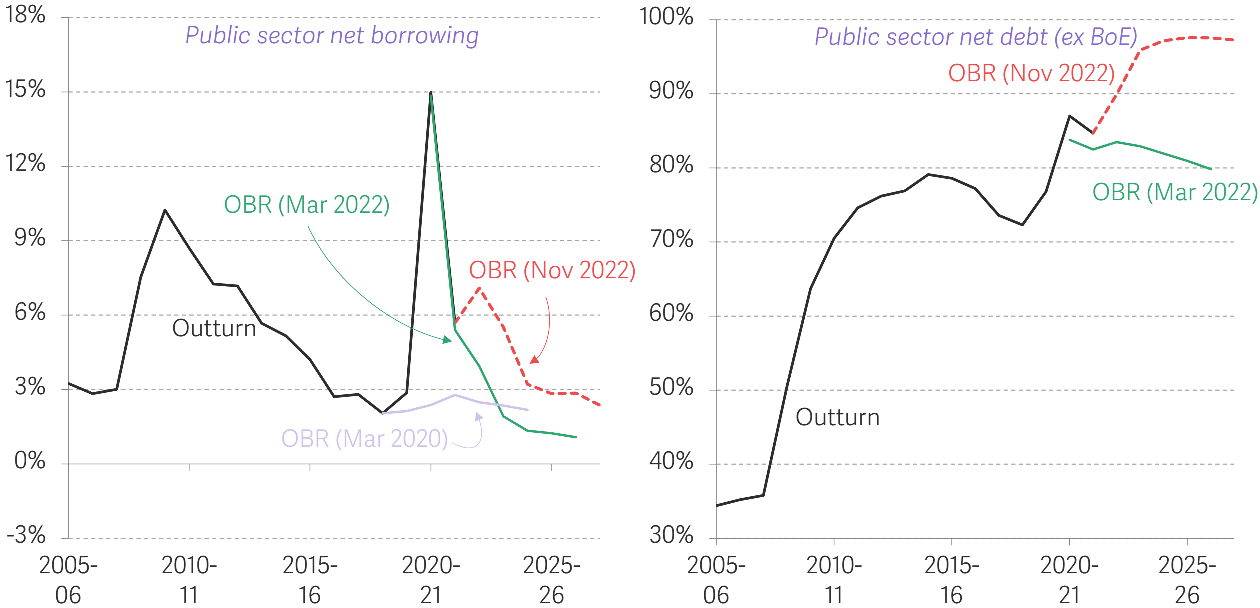
While extra fiscal support has been the priority for this year and next, the Chancellor has then put in place a significant fiscal tightening to which we now turn.

Amidst the fallout from the mini-budget, the Government has focused on fiscal sustainability in the medium term

Higher interest rates, a smaller economy and the cost of the energy package mean that the public finances are in a much worse shape than expected at the start of the year. Indeed, as shown in Figure 17, borrowing is expected to remain permanently higher than expected back in March (only falling to 2.4 per cent of GDP by 2027-28) and debt is now projected to rise again and stabilise at over 97 per cent of GDP. The 'ratcheting up' of debt since the turn of the century following the financial crisis, pandemic and the cost of living crisis now stands out clearly.

FIGURE 17: **Borrowing is expected to remain permanently higher and debt is ratcheting upwards again**

Public sector net borrowing and public sector net debt (excluding the Bank of England) as a share of GDP, outturn and select OBR forecasts: UK



SOURCE: OBR, Economic and Fiscal Outlook – November 2022.

The Chancellor had already reversed some of the decisions taken at the mini-budget in order to reassure markets that the public finances will be kept on a sustainable course. He went further in the Autumn Statement, guided by a new set of fiscal rules – these are discussed further in Box 4. To meet them, the Government has raised taxes and cut spending by a total of around £55 billion by 2027-28.

BOX 4: **The Government's new, looser fiscal rules**

The Chancellor announced two fiscal 'targets' in the Autumn Statement, effectively replacing the existing rules.[11] The first target is to ensure public sector net debt (excluding the Bank of England) falls as a share of GDP at the end of a rolling five-year horizon (currently applying in 2027-28). This is the same as one of the pre-existing rules, but with the horizon lengthened by two years. The second rule is to ensure that public sector net borrowing in the same year of the forecast is below 3 per cent of GDP.

These rules are noticeably looser than their predecessors, offering the Chancellor significant flexibility on the timetable over which he consolidates (sensibly allowing him to do so largely

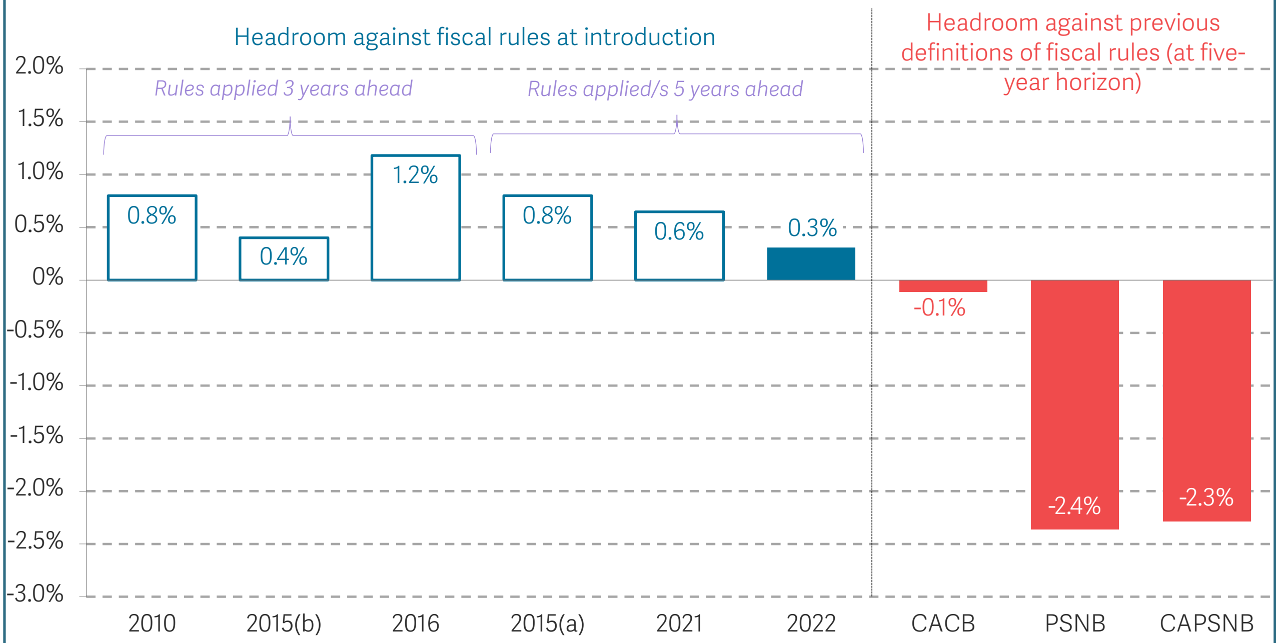
11 The Government has also chosen to keep the pre-existing welfare cap rule, but this does not pose a significant constraint and so we do not discuss it.

after the current recession) and how he does it (focusing on the overall level of borrowing rather than the current balance gives him more scope to cut capital spending to achieve his fiscal rules if required).

The 'headroom' (i.e. the margin for error) against meeting the rules is the lowest for any set of rules at their introduction since 2010 (0.3 per cent of GDP), as Figure 18 shows.[12] It is also clear that, even with a generous five years to meet them, the current forecasts suggest the Government would fail to meet previous definitions of fiscal rules.

FIGURE 18: **The Government has little headroom against its new fiscal rules and those rules themselves are not very constraining**

Fiscal headroom at introduction for fiscal rule regimes since 2010 and current headroom against those previous rules based on the November 2022 forecast, as a share of GDP: UK



NOTES: The headroom for rules introduced in 2010 and the first set in 2015 were based on the cyclically adjusted current balance (CACB); the second set of rules in 2015 was based on public sector net borrowing (PSNB); the set in 2016 was based on cyclically adjusted public sector net borrowing(CAPSNB); and the set in 2021 was based on the change in public sector net debt excluding the impact of the Bank of England. CACB is a rule to have a cyclically adjusted current balance, PSNB is a rule to have negative public sector net borrowing (i.e. a borrowing surplus) and CAPSNG is a rule to have a cyclically adjusted public sector net borrowing surplus.
SOURCE: OBR, Economic and Fiscal Outlook (various).

Reasonable people will disagree about optimal fiscal rules (this is the sixth set since 2010), but there are some important issues to highlight with the new rules. First, the framework treats current and investment spending as broadly equivalent despite clear evidence that investment can raise the

12 The 'debt falling' rule is harder to meet under the OBR's forecasts and so that is the rule on which we focus our attention.

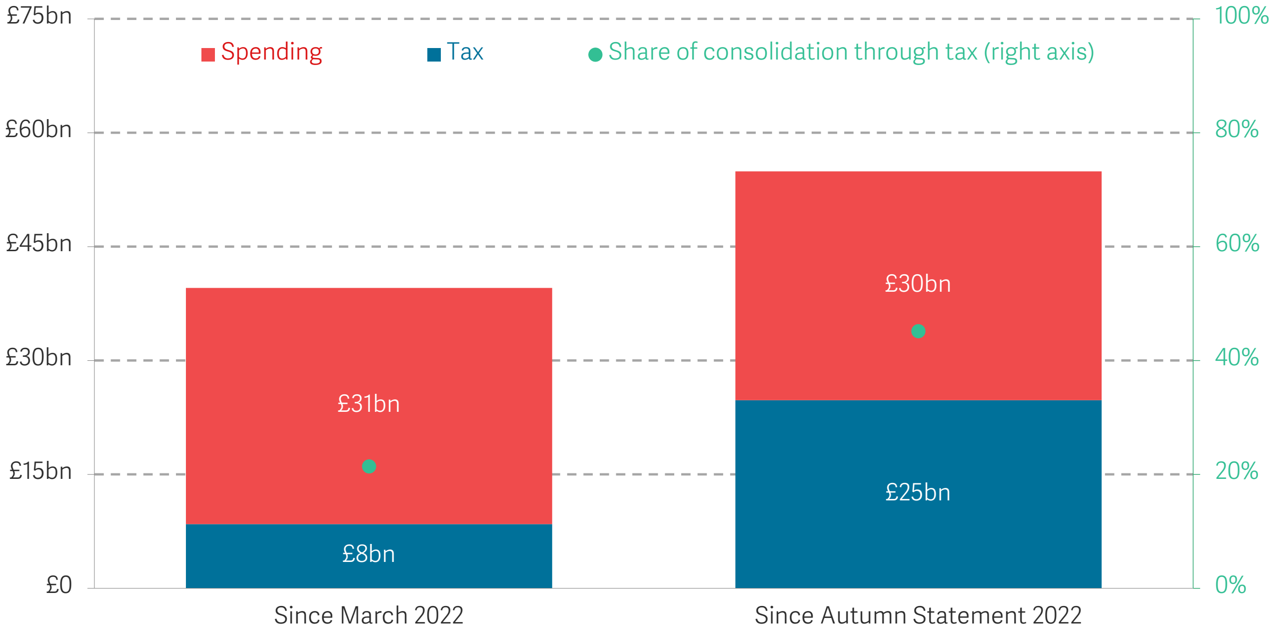
level of long-term economic activity and thus future tax revenues. Second, nothing in the framework is designed to deliver actual falls in public sector debt, which is particularly concerning given the ratchetting-up of debt after each crisis. Finally, the long horizon, while useful in that it allows adjustment in the face of shocks, provides little constraint on actual spending and taxes: it constrains fiscal plans rather than outcomes.[13]

Since March, the net consolidation is focused on spending cuts but, looking since the pandemic began, the tightening is tax heavy

The medium-term fiscal tightening in the Autumn Statement amounts to £55 billion by 2027-28, split fairly evenly into spending cuts and tax rises (£30 billion and £25 billion respectively). That is broadly equivalent in scale to the consolidation announced by George Osbourne in his first Budget in 2010, in which total consolidation measures equated to around £50 billion at the end of the forecast.[14]

FIGURE 19: **The total planned consolidation and its nature depends on the baseline against which it is measured**

Announced net fiscal consolidation by tax and spend measures, since various fiscal event milestones: UK, 2027-28



SOURCE: RF analysis of OBR, Economic and Fiscal Outlook - various; HM Treasure, Autumn Statement 2022.

13 This itself could create a bias towards higher current spending or lower taxes and away from higher investment spending. This is because investment spending requires long-term planning, so will be more likely to be cut to meet the future rule target, but, as the horizon rolls over each year, current spending might rise or taxes be cut. For more detail on the optimum set of fiscal rules, see: R Hughes et al., Totally (net) worth it: The next generation of UK fiscal rules, Resolution Foundation, October 2019.

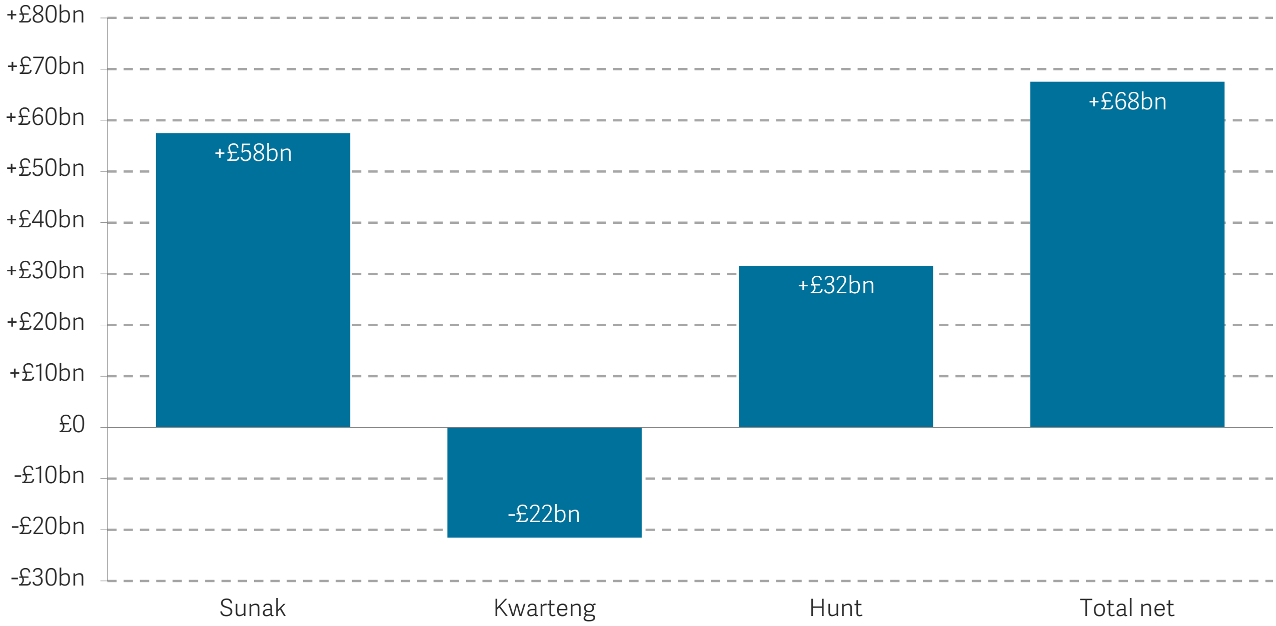
14 This is calculated using the policy measures announced in the second Budget of 2010 uprated to 2026-27 prices using the GDP deflator. Note that the previous Labour government had announced consolidation measures in previous fiscal events which meant that the total consolidation planned at the time of the second 2010 Budget was substantially larger than £50 billion.

But assessing the consolidation in this way misses that there were significant tax cuts in the mini-budget, followed by U-turns on some of those tax cuts. So, Figure 19 also shows the total consolidation of decisions taken since March 2022, i.e. encompassing all of the decisions taken in the mini-budget and subsequent U-turns. Taking this perspective reduces the scale of the consolidation to about £40 billion in 2027-28, with only around a fifth coming from tax rises. This is because, to a large extent, the tax rises announced in the Autumn Statement are offsetting the remaining tax cuts from the mini-budget, principally the abolition of the Health and Social Care Levy (we show this in detail below, in Figure 21).

But it is worth taking an even broader view since the pandemic. For that bigger picture, the story has been as follows: Rishi Sunak as Chancellor raised taxes to fund an increase in spending on public services, Liz Truss followed that by cutting taxes in the mini-budget, and Jeremy Hunt has reversed most of Sunak's spending rises and more than all of Truss' tax cuts. On this basis the net result is that total long-term spending plans are largely unchanged since the start of the pandemic, leaving the consolidation entirely driven by tax rises. [15] This is in sharp contrast to the post-financial crisis fiscal tightening, when almost 80 per cent came from spending cuts. As shown in Figure 20, net tax rises announced since the start of the pandemic are expected to bring in an additional £68 billion (or 2.3 per cent of GDP) in 2027-28.

FIGURE 20: **Since the start of the pandemic, there have been significant tax rises**

Impact of tax policy changes under successive Chancellors: UK, 2027-28



SOURCE: RF analysis of OBR, Economic and Fiscal Outlook - November 2022.

15 OBR, Economic and Fiscal Outlook – November 2022, Chart 18.

The Autumn Statement announced significant tax rises, but the focus on threshold freezes over rate rises limits its progressivity

The Autumn Statement was big on tax. The Chancellor announced 30 tax measures that are expected to raise a total of £25 billion in 2027-28.[16] The big announcements include:

- Reducing the Income Tax additional rate threshold (i.e. the point from which the 45 per cent rate is payable) from £150,000 to £125,140 from April 2023, raising around £0.9 billion in 2027-28.
- An additional two-year freeze, until April 2028, on personal tax thresholds within Income Tax, National Insurance (NI) and Inheritance Tax, which together will raise £1.3 billion in 2027-28.
- A staged reduction in the generosity of the Dividend Allowance and the Capital Gains Tax Annual Exempt Amount, raising £1.4 billion in 2027-28.
- Introducing Vehicle Excise Duty on electric cars, vans and motorcycles from April 2025, raising £1.6 billion in 2027-28.
- Extending windfall taxes on energy companies under the Energy Profits Levy and a new Electricity Generator Levy to help fund government support for energy bills, raising £5.6 billion in 2027-28.
- A new five-year freeze of the NI Secondary Threshold for employers at £9,100 until April 2028, raising almost £6 billion in 2027-28.

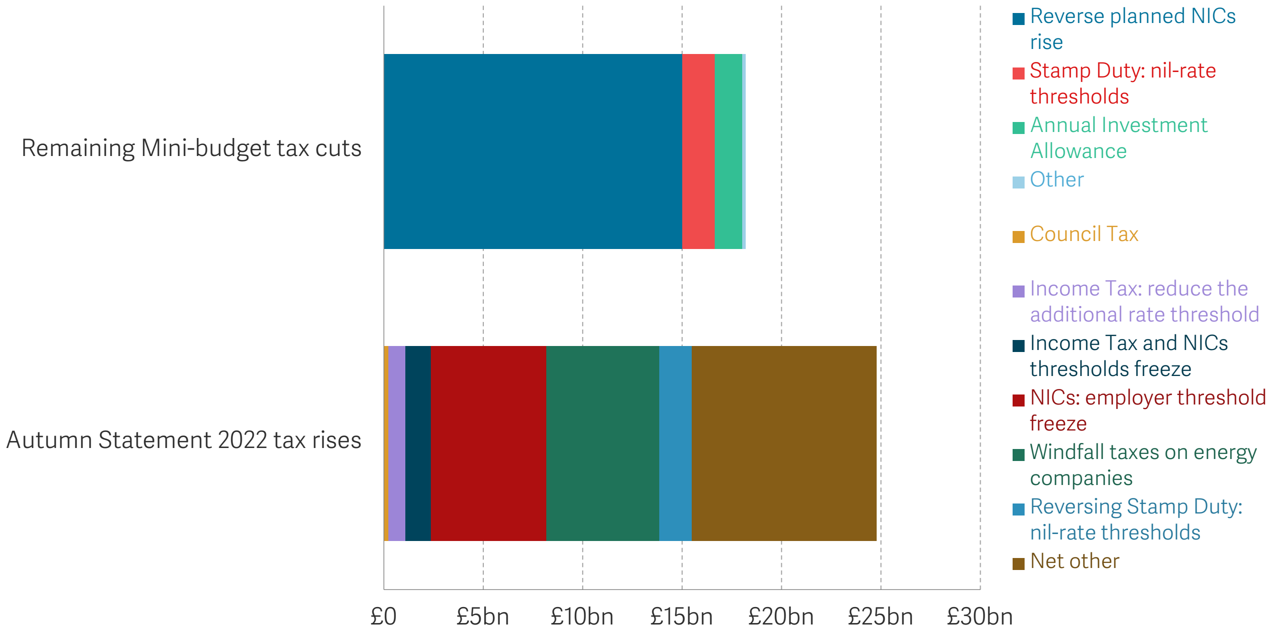
However, as shown in Figure 21, the £25 billion of tax rises announced in the Autumn Statement did little more than offset the £18 billion of tax cuts that remained from Liz Truss' tenure as Prime Minister, the largest of which is the reversal of the NI rate rise introduced in April 2023 (and the abolition of the 'Health and Social Care Levy' that was to replace it).

Among the tax rises in the Autumn Statement were three substantial cuts to tax thresholds. First, the reduction in the Income Tax additional rate threshold will cost additional-rate payers up to around £1,200 per year (for comparison: someone on £150,000 would have paid around £1,700 a year in the Health and Social Care Levy, and someone on £300,000 would have paid £3,600). The fact that the threshold has been set at the strange-looking value of £125,140 reflects that the withdrawal of the Personal Allowance in effect raises the marginal rate of Income Tax to 60 per cent between £100,000 and £125,140, and so the new measure abolishes the 40p band that currently exists between £125,140 and £150,000: a small simplification.

16 This excludes any additional Council Tax revenues that will arise if local authorities use their new-found freedoms to increase Council Tax rates faster.

FIGURE 21: **Most of the Autumn Statement tax rises simply offset the remaining £18 billion tax cuts from Liz Truss' tenure**

Impact of Mini-budget and Autumn Statement tax policy announcements, 2027-28 nominal terms: UK



SOURCE: RF analysis of HM Treasury, Autumn Statement 2022 Policy Decisions.

Second, the dividend allowance will be cut in stages from £2,000 to £500, costing affected higher- rate payers around £500. Third, the Annual Exempt Amount for Capital Gains Tax will be slashed in stages from £12,300 to £3,000, raising bills by up to £2,600 a year for around 300,000 people.[17] These welcome changes reduce the bias in the tax system towards those who can divide their income across different types of income.[18]

These changes predominately affect middle- and higher-income households. As a result, the combined impact of these new personal tax measures plus the two-year extension of the income tax and NI threshold freezes is very progressive: 89 per cent of the revenue from these changes in 2027-28 comes from the top half of the household income distribution, and 70 per cent comes from the top one-fifth.

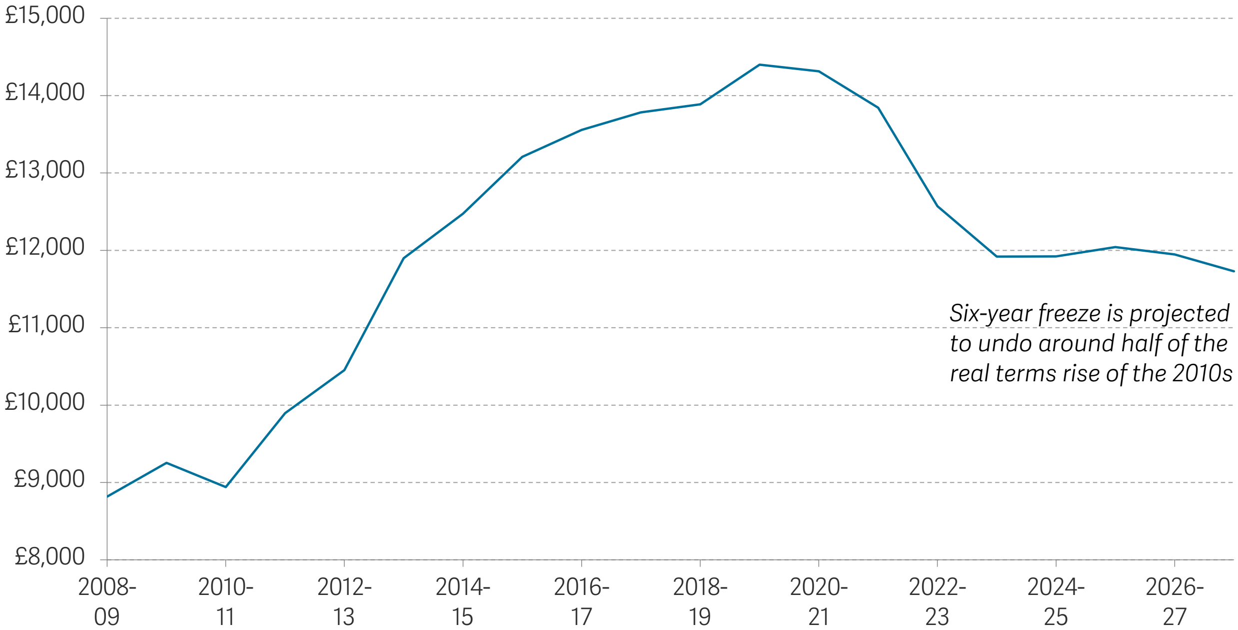
But, alongside a higher Corporation Tax rate – where the new 25 per cent standard rate reverses most of the headline rate cuts since 2011-12, when the rate was 26 per cent – the tax-increasing policy reform of choice this Parliament has been to freeze various tax thresholds.[19] The Autumn Statement has raised money from four sets of threshold freezes, which together will raise £7.5 billion in 2027-28 (on current inflation forecasts).

17 HMRC, Capital Gains Tax statistics, August 2022.
18 G Bangham et al., Unhealthy Finances, Resolution Foundation, November 2020.
19 In 2020, we made the case that threshold freezes and Corporation Tax rate increases were the 'easy options' for fiscal consolidation, although we did not propose that the Government rely quite so heavily on them as it has in practice. See: G Bangham et al., Unhealthy Finances, Resolution Foundation, November 2020 for further details.

First, the extension of freezes in the Income Tax and personal NI systems to 2027-28 means that the starting point for paying tax will remain at £12,570, and the higher-rate threshold will remain at £50,270, for longer than previously planned. These will not rise until April 2028. However, the OBR's current inflation forecast would have meant zero uprating in 2025-26 and 2026-27 even without the Autumn Statement's change (due to the predicted fall in the CPI index), and the usual rules for changing tax thresholds suggest that only a 0.9 per cent rise would have happened in April 2027, so the extension of the freeze is not currently expected to have as large an impact as those taking effect in April 2023 and April 2024. But the full impact of the six-year personal allowance freeze is substantial: the personal allowance would have been expected to reach £15,400 in 2027-28, rather than £12,570, a difference equivalent to paying £600 more in Income Tax that year. A higher personal allowance was a signature tax cut of the 2010s: this freeze undoes around half (49 per cent) of those rises in real terms, and takes its level back to around where it was in 2013-14 (see Figure 22).

FIGURE 22: **The six-year personal allowance freeze is set to undo around half of its real terms rise over the 2010s, taking it back to around its 2013-14 level**

Income Tax personal allowance, in 2022-23 real terms: UK



NOTES: Age-related personal allowances not included.
SOURCE: RF analysis including CPI forecasts from OBR, Economic and Fiscal Outlook, November 2022.

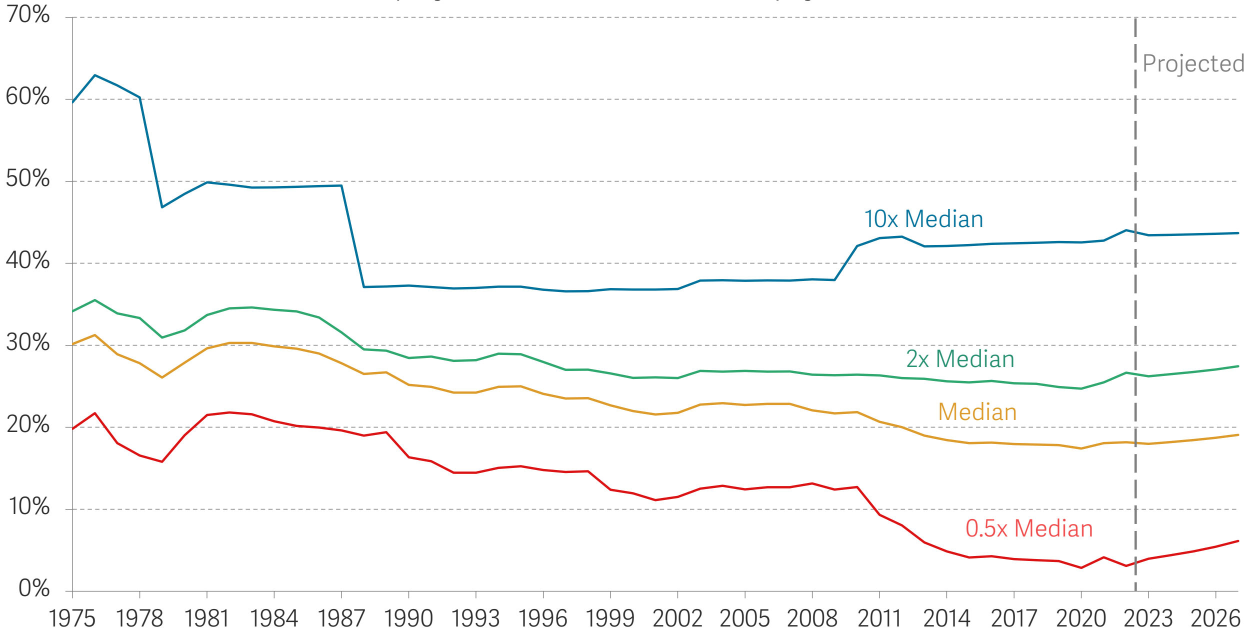
Second, freezes in the Inheritance Tax system means that the combined amount that can be inherited tax-free remains at £1 million until April 2028. However, just as with the extension of the income tax threshold freezes, the weak outlook for inflation in 2025 and 2026 means that this policy change raises relatively little. Prior to this extension, the OBR forecast that 7 per cent of deaths would lead to Inheritance Tax liability by 2026-27 – up from 4 per cent in 2019-20 – still only a small minority of estates.[20]

Third, the freezing of the VAT threshold has also been extended (though only to April 2026), which will mean that fewer businesses are exempt from the tax. The UK's VAT threshold of £85,000 is very high by international standards, and it is well known that it distorts business behaviour, so this freeze is welcome.[21]

Fourth, and most significantly, there is a new five-year freeze in the employer NI threshold: this is the biggest single tax rise in the Autumn Statement, as the counterfactual would have been large inflation-linked rises in April 2023 and April 2024. In aggregate, this is broadly similar to replacing the employer Health and Social Care Levy. But its distribution across the workforce will differ: the threshold freeze will mean a mostly flat tax rise of around £240 a year per employee by 2027-28 (based on current inflation forecasts). This means that lower-paid workers will attract higher tax bills under this threshold freeze than if the Levy's 1.25 per cent tax rate had remained; the crossover point is around £18,800 a year.

FIGURE 23: **Effective tax rates are rising due to freezes, but only back to 2013-14 levels for a typical employee**

Effective tax rates for employees on different levels of pay: UK



NOTES: Includes Income Tax and Employee (but not Employer) National Insurance. For consistency, tax rates are for unmarried employees under 65 with non-volatile earnings. Recent divergences in Scotland are not included. Projections include threshold freezes. For 2022-23 the temporarily raised rates of National Insurance – along with the higher starting point – are used.
SOURCE: RF analysis using median earnings figures from ASHE/NESPD; tax history from HMRC and IFS; and earnings projections from OBR.

20 OBR, Economic and Fiscal Outlook, March 2022.
21 G Bangham et al., Unhealthy Finances, Resolution Foundation, November 2020.

The big picture on Income Tax and NI for most people is that the multi-year threshold freezes represent a large tax rise, with the OBR estimating they raise a total of £35 billion by 2027-28. As Figure 23 confirms, over the period of the freeze as a whole, effective (average) tax rates are set to rise for employees, yet only back to 2013-14 levels for a typical employee (with a tax rate of 19 per cent) or a low-earning employee (6 per cent).[22]

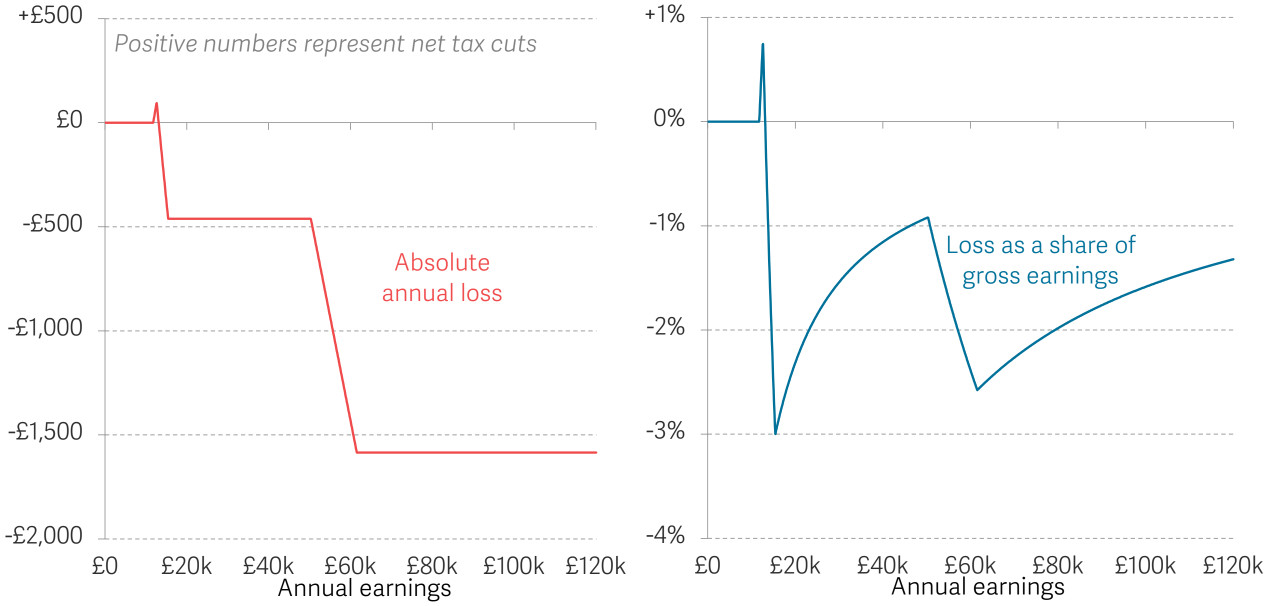
As with employer taxes, a reliance on threshold freezes rather than rate rises (i.e. the Health and Social Care Levy) makes the distribution of tax rises less fair, in some ways, than it could have been. The Levy had its own inequities, and the combination of raising NI while cutting the basic rate of Income Tax (which was policy under Chancellor Sunak) was particularly nonsensical. But to raise additional revenue from Income Tax and personal NI contributions via threshold freezes does lead to some regressive results, as Figure 24 shows. For example, an employee earning £15,500 in 2027-28 will lose 3.0 per cent (£500) of their gross income due to tax rises, relative to if none of the policy changes since 2021 happened; and someone on £62,000 will lose 2.6 per cent (£1,600); someone earning £124,000, though, will lose 1.3 per cent of their income (also £1,600). Furthermore, as we show later in this note, although the top 20 per cent and middle one-fifth face tax rises of around 3.7 per cent of income (£3,600 and £1,400 respectively) from the personal tax rises announced in this Parliament, compared to 1.8 per cent or £350 for the poorest fifth, the very top 5 per cent pay less proportionally, with personal tax rises only worth 3 per cent of income.[23] These results are all driven by the largely flat cash tax rise for anyone affected by each frozen tax threshold.

The reluctance to raise headline personal tax rates is perhaps also reflected in the upward trajectory of Council Tax levels. The Government is giving local authorities in England additional flexibility to raise Council Tax bills without the need for a local referendum. As a result of this policy, the OBR expects Council Tax bills to rise by around 5 per cent a year over the next five years, raising around £4.8 billion a year by 2027-28. This would see bills rising by around £250 for the average band D property by 2027-28.[24] However, as demonstrated in Figure 25, universal increases in Council Tax are much less progressive than increases in Income Tax.

22 These figures include Income Tax and employee National Insurance, but not employer National Insurance.
23 The richest tenth of households will see tax rises of around £4,300 in cash terms, or 3 per cent of income.
24 Office for Budget Responsibility, Economic and fiscal outlook, November 2022.

FIGURE 24: **Relying on threshold freezes means that someone earning £124,000 will experience the same cash tax rise as someone on £62,000, and the greatest tax rise relative to income is for someone earning around £15,500**

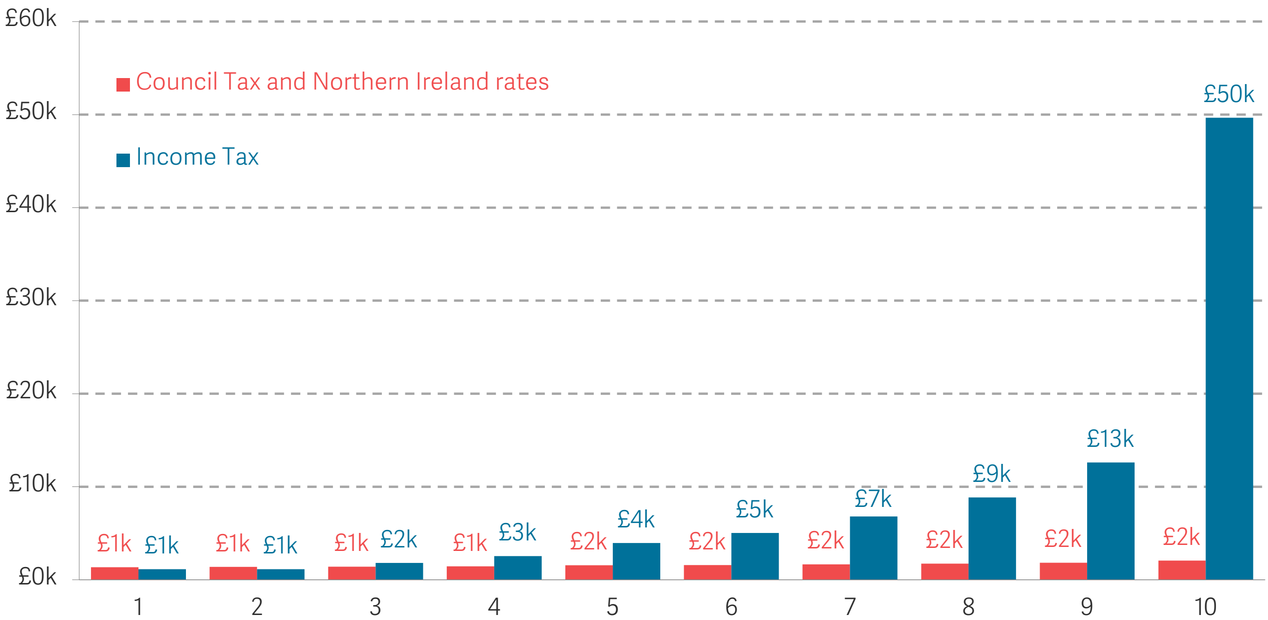
Combined impact of Income Tax and employee National Insurance changes in 2027-28, by level of employee earnings: UK



NOTES: Includes freezes in the personal allowance and higher rate threshold, and the increased starting point for National Insurance.
SOURCE: RF analysis, including counterfactual inflation-linked uprating using OBR, Economic and Fiscal Outlook, November 2022.

FIGURE 25: **Increases in Council Tax would be relatively regressive compared to Income Tax**

Average Council Tax and Income Tax paid by individuals per year, by equivalised household disposable income decile group, 2020-21: UK



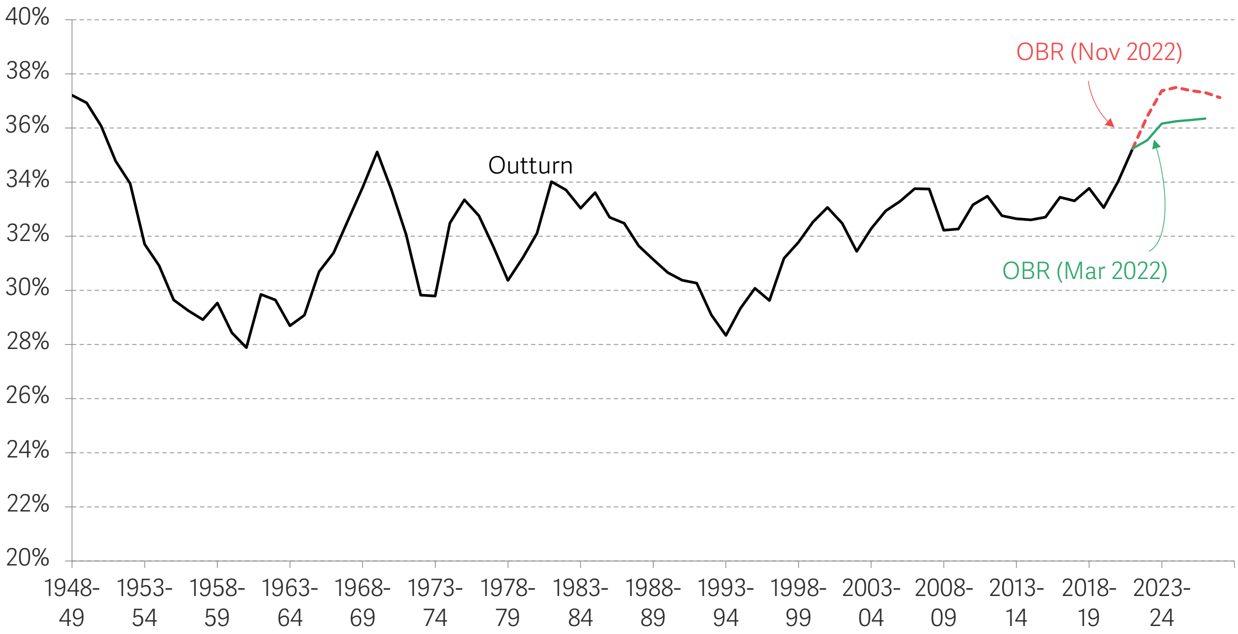
SOURCE: ONS, The Effects of Taxes and Benefits on Household Income, UK, 2020-21.

Tax revenues are forecast to rise as a share of GDP to record levels, but there are many sources of uncertainty

The overall effect of the Autumn Statement decisions, coming on the back of two tax-rising Budgets in 2021 and changes to the economic forecasts, is that tax as a share of GDP is on course to hit to a 70 year high by the middle of the decade. As Figure 26 shows, it is expected to reach 37.5 per cent by 2024-25, its highest level since the Second World War. This also represents a rise from the March 2022 forecasts, although this is due more to changes in how much previous policy announcements are expected to raise than to new policy changes.[25]

FIGURE 26: **Taxes relative to GDP are projected to rise to their highest levels in over 70 years**

National accounts taxes as a proportion of GDP: UK



SOURCE: RF analysis of OBR, Public finances databank.

However, there are many ways in which the forecast for taxes might change significantly. First, the Energy Profits Levy and Electricity Generator Levy are set to disappear after 2027-28, with an estimated revenue of £5.6 billion in their final year (these are discussed further in Box 5.) All else equal, this revenue may need replacing.

25 See Chart 15 in OBR, Economic and Fiscal Outlook, November 2022.

Second, the OBR's forecast assumes that Fuel Duty rises significantly in 2023. A temporary 5p cut is due to expire, and the rate is additionally due to rise in line with RPI inflation. The OBR estimates these together would add 12p per litre to the price of petrol and diesel, and add £5.7 billon to tax receipts next year. How likely this is may depend in part on the trajectory of prices nearer the time, but given that this would be the first time any Government has raised Fuel Duty rates in cash terms since January 2011, it is surely a good bet that this does not happen in full. Allowing the 5p cut to expire but cancelling the RPI-linked increase would cost over £2 billion a year compared to the current revenue forecasts.

In contrast, the Chancellor did make a start on addressing a longer-term fiscal risk, by introducing Vehicle Excise Duty (VED) for electric vehicles. As such, electric cars registered from April 2025 will be subject to VED at the lowest first year rate of £10, jumping to £165 thereafter. A flat annual charge per car is not an ideal form of vehicle taxation, but this should perhaps be seen as a policy that could make a transition to road pricing easier.

The Autumn Statement also reverses the increase in the nil-rate threshold of Stamp Duty Land Tax announced in the mini-budget. Instead, this is now due to be a temporary measure, remaining in place until the end of March 2025, and thereby raising £1.6 billion in 2027-28. However, it is unclear whether any future Chancellor will want to go through with a significant increase in Stamp Duty, with the associated disruption to the housing market.

Finally, although many parts of the economic outlook will shape future tax receipts, it should be noted that the amount of revenue raised by threshold freezes will depend on inflation. The OBR's forecast of deflation is notable, and if the Bank of England's inflation projections for 2023 to 2025 turn out to be more accurate, then the Income Tax and NI freezes would raise an additional £5 billion to add to the £35 billion that is currently forecast.

BOX 5: Bolstered windfall taxes will push North Sea tax receipts to their highest on record, and recoup excessive profits from electricity generators

In his hunt for additional revenue sources, the Chancellor has increased the Energy Profits Levy rate by 10 percentage points, raising the effective tax rate on North Sea oil and gas companies' profits to 75 per cent. This is close to double the pre-crisis rate and in line with that in Norway (78 per cent). As such, anticipated receipts this year are up from £5 billion to £7.2 billion, with revenues in 2023-24 now expected to reach an all-time high in cash terms (£20.7 billion, of which £10.8 billion would be due to the Energy Profits Levy) and the highest as a share of GDP since the mid-1980's North Sea boom.

Renewable and nuclear electricity generators that have benefitted from surging electricity prices will also face a new tax, paying 45 per cent of profits made on electricity sold at £75 per megawatt hour or more.[26] When combined with Corporation Tax, this will mean a headline rate of 70 per cent, slightly lower than that which applies to oil and gas companies, and applying only to sales resulting in 'extraordinary profits'. However, renewable and nuclear electricity generators will not be able to reduce their tax bill by investing in the UK, unlike oil and gas companies, who are incentivised to bring additional North Sea oil and gas fields online; this is somewhat at odds with the Government's aims of achieving a net zero emissions economy and runs contrary to advice from the Climate Change Committee.

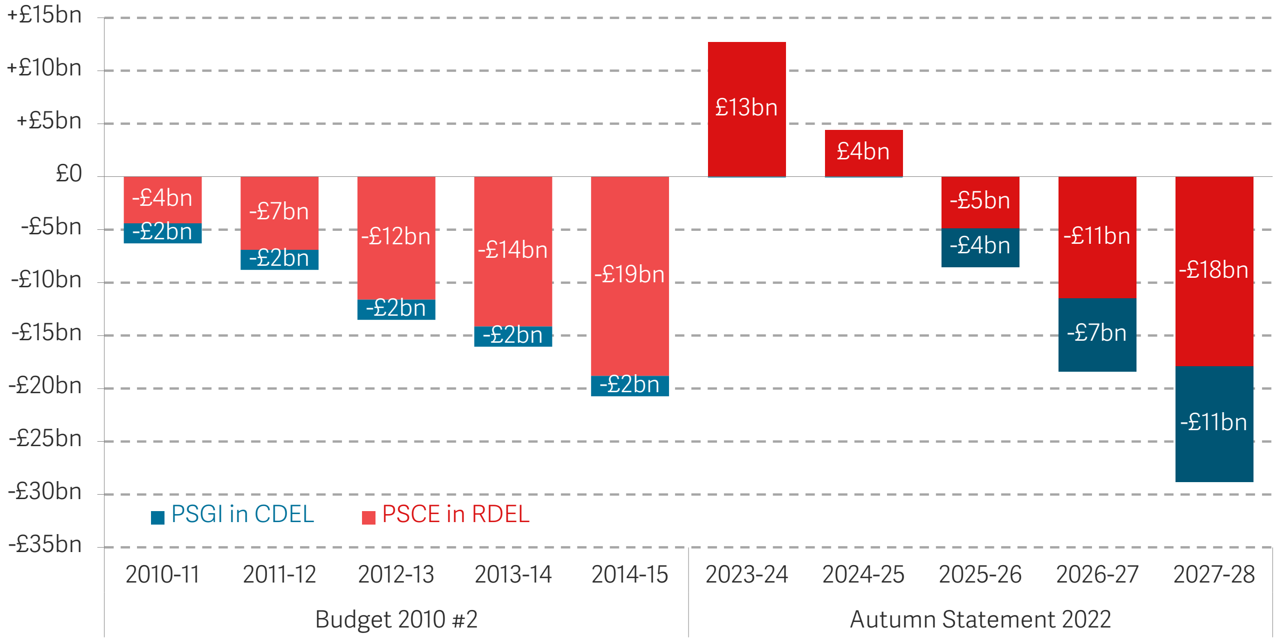
The spending side of the consolidation has been pencilled in for the second half of the decade

The Autumn Statement included significant spending cuts, rising to £30 billion in 2027-28 (in 2022-23 prices). As shown in Figure 27, the scale of this is of the same order of magnitude as that announced in George Osborne's June 2010 Budget, but there are big differences in the composition. In contrast to very concrete tax rises already underway, spending cuts this time are only pencilled in to begin towards the end of the forecast period rather than immediately as in 2010.[27]

26 This conditionality means that companies that have sold power ahead at prices below £75/MWh will not be impacted.
27 The cuts to departmental budgets announced in the Autumn Statement are larger than those announced in Budget June 2010, but the forecast decline in the path of RDEL and CDEL relative to GDP (which measures the intensity of public services austerity) is significantly smaller. The plans in Budget June 2010 involved RDEL falling by 4.5 percentage points relative to GDP over the forecast period (as a result of large cuts already put in place prior to the 2010 election for these years) compared to a fall of 1 percentage point in Autumn Statement 2022.

FIGURE 27: **The current consolidation is more focussed on departmental spending and more back-ended than that announced in the Budget of June 2010**

Real change in Public Sector Gross Investment (PSGI) and Public Sector Current Expenditure (PSCE) announced at Budget June 2010 and Autumn Statement 2022: UK



NOTES: PSGI refers to capital investment and PSCE refers to day-to-day spending. All figures are in 2022-23 cash terms using the GDP deflator.
SOURCE: RF analysis of OBR, Policy measures database and Economic and Fiscal Outlook, November 2022.

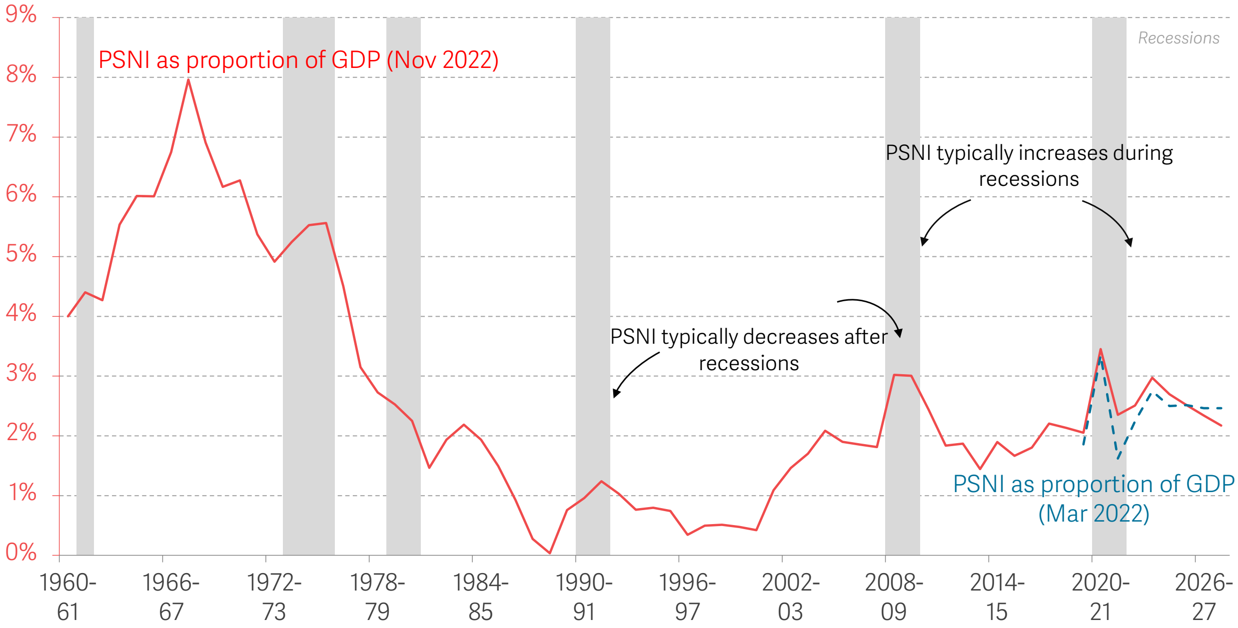
The Chancellor has chosen to prioritise cuts to public investment to fill the forecast fiscal hole

As Chancellor, Rishi Sunak had intended for Public Sector Net Investment (PSNI) to rise to 2.5 per cent of GDP by 2026-27, the highest sustained levels since the 1970s. But, faced with the need to make savings, Rishi Sunak as Prime Minister has followed the example of every recent government delivering a fiscal consolidation by reaching for cuts to investment (see Figure 28). PSNI is planned to be held constant in cash terms from 2025-26 onwards, saving £15 billion by 2027-28 when it will have fallen to 2.2 per cent of GDP. This turns a previously expected 0.6 percentage points of GDP rise into one of only 0.1 percentage points, cancelling roughly four-fifths of the increase in PSNI originally planned by Rishi Sunak.

While, by the end of the OBR's forecast period, PSNI as a share of GDP is still set to be about 0.2 percentage points above the average for this century, these cuts remove a key plank of Boris Johnson's 'levelling up' agenda, which rested on capital allocations to local areas, and pose a challenge to the Government's net zero ambitions. More generally, they come in the context of the UK's long-standing weakness in investment.[28]

FIGURE 28: **Public sector net investment is only expected to reach 2.2 per cent of GDP by 2027-28**

Real public sector net investment as a proportion of GDP: UK, 1960-61 to 2027-28



SOURCE: RF analysis of OBR, Public Sector Finances Databank; Bank of England, A millennium of macroeconomic data for the UK, 2020.

While the Chancellor has attempted to maintain budgets in real terms, uncertainty around inflation means there is a risk that more money will be needed or public services spending power fall

Alongside cuts to public investment, the Chancellor has pencilled in bigger reductions in day-to-day public service spending for after 2024-25 (and the next election).

But public service spending power is at more immediate and concrete risk from higher-than-expected inflation eating into departmental budgets that run to 2024-25, agreed as part of Spending Review in October 2021 (SR21). Figure 29 demonstrates how the higher OBR forecast for GDP-deflator inflation compared to March means that those budgets are now approximately £5 billion smaller in 2023-24 and 2024-25 than originally expected. Indeed, this is an underestimate of the impact of inflation because important elements of departmental costs – such as higher imported energy costs – are not accounted for in the GDP-deflator.

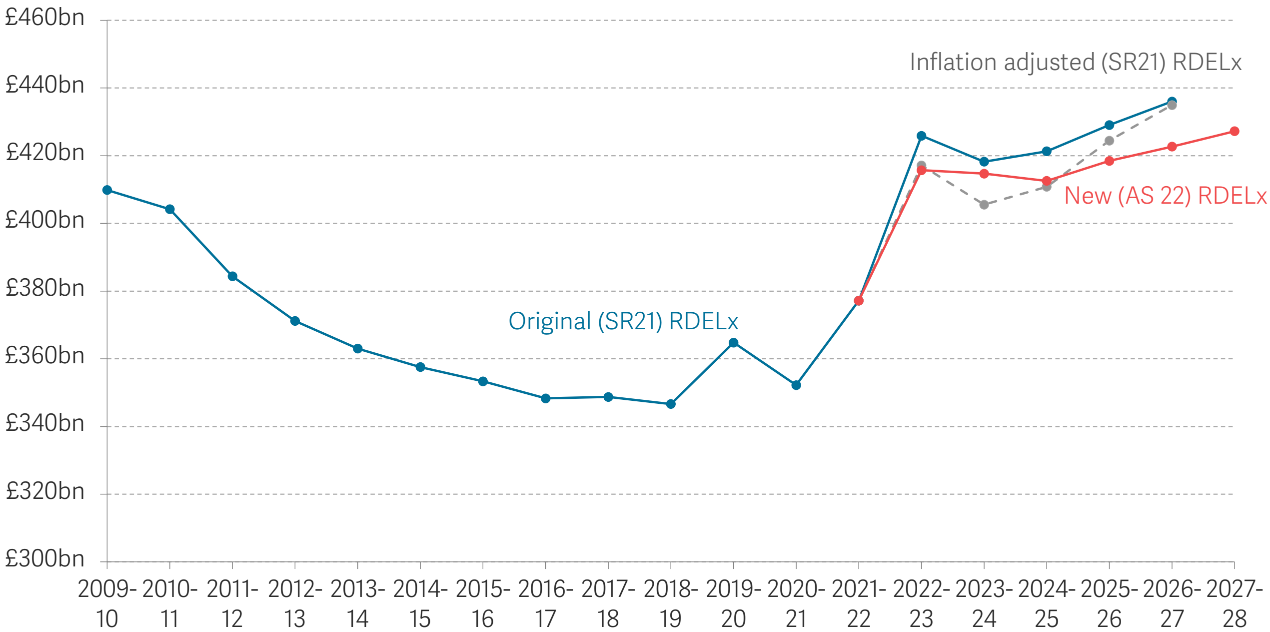
28 Resolution Foundation & Centre for Economic Performance, LSE, Stagnation nation: Navigating a route to a fairer and more prosperous Britain, Resolution Foundation, July 2022.

To partly compensate, an extra £3.3 billion was made available to the NHS in 2024-25 and an extra £2.3 billion given to schools in both 2023-24 and 2024-25 (to argue that real, per-pupil, spending levels are being maintained). These increases (and their Barnett consequentials, plus smaller increase elsewhere) leaves overall day-to-day spending flat in real terms in 2023-24, while the Government has in effect reallocated the £5 billion which was originally reserved to bring Overseas Development Assistance (ODA) back up to 0.7 per cent of GNI in 2024-25 to fund them in that year.[29] These increases do not, however, completely offset the impact of higher inflation, with real spending growth over the SR21 period falling from an expected 3.5 per cent a year when first announced in October 2021, to under 3 per cent a year now.

The Chancellor also announced a plan to reduce the rate at which spending grows following the end of the spending review period, with the aim of ensuring a 1 per cent per year real-terms increase in total RDELS. This is lower than the previous assumption of a 2.5 per cent a year real-terms increase. If this were to come about, then spending would be roughly £22 billion lower in 2027-29 than expected before the Autumn Statement.

FIGURE 29: **The top ups to schools and NHS budgets offsets some of the impact of inflation on total spending in the near term**

Real Resource Departmental Expenditure Limits excluding depreciation (RDELx): UK



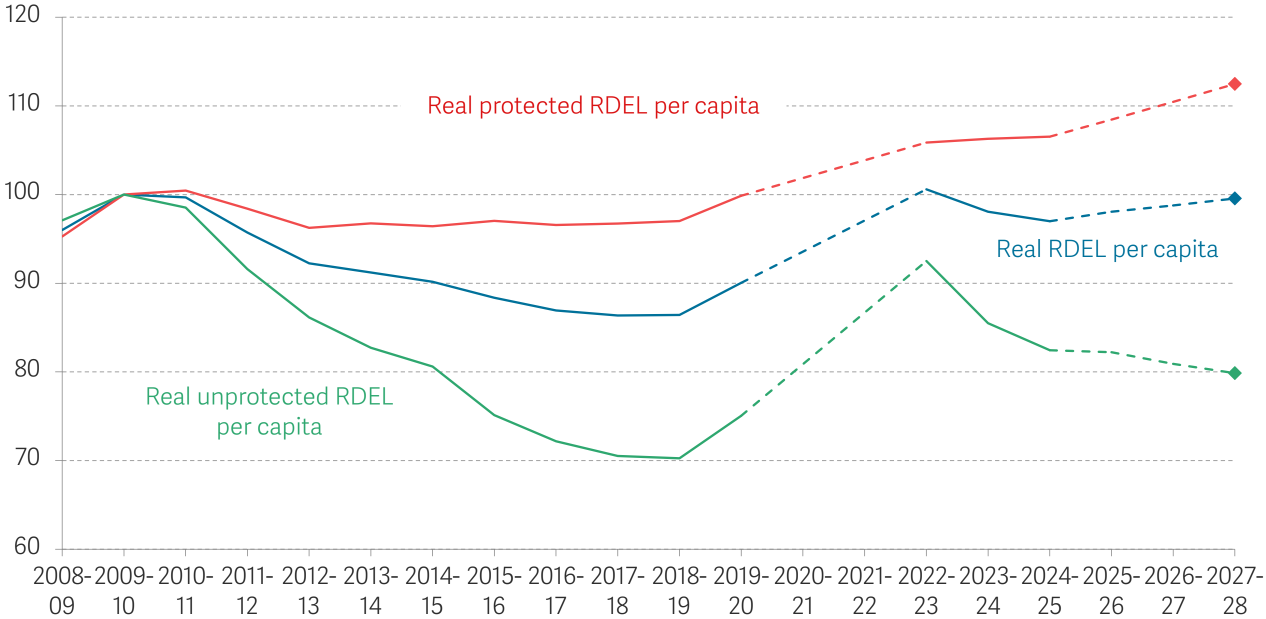
NOTES: Deflated to 2021-22 cash-terms using the GDP Deflator. Totals exclude DEL Covid spending and energy spending, adjustments are made to remove the impact of Business Rates Reliefs.
SOURCE: RF analysis of OBR, Economic and Fiscal Outlook, November 2022; and HMT, PESA tables and Autumn Statement 2022.

29 ODA was expected to be returned to 0.7 per cent of GNI in 2024-25 when the Government's fiscal rules were expected to be met. Given the deterioration the economic outlook and public finances these two conditions are no longer forecast to be the case at any point prior to 2027-28 (as the Government is no longer targeting a current balance), and, as a result, ODA is set to remain at 0.5 per cent of GNI freeing around £5 billion of spending per year.

The impact of these plans for actual public services, and the public finances, are highly contingent on the outlook for inflation and the manner in which it feeds into the prices of the inputs of government provided services. In particular, the OBR is predicting very low levels of inflation in the final three years of the forecast period, which allows real spending growth to be maintained with relatively modest nominal increases in PSCE of £30 billion between 2024-25 and 2027-28. If, instead, inflation were to return to 2 per cent in these final three years, then maintaining this 1 per cent real-terms increase in PSCE would cost over £40 billion.

FIGURE 30: **Current levels of spending would mark a return to the austerity period in unprotected departments**

Indices of real per capita departmental expenditure limited (2009-10=100), by 'protected' and 'unprotected' departments: UK, 2008-09 to 2027-28



NOTES: Protected departments include Department for Health and Social Care, Department for Education, Foreign Commonwealth and Development Office, and the Ministry of Defence. The health budget is assumed to grow at 3 per cent in real-terms per year; the foreign office budget and defence budget are assumed to grow to match commitments for aid to be 0.5 per cent of GNI and defence spending to be 2 per cent of GDP; the education budget is assumed to be kept flat in real terms. The lines between 2019-20 and 2022-23 are interpolated due to volatility in the GDP deflator.
SOURCE: RF analysis of OBR, Economic and Fiscal Outlook, November 2022; HMT, PESA Tables various and Autumn Statement 2022.

Importantly, given that the bulk of spending cuts are planned for beyond the end of the spending review period, the Chancellor has not provided any information on where they will fall. Figure 30 demonstrates that if the Department of Health and Social Care, Department of Education, Ministry of Defence and Foreign Office were as protected as they have been historically, then the planned spending cuts would lead to real per capita spending in unprotected departments falling to 2014-15 levels. This fall involves spending being cut by around 0.8 per cent a year in the final three years of the forecast.

It is not clear that such spending plans are deliverable. They would require an extended period of holding public sector wages down below those in the private sector, when the most recent data already shows public sector wages falling by over 6 per cent in real terms relative to 1.8 per cent in the private sector.[30] Given the need to clear Covid-related backlogs in many areas of public service provision, maintaining such a differential may prove too large to recruit and retain the necessary workforce. Recent history also provides many examples of tight spending assumptions being pencilled in, and then increased long before they become actual departmental spending plans.

Measures announced in the Autumn Statement provide some short-term support for living standards, but the outlook remains bleak

While the outlook for public spending remains highly uncertain, it is painfully certain that the immediate outlook for household living standards is dire. That comes despite government policy acting to soften the blow.

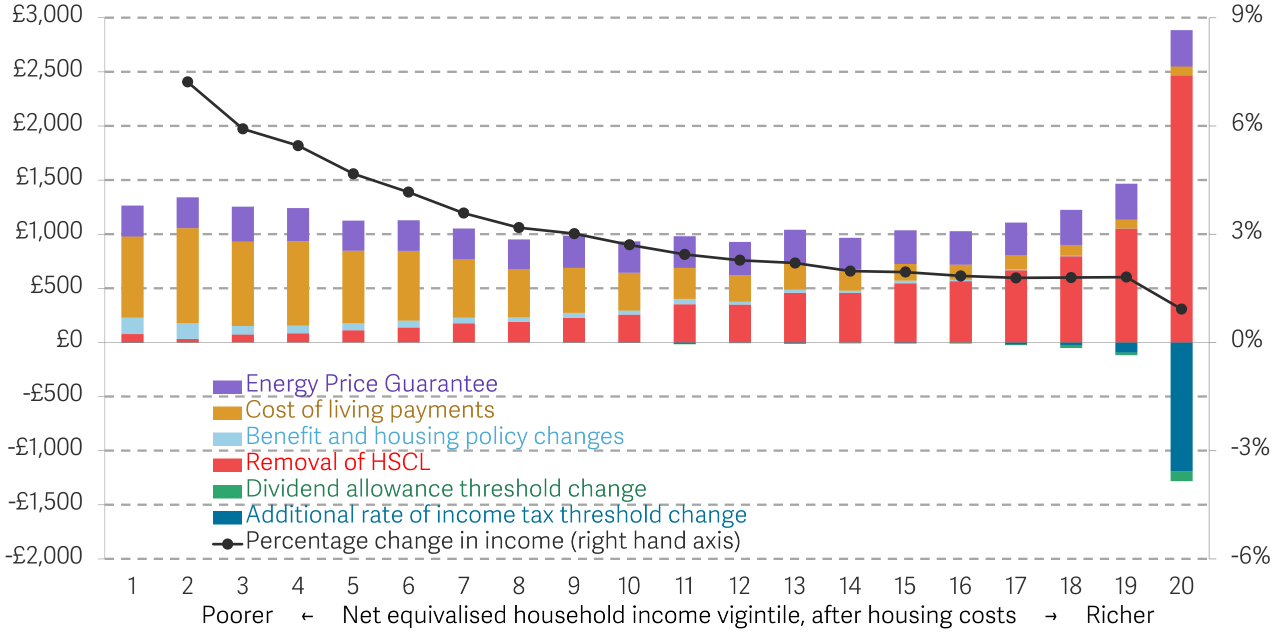
In Figure 31, we show the impact of changes to personal taxes and benefits, as well as the Energy Price Guarantee, that have been announced since March 2022 and that are in effect in 2023-24. In cash terms they provide most support to those on the lowest and highest incomes, with the top and bottom quintile both seeing average gains of £1,300. This is delivered principally by Cost of Living Payments to the bottom and the abolition of the Health and Social Care Levy at the top, partially offset by the reduction in the threshold for the additional rate of Income Tax to £125,140 (which costs the top 5 per cent an average of £1,190). The middle income, or typical, household receives less support: £950.

Importantly, there is no series in this chart corresponding to the very welcome announcement in the Autumn Statement that social security benefits will be uprated in April 2023 by CPI (discussed in Box 6) because this represents existing government policy.[31]

30 ONS, Labour market overview, UK: October 2022
31 The analysis in this section also excludes any changes in Council Tax as a result of the Government increasing the flexibility that councils in England have to raise their council tax bills without local referenda. The OBR expects this increased flexibility to result in the average B and D council tax bill to be £250 higher by 2027-28.

FIGURE 31: **Households across the income distribution have benefited equally from tax and benefit changes and energy policy announced this year**

Impact of policy changes announced since March 2022 on household incomes and reduced energy spending, by income vigintile: UK, 2023-24



NOTES: Income changes expressed in 2023-24 prices. Capital Gains Tax change not included in this chart due to its small impact. Cost of living payments refers to the £900 means-tested benefit payment, £300 pensioner payment, and £150 disability payment. Benefit and housing policy changes refers to CPI uprating of the benefit cap, social rent uprating of 7 per cent instead of 11.1 per cent, and CPI uprating of Pension Credit. Dividend allowance change reduces the threshold from £2,000 to £1,000 in 2023-24, and £500 in 2024-25. Additional rate of income tax threshold reduced from £150,000 to £125,140 in 2023-24.
SOURCE: RF analysis of DWP, Family Resources Survey using the IPPR tax-benefit model; DWP, Households Below Average Income; ONS, Living Costs and Food Survey.

BOX 6: **Changes to social security benefits in April 2023**

The Chancellor announced that most social security benefits will go up in April 2023 in line with September's rate of CPI inflation, which stood at 10.1 per cent. This increase represents the biggest percentage rise in the rates of key benefits since April 1991.[32]

Although increasing working-age benefits in line with inflation is the usual practice, and increasing the state pension in line with inflation is following the rules of the state pension triple lock, this is a significant, and very welcome, decision, coming after weeks of speculation that the Government would try to save money by choosing a different way forward. Had it, for example, decided to increase the value of working-age benefits in line with earnings instead, this would have amounted to a 4.2 per cent cut in real

32 DWP, Abstract of DWP benefit rate statistics 2021.

terms, and an average loss of £244 per household on UC.[33]

Indeed, the Chancellor was more generous than simply following the normal OBR assumption as he additionally announced that:

- the Pension Credit is to be uprated by CPI instead of average earnings next April (a cost of £700m in 2023-24);
- the Benefit Cap will be uprated by inflation in April (costing £315m), ensuring more people can benefit from the wider uprating;
- increases in social rents in April 2023 will be limited to 7 per cent instead of 11.1 per cent (a £135m saving for the exchequer through reduced spending on housing benefits, but a cost of greater magnitude to social landlords); and,
- the waiting period for Support for Mortgage Interest loans will be reduced to three months (at no cost in 2023-24).

Despite the discretionary support for household incomes next year, and confirmation that benefits will rise in line with prices, the immediate outlook for household incomes is truly dire. Figure 33 shows the OBR's projection for average Real Household Disposable Incomes (RHDI).[34] RHDI is set to fall by 7.1 per cent between 2021-22 and 2023-24, equivalent to a £1,700 fall per household: by far the largest fall on record.

Personal tax and benefit changes announced over this Parliament mean typical household incomes will be £1,100 lower by 2027-28

Looking to the longer term, and accounting for all announcements this Parliament as we do in Figure 32, policy decisions (in particular the freezing of personal tax thresholds) are deepening the squeeze for all but the poorest quarter of the population (one exception is the higher threshold for National Insurance contributions announced by Chancellor Sunak in May which has boosted incomes by £120).. The result is broadly progressive as households in the poorest income quintile (the bottom four vigintiles shown below) are not only affected in only small ways by the threshold freeze but also gain from the cut in the Universal Credit taper rate (from 63 to 55 per cent) and increases to the UC work allowances: together, these have boosted incomes in this quintile by £540 per year.

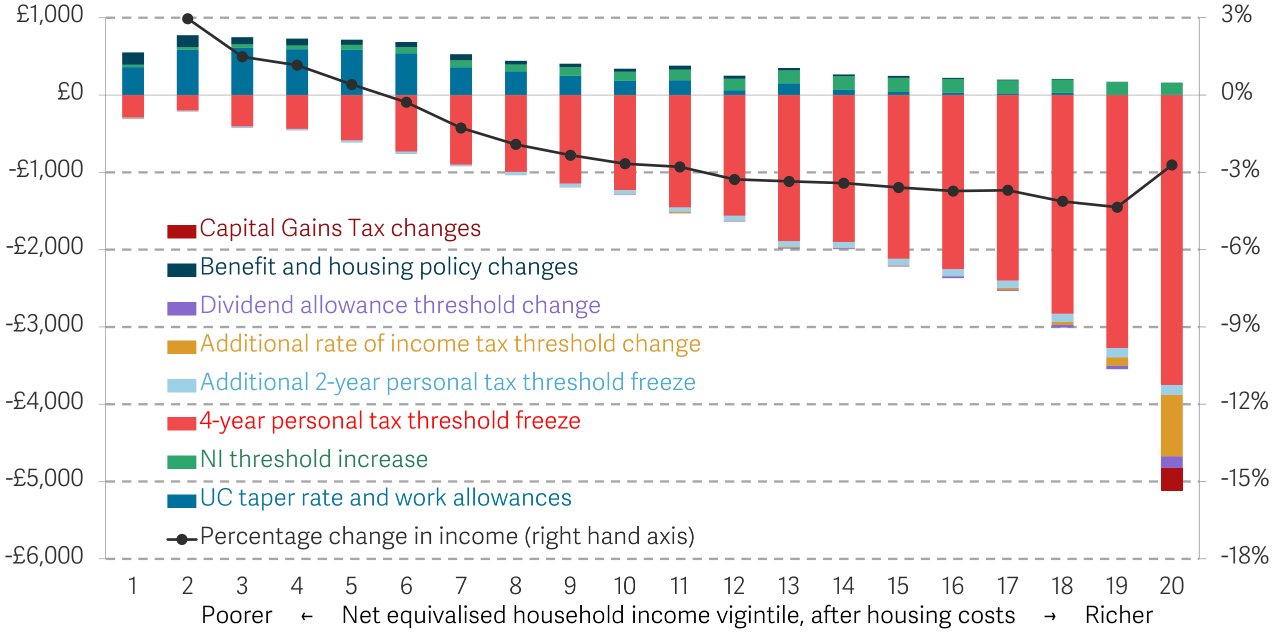
As a result of all these changes, the richest 10 per cent of households will be, on average, £4,200 worse-off in 2027-28. The middle quintile of households will be £1,100 worse-off, and the lowest-income quintile will be £350 better-off on average. These policy changes

33 Source: RF analysis of DWP, Family Resources Survey using IPPR tax-benefit model; DWP, Households Below Average Income.
34 We calculate our Real Household Disposable Income by converting the RHDI figures provided by the OBR and ONS from 2019 prices to 2022 prices, then dividing total RHDI by total population, and then annualising it.

mean an average income fall of 3.4 per cent for highest-income quintile, 2.8 per cent for the middle, and a 1.8 per cent rise for the poorest households.

FIGURE 32: **High-income households will be paying £4,200 more in personal taxes by 2027-28**

Impact of permanent tax and benefit changes announced this Parliament in 2027-28 by income vigintile, in 2023-24 prices: UK



NOTES: We assume Capital Gains Tax changes affect the top vigintile only. Benefit and housing policy changes refers to CPI uprating of the benefit cap, social rent uprating of 7 per cent instead of 11.1 per cent, and CPI uprating of Pension Credit. Additional rate of income tax threshold reduced from £150,000 to £125,140 in 2023-24. Additional 2-year Personal Tax threshold freeze includes all Income Tax and National insurance thresholds (excluding employer NI), and refers to 2026-27 and 2027-28. 4-year Personal Tax Threshold Freeze refers to Income Tax threshold freeze from 2022-23 to 2025-26, and National Insurance thresholds (excluding employer NI) from 2023-24 to 2025-26. National Insurance thresholds were brought in line with Income Tax thresholds in July 2022. The UC taper rate was reduced from 63 per cent to 55 per cent and work allowances were increased by £500 a year in December 2021.
SOURCE: RF analysis of DWP, Family Resources Survey using IPPR tax-benefit model; DWP, Households Below Average Income.

This leaves the outlook for living standards during the 2020s in a truly dreadful place. Real household disposable incomes are forecast to remain lower at the start of 2028 than they were before the pandemic hit in 2019.

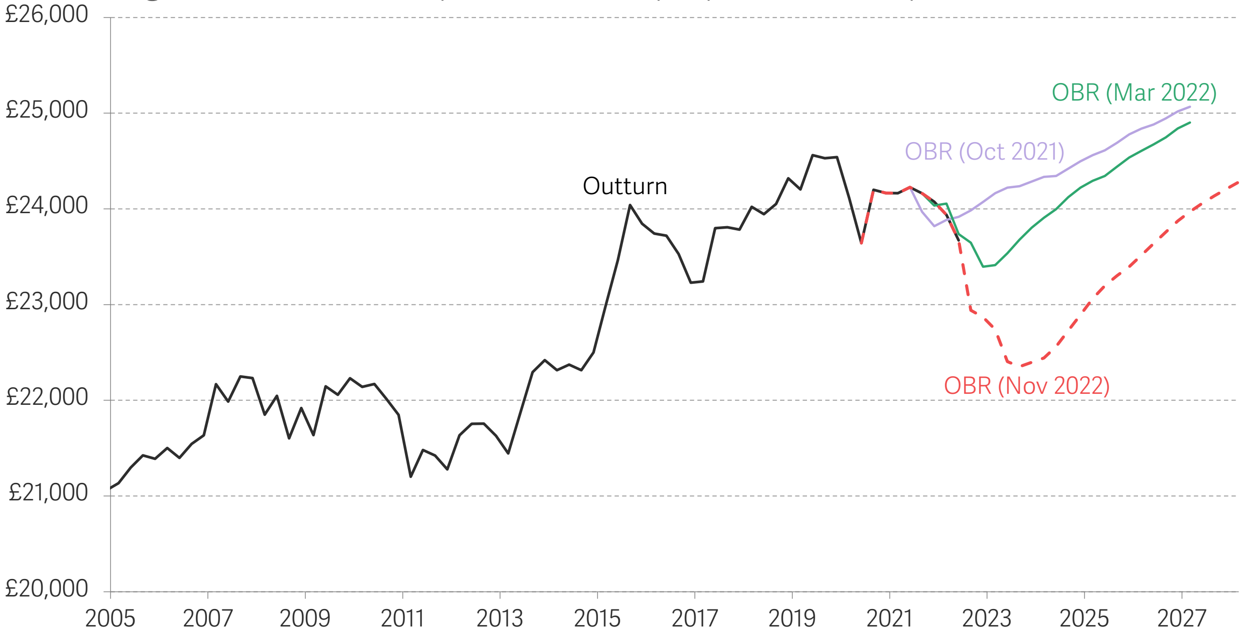
In addition, RHDI will remain below its Q4 2019 level (i.e. just before the pandemic) even by the end of the forecast period, meaning the average household is likely facing a decade of no income growth.

The outlook for household incomes is so dire, in part, because households are facing a time of record-low earnings growth: the OBR's new forecast for earnings shows real wages to be falling by more, and for longer, than was predicted in March. Inflation-adjusted pay won't return to 2008 levels until 2027 under yesterday's OBR forecasts, meaning workers are facing 19 years of no cumulative wage growth. Tax rises for people across the income distribution (as shown in Figure 32), also drag down on incomes, and the policies to help with energy bills in 2023-24 are less generous than their equivalents in 2022-23 (as shown in Figure 13).

Despite this awful outlook for household incomes, there are some factors which prevent incomes from falling by even more. The OBR estimates that the EPG and various cost of living payments boost the level of RHDI per person by 4.5 per cent in 2022-23 and 2.5 per cent in 2023-24.[35] And, in positive news for low-paid workers, the National Living Wage is set to rise from £9.50 to £10.42 next April: a 9.7 per cent increase, which will boost incomes at the lower end of the distribution.

FIGURE 33: **Household incomes are forecast to remain below 2019 levels for a decade**

Average Real Household Disposable Income per person, in 2022 prices: UK



NOTES: Includes non-profit institutions serving households (NPISH).
SOURCE: ONS; OBR, Economic and Fiscal Outlook, various.

Conclusion

Yesterday, Jeremy Hunt delivered an Autumn Statement that combined the 'tough choices' rhetoric of George Osborne and the policies of Gordon Brown. In the face of grim economic – and grimmer fiscal – forecasts, he announced energy support today but

35 OBR, Economic and Fiscal Outlook, November 2022.

tougher times tomorrow, with huge stealth tax rises for the middle and top followed by far less concrete spending cuts pencilled in for after the next election.

These decisions were made in the light of the fact that, as an energy importer during an energy price shock, Britain is getting poorer. Deciding exactly how that blow should be shared out between different households, as well as between current and future taxpayers was, to a significant extent, the task facing the Chancellor. He has decided that households will do so with higher energy bills, higher taxes, and worse public services than previously expected. Whether or not making the choices was tough, the reality of living through the next few years will be.

The Resolution Foundation is an independent research and policy organisation. Our goal is to improve the lives of people with low to middle incomes by delivering change in areas where they are currently disadvantaged.

We do this by undertaking research and analysis to understand the challenges facing people on a low to middle income, developing practical and effective policy proposals; and engaging with policy makers and stakeholders to influence decision-making and bring about change.

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