Resolution Foundation BRIEFING

Hitting the buffers

Previewing the key decisions for Autumn Budget 2026 in the context of another rise in the cost of living

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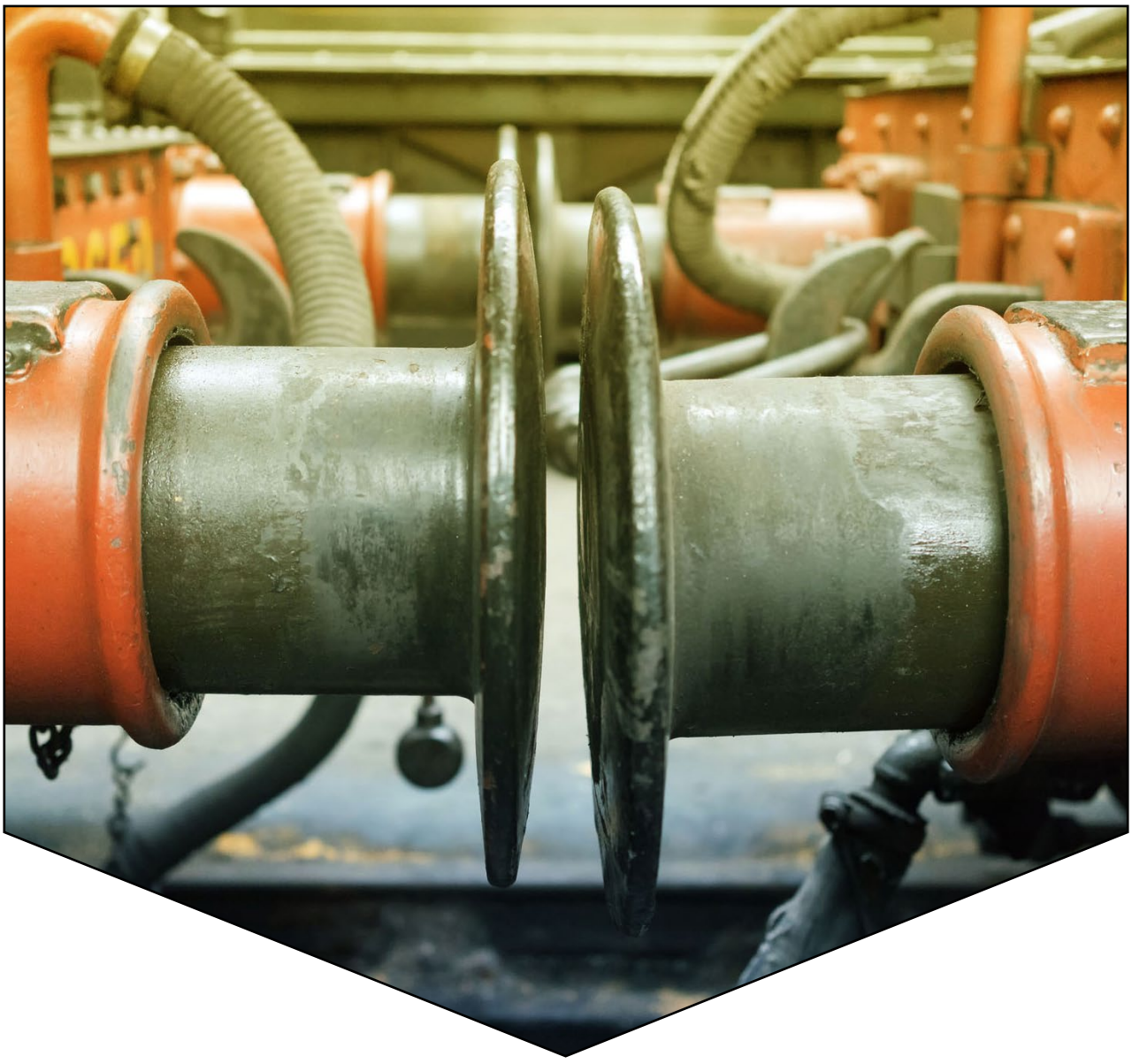

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Summary

As a new Chancellor settles into No.11, it's hard to shake the sense of yet another difficult Budget ahead. Yes, growth has beaten the forecasts made back in March. And the UK was the fastest growing of the world's G7 major economies over the first half of the year. John Healey's problem, though, is that conflict in the Middle East has once again pushed up energy prices and interest rates. So, despite the signs that the UK economy is becoming more resilient, household and public finances are in for another shock. In response, the Government appears to be playing for time, setting expectations for a small Budget, while potentially delaying tough decisions, such as how to fund defence, for next year's spending review. But there are two key challenges that cannot be ducked: how to support families through the latest jump in the cost of living; and how to stabilise the public finances.

In that context, the OBR's forecasts are not likely to make pleasant reading in the Treasury. The main culprit is the rising cost of government borrowing on global markets, from which the UK has certainly not been immune. We estimate that our debt-servicing costs, which were already volatile and uncomfortably high, will be around £14 billion higher by 2029-30 than was forecast back in March. Stronger economic growth is also unlikely to last. Weaker net migration will blow a further hole in the public finances, although this will be offset by higher inflation and higher asset prices pushing up tax revenues. Taking everything together, we estimate that the buffer against the binding fiscal target (i.e. bringing current spending into line with tax receipts by 2029-30) will be halved to £12 billion. Although there is great uncertainty about the exact numbers, the broad strokes of the fiscal picture – a significant deterioration, chiefly driven by rising debt-interest costs – seem clear.

Strapped families need focused help, not false hope

Against this troubling backdrop, the first challenge facing the Government is how to ease the pressure on families facing energy bills expected to rise to around £2,000 per year from January, a level close to the peak hit in the aftermath of Russia's invasion of Ukraine. Our work on the cost of living shows that the experience of 13 years of normal inflation in five has hit everyone's living standards, with the typical family £2,900 worse off than they would have been if the economy had behaved as was expected before the pandemic. But the rapid rise in the cost of life's essentials hits poorer families especially hard. So it is vulnerable households, like the almost one-in-five households in the poorest half of the country already behind on priority bills, who are most at risk during the tough winter ahead.

The Government cannot be indifferent to this, but nor can it ignore the fact that action here must be squared with the challenge of the public finances. There can be no repeating the 2022 approach of borrowing large sums to provide blanket support: that simply ramps up demand across the economy, piling pressure on the Bank of England to raise interest rates, which in turn feeds through into a higher cost of debt for the Government and families alike. Unfortunately, the starting point is one where inflation is already high, fiscal policy is loose, and financial markets are retreating from sovereign debt; these are exactly the circumstances in which it would be a mistake to answer higher energy costs with significant extra borrowing.

Wishful thinkers think they can spy a happier chain of events. They might imagine that blanket fiscal measures directly bring down inflation, and thereby reduce the upward pressure on interest rates. On that basis they might argue that there is less need to fund price-reducing subsidies as other interventions. We disagree. It is true that the Bank of England is more than usually attentive to current headline inflation, because of the risk of a continued wage-price spiral. But repeating the expensive, universal support of the recent past would pump more money into the economy when the Government is already close to doing too much of this. Moreover, if support is temporary, then it will simply put upward pressure on inflation when it is removed, pushing back the point at which inflation returns to target, and risking precisely the opposite effect to the one desired. Permanent measures wouldn't whipsaw inflation in the same way, but would only avoid doing so because permanently exacerbate our fiscal challenges. The grim upshot is that, with scope for more borrowing severely limited, immediate cost of living measures need to be both targeted and temporary.

Surgical strikes on the most dangerous deprivations

With public money tight, prioritising is crucial. Those families who will otherwise struggle to keep warm or retain a roof over their head must come first. With energy bills set to rise to around £2,000, the unlucky minority saddled with both low incomes and especially high fuel bills will be filled with trepidation about the winter ahead. Further help in the Budget must be directed towards the most exposed, not least because the first measure of relief arrived through the suspension of VAT on electricity bills, a giveaway that is thinly spread across all homes.

A tractable way to support struggling families is by applying a temporary discount to gas and electricity prices for households where no individual has an income above £24,000. Such a temporary scheme would cost £2 billion this year and could provide an average £175 per eligible household, with heavier energy users enjoying more relief. There are practical challenges with such a system which may mean this isn't deliverable by January. If so, then that is a sad indictement of the state's capacity to deliver (given

that this coming shock has been clear since March) and a further reminder that we must develop better systems in ordinary times to be ready to respond to shocks when they arrive. If things have been left too late to get this new form of targeting up and running, then the Government should increase the Warm Home Discount (which goes to means-tested benefit recipients) and provide a top up to the Crisis and Resilience Fund (which can reach low-income households not on benefits) for this winter, at the same time as acknowledging the limits of targeting support in this way, and turbocharging efforts to set up something better for the future.

The other non-negotiable is making sure that families can pay their rent. Support for private tenants on low incomes has been frozen over a period when rents have risen by more than 20 per cent. This burns an intolerable hole in the budgets of over 900,000 households receiving Universal Credit, with a family renting a typical two-bedroom home facing a shortfall of nearly £160 a month. Having made a very personal priority of tackling homelessness, Andy Burnham has to fix the broken link between the housing support available and the rents people actually face. Permanently relinking Local Housing Allowance to the 30th percentile of local rents would cost £2.3 billion by 2029-30. There are a range of ways to find that money, but if it were funded from within the existing working-age welfare budget, then one option is a slight increase in the Universal Credit taper rate from 55 per cent to 58 per cent (still low by historical standards).

The 'Your First Home' scheme trailed by the Prime Minister will lower the deposit barrier holding back many would-be homeowners, and ease cost of living pressures for beneficiaries by reducing their subsequent mortgage payments. But targeting the scheme at those currently unable to buy will be difficult, especially as the new scheme can be used only on new builds, which tend to cost more than their pre-existing equivalents. That restriction is good news for developers, but a 2.5 per cent deposit on a new-build property will still be more than what many reluctant renters can manage.

Ceding to demands to extend, yet again, the long freeze on Fuel Duty into next year is not the place to pour scarce resources. Instead, the aim should be to get Fuel Duty rising. 'Little and often' should be the mantra here, with small, predictable increases ending years of fiscal fictions.

How big a buffer, and how to build it?

Rachel Reeves used her Budget last year to increase the buffers – or headroom – against the fiscal rules, leaving a margin of £24 billion at the Spring Forecast. If, as we estimate, that figure has now been halved to £12 billion, the Chancellor must decide how to respond. Some argue that headroom should bear the brunt of the hit to the public finances: conflict in the Middle East is, hopefully, temporary, and such unexpected

events are exactly the sort of thing such a cushion is for. But the perfect storm of high inflation, already loose policy and jittery financial markets means there is a strong case for acting to repair the public finances. That doesn't necessarily mean getting all the way back to £24 billion, however. The fiscal rules focus on the future, and the point where they bite has recently moved forward a year, from four years ahead to three. Focusing less far into the future makes things a little less uncertain, reducing the buffer required. Consequently, on our calculations, £18 billion in headroom this Autumn can now reasonably be deemed equivalent to £24 billion back in the Spring.

Nonetheless, the case for prudence is heightened by the uncertainty around how future spending commitments will be financed, most obviously the potential rise in defence spending to 3 per cent of national income by the end of the decade. In this context, there is a case for providing investors with some reassurance that the Government has a grip on its broader finances. A credible interpretation of these risks to the fiscal framework would, in our view, involve aiming for headroom of at least £20 billion by 2029-30.

Choosing to prioritise the public finances by building such a buffer means there is simply less money for other things. In these circumstances, the key question for the Chancellor is the balance between lower spending and higher taxes. Living within existing spending plans in cash terms will be tough, and – in an inflationary environment – we should think of doing so as making a contribution to repairing the public finances. It looks very hard to do much more. The spending review due next year is currently set to land 'unprotected' departments with a difficult 2.2 per cent real-terms cut – or a disastrous 5.5 per cent reduction if we are also to push defence spending up to 3 per cent – in 2029-30. In this context, it seems unrealistic for the Chancellor to promise net departmental spending cuts at this fiscal event. There are those who would say the benefits bill should be the place to cut. After a bold move to depart from the state pension Triple Lock, there could be pressure on working-age benefits. But reforms here must be carefully designed (as we set out in forthcoming work) and there is no chance of credible reforms emerging in time for this Budget.

In such a constrained spending environment, some revenue raisers will be needed. After the savings achieved by sticking to existing cash expenditure plans, around £8 billion of tax rises will be needed to build a £20 billion buffer. There is scope to achieve this through measures which would also improve the efficiency of our tax system. Ending escape routes from Capital Gains Tax, specifically on death and on exit from the UK, could pull in £4 billion. Reducing the turnover threshold at which firms have to register for VAT would raise £2 billion, and charging National Insurance on partnership income another £2 billion. Further contributions could come from additional charges on banks, and reducing the £2 million threshold at which the new Council Tax surcharge (or 'mansion

tax') will begin to bite. If the Government wants to make further progress towards higher defence spending in this Parliament (as Healey thought necessary as defence secretary), however, it may still need to do more. It should consider effecting a 2p 'switch' by lowering employee National Insurance rates and raising Income Tax rates, a move which would shield working-age employees while raising £6 billion, including from unearned income and better-off pensioners. That may be controversial, but if major new expenditure is to be funded, then somebody is going to have to pay for it. Announcing such a move would go a long way to rebuilding confidence in our public finances.

The Budget must not duck the challenges we face right now

In the face of difficult fiscal reality, what is most needed is a Budget that faces up to our problems, rather than ducking them. The Chancellor should be realistic about the twin challenges posed by cost of living pressures and our stretched public finances. The right way to answer them both is through a three-part strategy. First, providing targeted support to the families facing the most acute hardship (while also keeping borrowing falling). Second, setting out tax rises which repair the public finances and improve the system. Finally, keeping a tight grip on spending. Expenditure control requires minimising 'unfunded' announcements, setting an envelope that can hold through next year's spending review, and launching a process for finding the savings needed to do so. If the Chancellor does all this, it would not be the small Budget that the Government seems to favour. Instead, it would be a Budget that plots a course for an economy that can be stronger and more resilient in a more volatile world.

The Budget will be a difficult one despite some positive signs on the economy

Despite a change of Prime Minister, it's hard to shake the sense of yet another challenging Budget ahead. For all the attention given to Andy Burnham's new approach and agenda, the outlook and challenges will seem very familiar. With conflict in the Middle East and volatile financial markets, the financial outlook at this Budget will be a difficult one despite signs of welcome economic resilience. But with major decisions on how to fund defence, social care and house building pushed back to next year's Spending Review, the aim appears to be to hold a low-key fiscal event with minimal policy. Yet a low-key Budget may not cut it, as John Healey must still find a way to balance the need to support families through the latest jump in the cost of living with the need to build confidence by repairing the damage to the public finances.[1] In this briefing note, we start by assessing what the economic backdrop might mean for the OBR's updated fiscal forecasts, before previewing the big choices facing the Chancellor.

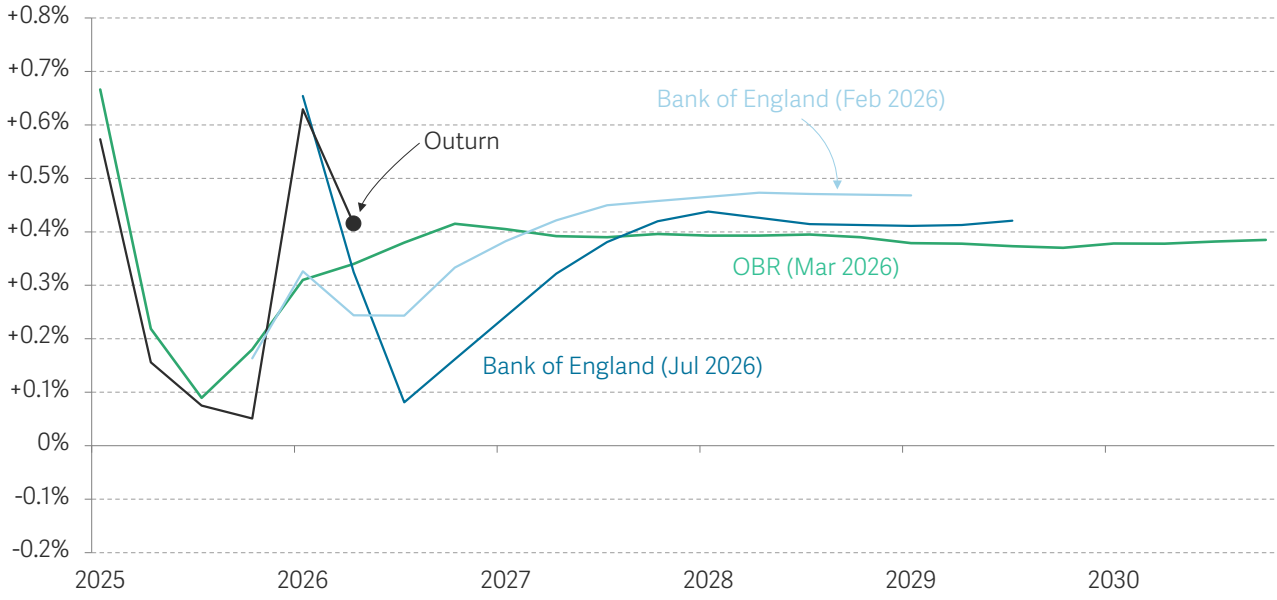
Growth has been stronger than expected so far this year, but conflict in the Middle East has worsened the short-term outlook

The Government has a good news story to tell about the resilience of the economy. Growth has been solid so far this year at 1.1 per cent in the first half of 2026, well above the 0.7 per cent forecast by the OBR in March.[2] This makes the UK the fastest growing economy in the G7 so far this year, and the OECD recently upgraded its forecast for the year as a whole from 0.9 per cent to 1.1 per cent.[3] We expect the energy shock to push growth below the OBR's March forecast in the near term, before growth picks up in the medium term as GDP recovers towards the level the OBR forecast in March (as the Bank of England's July forecast in Figure 1 illustrates).

1 M Brewer et al., Counting the cost: The impact of five years of high inflation on living standards, Resolution Foundation, October 2026, https://doi.org/10.63492/vxy3542.
2 GDP growth for Q2 2026 was originally estimated at 0.4 per cent in the August data release, which would have put total growth for H1 2026 at 1.0 per cent. In September this was revised up to 0.5 per cent (and 1.1 per cent for H1 2026) but this was likely too late for the OBR to incorporate into its forecast.
3 OECD, Economic Outlook, Interim Report, September 2026.

FIGURE 1: **Growth has outpaced forecasts in the first half of 2026**

Quarterly growth in real GDP, chained-volume measure, outturn, Bank of England and OBR forecasts: UK



NOTES: Bank of England forecasts are converted to smoothed quarterly averages after the first four quarters of data. Small revisions to GDP included in the Blue Book are not used in the outturn data as they came too late for the OBR to use in its forecast.
SOURCE: RF analysis of ONS, National Accounts; Bank of England, Monetary Policy Report, various; OBR, Economic and Fiscal Outlook, various.

Alongside this decent growth, unemployment has been lower than the pre-war forecast. It fell slightly from 5.0 per cent in February to 4.9 per cent in June, compared with the 5.3 per cent peak expected by the OBR this summer. Uncertainty remains around the quality of the Labour Force Survey, with response rates still below pre-pandemic levels, and with a specific data collection problem in May and June.[4] So, as the ONS has noted, it is better to look at the payroll and vacancies data it provides, which suggests the labour market has continued to loosen since the spring.[5]

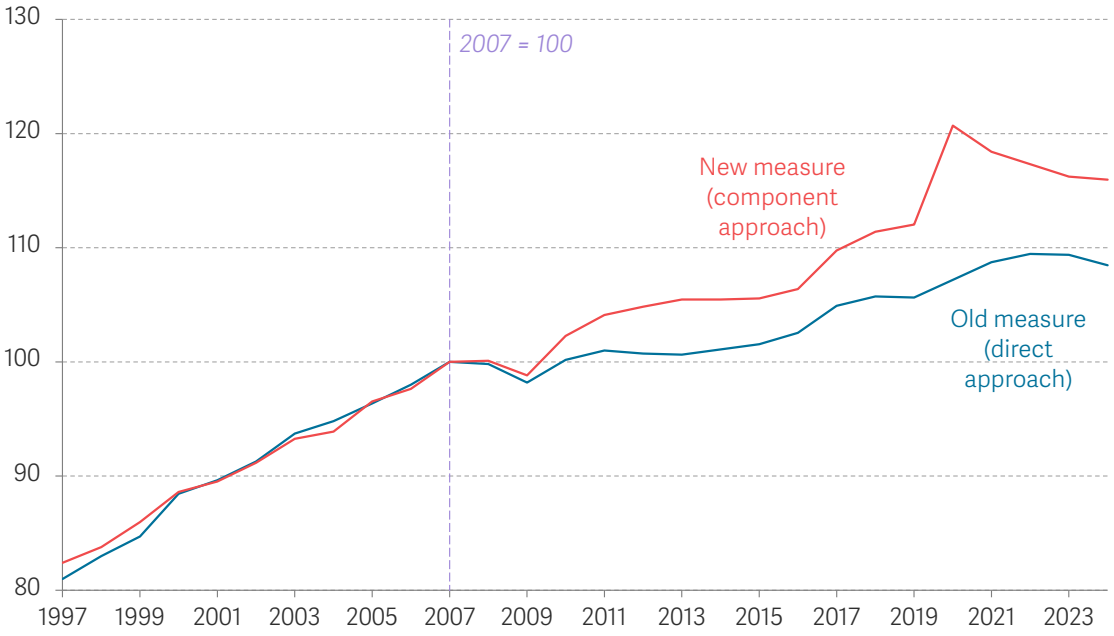
Looking past the short-term data, there are further grounds for optimism. Productivity growth – the rate at which workers become more efficient each year for each hour they work – is crucial to the OBR's longer-term GDP forecasts, and new ONS estimates paint a much brighter picture. The ONS's new 'component' approach to measuring hours corrects for the Labour Force Survey's apparent tendency to overstate them, implying that the same output has been produced with fewer hours worked. As Figure 2 shows, on these estimates, output per hour grew by 1.0 per cent a year between 2007 and 2019, double the previous estimate of 0.5 per cent. That takes the UK from the second-worst productivity growth in the G7 over this period to the second-best, behind only the

4 ONS, Labour Force Survey quality update, July 2026.
5 H Williams, 'Almost a million workers 'lost by unreliable official data, claims think tank', PA Media (via Express & Star), 20 November 2024.

US. International comparisons of productivity levels are largely unchanged, however: output per hour is still 10 per cent higher in France and 20 per cent higher in Germany than in the UK. But Britain's productivity slowdown between the financial crisis and the pandemic was less of an international outlier than previously thought.[6]

FIGURE 2: **A new measure of productivity has the UK performing much better than previously thought**

Indices of real output per hour, by approach to measuring hours worked (2007 = 100): UK



NOTES: Real output is the chained volume index of the whole economy GVA. It is consistent with the Blue Book 2026 and is the same for both measures.
SOURCE: ONS, Component approach to measuring labour productivity, UK: 1997 to 2024.

The OBR's assessment of 'trend' productivity is a key input to its forecasts for the public finances. The decision last year to downgrade its assumption for medium-term productivity growth from 1.3 per cent to 1.0 per cent a year pushed up borrowing by £16 billion in 2029-30, more than wiping out the £10 billion of headroom the Government had at the time.[7] On the ONS's new estimates, the OBR's assumption now sits below Britain's post-financial crisis average (1.3 per cent between 2009 and 2019).

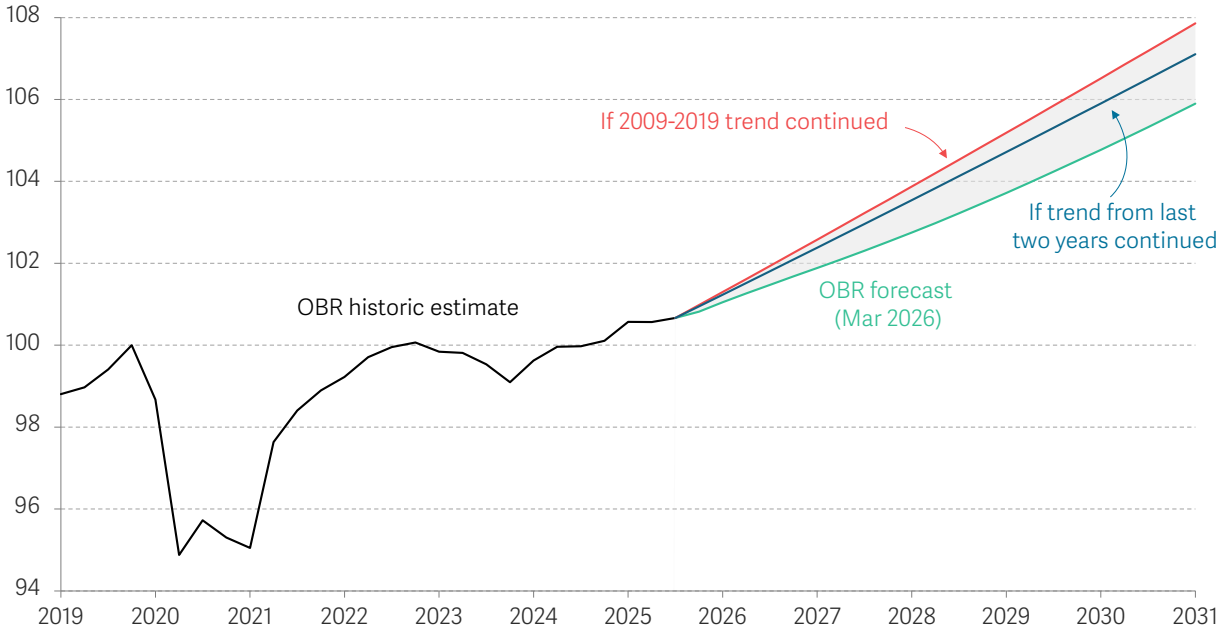
The most recent data tells a similar story. RF's admin-based measure, which avoids the Labour Force Survey's post-pandemic problems in counting workers, shows output per hour growing by 1.1 per cent a year in the two years to the second quarter of 2026,

6 S Pittaway & H Slaughter, Revision of labour: Unpacking the ONS's new estimates for productivity and hours worked, Resolution Foundation, September 2026, https://doi.org/10.63492/hfg9936.
7 H Aldridge et al., Stairway to headroom: Putting the Autumn Budget 2025 decisions on tax, spending and borrowing into context, Resolution Foundation, November 2025, https://doi.org/10.63492/gad912.

a sharp turnaround from an average fall of 0.7 per cent a year in the two years before.[8] As Figure 3 shows, if productivity were to keep growing at either its revised post-crisis rate or this recent rate, it would end the forecast period above the OBR's March 2026 path (which ramps up to 1.0 per cent a year by the end of the forecast). This might sound like good news for the public finances, but there are reasons to doubt a big shift in the coming forecast. First, the OBR is unlikely to have received this data in time to reflect it in its Budget forecast. Second, there's no guarantee it will shift its assumption based on this data. The OBR could see the new data as vindication for its previous optimism that the UK would recover from a period of especially low productivity, without choosing to double down on that optimism. Third, hours worked matter for the public finances too. If UK workers are more productive but also working fewer hours, the net effect on the public finances may be small.

FIGURE 3: **The OBR no longer looks optimistic about productivity growth relative to recent history**

Productivity level per hour (Q1 2019 = 100), actual and various counterfactual growth paths: UK



NOTES: The blue line estimates productivity growth using average hours and an admin-based employment estimate. For details, see A Corlett, Get Britain's Stats Working, Resolution Foundation, November 2024. The red line uses the new component approach released by the ONS.
SOURCE: RF analysis of OBR, Economic and Fiscal Outlook, March 2026; ONS, Component approach to measuring labour productivity, UK: 1997 to 2024.

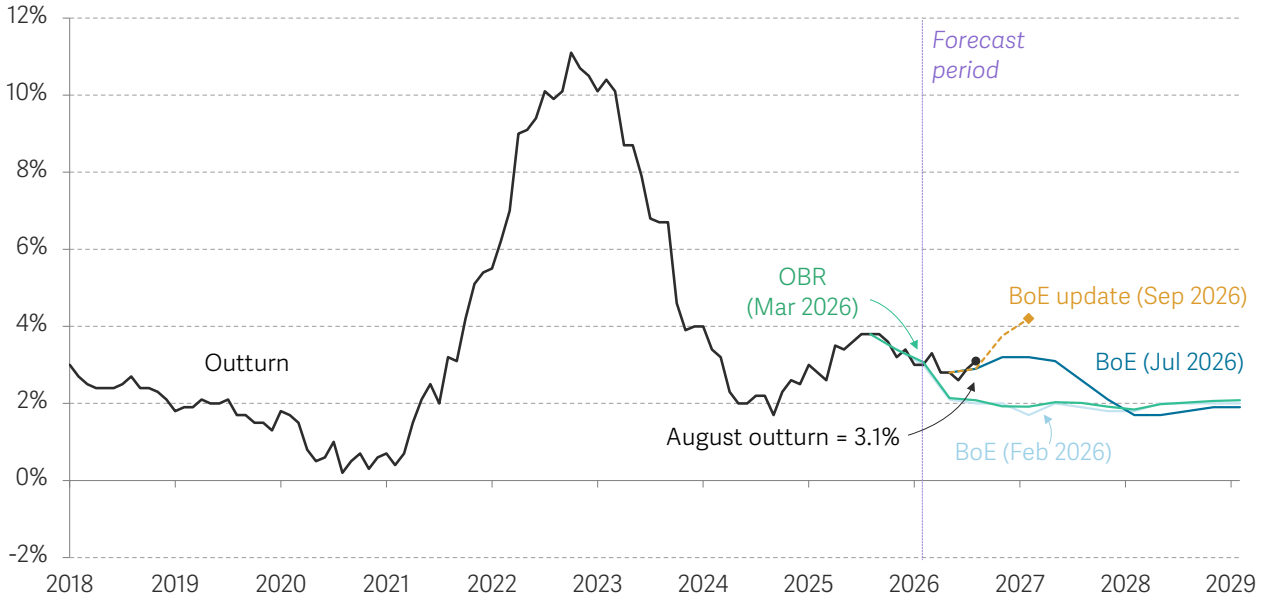
8 S Hunsaker & S Pittaway, The Macroeconomic Policy Outlook: Q3 2026, Resolution Foundation, August 2026, https://doi.org/10.63492/peqr754.

But conflict in the Middle East means the economic and fiscal outlook has deteriorated

Following the outbreak of hostilities in the Middle East, the inflation outlook is significantly worse. As shown in Figure 4, rising energy prices have pushed inflation above 3 per cent, rather than allowing it to return to the 2 per cent target. And the near-term outlook has continued to worsen: the Bank of England now projects a rise above 4 per cent early next year, having expected as recently as July that inflation would stay around its current level and then moderate. The one bright spot is that underlying domestic inflationary pressure, as measured by services inflation and private-sector wage growth, has eased slightly faster than expected in recent months; but this may not last as headline inflation rises further.

FIGURE 4: **Inflation has been higher than forecast, and is set to rise further**

Consumer price inflation, outturns and projections: UK



SOURCE: ONS, Consumer Price Inflation; OBR, Economic and Fiscal Outlook, March 2026; Bank of England, Monetary Policy Report, various.

The impact of higher inflation on living standards and interest rates will depend in large part on the labour market. Key to the Bank's decisions on interest rates (and in turn the fiscal forecasts) is how workers respond to higher inflation and how successfully they bargain for higher wages.[9] Following Russia's invasion of Ukraine, high inflation led to higher money wage growth than would otherwise have been the case. It is reasonable to think that money wage growth will also be somewhat higher as a result of the conflict

9 H Pill, Homophones, Remarks given at Edinburgh Chamber of Commerce roundtable, 3 September 2026.

in the Middle East, which would increase tax revenues in cash terms.[10] In the context of prospects for wage growth, Box 1 previews the decisions on the National Living Wage and youth minimum wage rates that will be taken at the Budget.

BOX 1: The Government is right to move more cautiously on youth minimum wages

New minimum wage rates for April 2027 may be announced at the Budget. Earlier this year, in the face of rising unemployment and a climbing NEET rate (young people not in employment, education or training), the Government decided to soften its approach to youth minimum wages. Previously, the Government's policy on youth minimum wages was bold: the rate for 18-20-year-olds was to converge on the adult rate. This led to large increases in the youth rates in 2025 (16.3 per cent) and 2026 (8.5 per cent) as the Low Pay Commission (LPC) sought to achieve convergence within this Parliament. Under the new remit, the Government has clarified that it's up to the LPC to determine the pace of convergence, and has additionally asked that "priority [be] given to the employment prospects of younger workers".[11]

The Government was right to soften its stance. That's not because there is strong evidence that minimum wage changes caused rising youth and adult unemployment over the past two years. A recent study compared youth employment trends across areas and sectors differently exposed to minimum wage changes and could not identify any impacts. But the study's estimates came with enough uncertainty that meaningful negative effects could not be ruled out.[12] Caution is the right approach when policy effects are uncertain and the labour market is weak, and particularly so when young people are faring badly (the NEET rate is not just high, but higher than we would expect given the level of adult unemployment).[13]

The remit for the adult minimum wage is largely unchanged, so the rate is likely to rise in line with expected median wage growth as in recent years. This again is a reasonable approach in the current labour market context.

10 M Brewer et al., Counting the cost: The impact of five years of high inflation on living standards, Resolution Foundation, October 2026, https://doi.org/10.63492/vxy3542.
11 Department for Business and Trade, Low Pay Commission Remit 2026: National Living Wage and National Minimum Wage, March 2026.
12 J Michael et al, Why has the NEET rate risen? Understanding trends and drivers using administrative data, IFS, May 2026.
13 L Judge et al, Lost in transition: An examination of why the UK NEET rate is high and rising, Resolution Foundation, April 2026.

Higher energy prices affect domestic prices and wages and thus the public finances. The direct impact shows up quickly in the price of fuel and energy bills. This then bleeds into the cost of producing goods and services, pushing up a broader range of prices. Finally, prices may rise further as workers and firms protect their purchasing power in the face of these higher prices. Higher inflation raises public spending on things linked to overall prices, such as benefit payments and index-linked debt. But the impact on receipts is ambiguous: higher prices and wages increase some tax revenues (for example, VAT and Income Tax); but the effect of further rises in energy prices is to provide a headwind to growth as families and firms spend more on energy and less on everything else. That weighs on employment and output, which reduces tax receipts. Departmental spending is fixed in nominal terms, so it is worth less in real terms as prices rise.

Lower net migration will reduce the fiscal room for manoeuvre

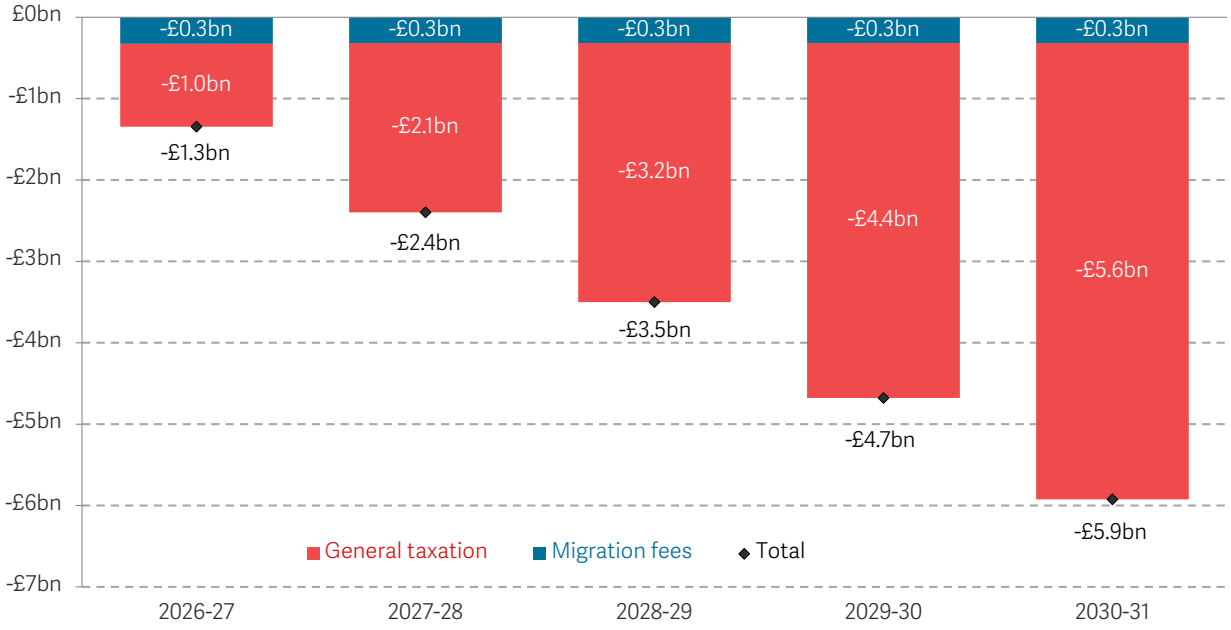
Net migration has been lower than expected and this will hit the public finance forecasts. The latest ONS data, published this month, estimates that net migration in the year to mid-2025 was 223,000, down from 652,000 the year before, while its long-run projection has fallen from 340,000 to 230,000 a year.[14] The OBR anticipated some of this fall at the Spring Forecast, when it cut its own long-run estimate to 290,000, but it is now likely to cut it further.[15]

On average, migrants make a net fiscal contribution to the Exchequer (particularly in the short to medium term), through both specific fees and charges and general taxation. So lower net migration is expected to weaken the Government's fiscal position further.[16] The OBR does not always follow the ONS population projections, but it typically adopts the ONS's long-run net migration estimate by the final year of its forecast, which would mean 230,000 annually from 2031 onwards.[17] If net migration were similarly reduced in each preceding year of the forecast (a cumulative reduction of 300,000 over five years), we estimate that this would correspond to a shortfall in receipts of £4.7 billion in 2029-30 relative to the Spring Forecast. On the other hand, a lower population will mean that fixed public expenditure plans stretch a bit further in per-person terms.

14 ONS, Population estimates for the UK, October 2026; National Population Projections, April 2026.
15 E Christensen & C McCurdy, The UK's demographic squeeze, Resolution Foundation, April 2026.
16 OBR, Economic and Fiscal Outlook, March 2024.
17 N Ridpath, L Rizzotti & M Warner, Migration and the public finance forecast, Institute for Fiscal Studies, September 2026.

FIGURE 5: **Lower net migration is also set to hit fiscal headroom**

Shortfall in receipts relative to Spring Forecast due to estimated lower net migration: UK



NOTES: These calculations assume a reduction in net migration of 60,000 over each year of the forecast. The receipts shortfall is assumed to accrue in the financial year that each population projection year ends, i.e., a net migration shortfall for the year ending mid-2026 corresponds to financial year 2026-27. The net fiscal impact of migrants is estimated from Box 4.5 in the OBR's Economic and Fiscal Outlook, March 2024.
SOURCE: RF analysis of OBR, Economic and Fiscal Outlook, various.

Higher borrowing costs mean headroom will be significantly lower than at the Spring Forecast

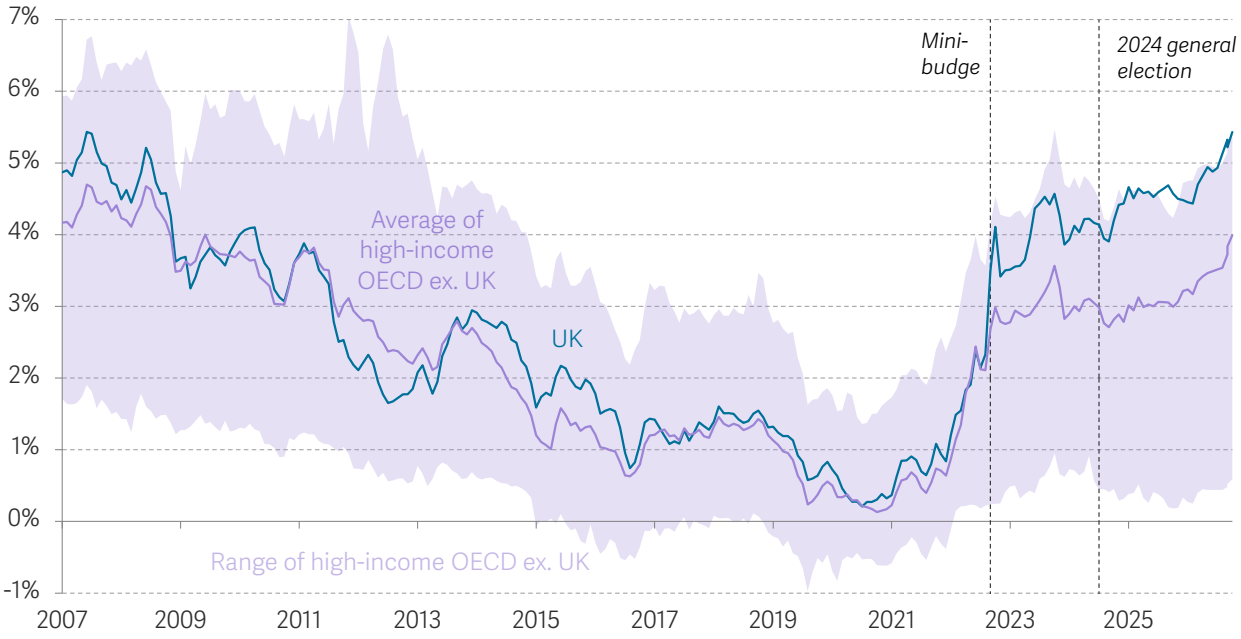
Conflict in the Middle East has also significantly raised the cost of servicing government debts. The combination of higher-than-expected inflation driven by the conflict, and broader concerns about government borrowing worldwide, have prompted further rises in sovereign bond yields globally. As shown in Figure 6, 10-year UK government bond yields are the highest among rich countries. That said, since the start of the war in Iran, yields have risen less for the UK than for others, including France, Italy and the US.[18] The extent to which higher yields feed into higher borrowing is uncertain, not least because we don't know exactly what period the OBR will use as the basis for its forecast, but our best guess is that it will use a 10-day window to 18 September. During that period, 10-year yields averaged 5.3 per cent, around 0.8 percentage points above the average in the window used for the Spring Forecast, but they have risen further since then. Expectations for short-term interest rates set by the Bank of England, which also affect gilt yields, have risen by even more and are around 1 percentage point higher on average over the next five years than they were at the time of the Spring Forecast. As explained in Box 2, the

18 This stands in contrast to the UK's previous recent experience, where yields have been especially sensitive to global news, including in the period immediately after the Iran war started. For more, see: S Pittaway, J Smith & G Thwaites, The Macroeconomic Policy Outlook: Q2 2026, April 2026, https://doi.org/10.63492/vbq6423.

Bank of England's (welcome) announcement in September that provided concrete plans to sell its remaining stock of UK government debt held for monetary policy purposes by 2034, in a way that should reduce the market impact, will we estimate add around £2 billion to borrowing in 2029-30 reflecting a slower rate of sales than assumed by the OBR in March.

FIGURE 6: **Global rises in borrowing costs have also affected the UK**

10-year government bond yields: high-income OECD countries



NOTES: High-income OECD countries are Australia, Austria, Belgium, Canada, Denmark, Finland, France, Germany, Italy, Japan, Korea, Netherlands, New Zealand, Norway, Spain, Sweden, Switzerland, and the United States.
SOURCE: RF analysis of OECD, Long-term interest rates; Bank of England, Yield Curves.

BOX 2: **The impact of the Bank's announcement on the unwinding of QE on borrowing**

During the financial crisis and the pandemic, the Bank of England undertook quantitative easing (QE), buying government debt (gilts) in order to reduce longer-term interest rates once short-term interest rates had gone as low as they can go. Since then, the Bank has started to unwind these purchases, selling its holdings back to the market. The debt held by the Bank of England represents an ongoing cost to the public sector now that the rate paid on central bank reserves (Bank Rate) exceeds the fixed rates paid on the gilts held. In essence, we have

refinanced some of our national debt at Bank Rate, rather than paying gilt rates.

In September, the Bank of England announced that it would wind down its holdings in the coming years, selling around £20 billion of gilts each year and allowing others to mature.[19] Although this implied a slightly faster rate of sales than expected by the market (see Figure 7), it was slower than incorporated into the OBR's March forecasts which assumed the Bank would undertake active sales of £32 billion each year.

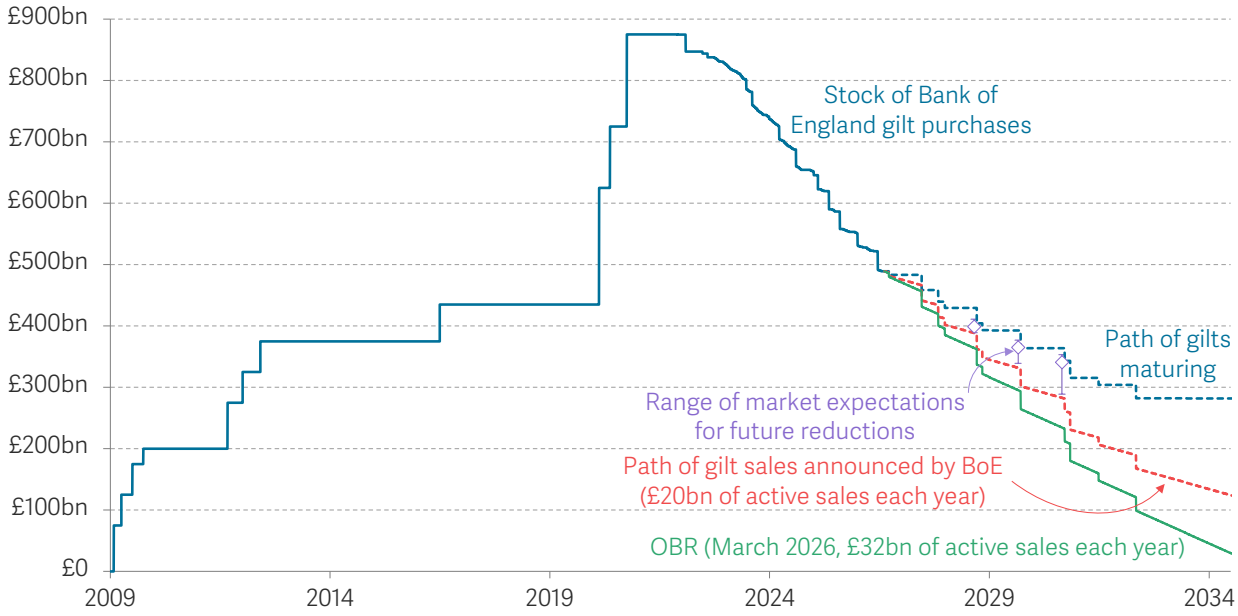
The new sales path has two effects on the public finances. First, sales themselves add to the supply of gilts to the market and so push up yields. Thus a slower pace of sales should reduce yields reducing debt interest costs and borrowing. The announcement included welcome specific new arrangements for the Bank to delegate sales to the Debt Management Office (DMO) which supported a fall in yields immediately upon announcement. Yields are usually taken by the OBR from the market and we assume they do not model a specific effect here, given uncertainty, despite the announcement coming at the very end of what we expect was their market window.

Second, the pace of sales determines the stock of national debt that is effectively refinanced at Bank Rate. A slower sales path means that is now expected to be higher than thought back in March over the forecast period. Given Bank Rate is above the effective gilt rate (and is expected to rise further above based on market pricing), this mechanically increases the cost of servicing our debts and pushes up on borrowing in the short term. We estimate that the path of slower gilt sales adds around £2 billion to borrowing in 2029-30 based on current market pricing.[20]

19 Bank of England, Monetary Policy Summary and Minutes – September 2026.
20 There was a fall of around 0.1 percentage points in 10-year gilt yields in the aftermath of the Bank's announcement on 17 September, with larger falls at longer horizons. As our headroom calculation is based on asset prices in a 10-day window to 18 September that fall is captured in our calculations but only receives a small weight, meaning that the impact on borrowing is larger than if we used the change in yields on that day.

FIGURE 7: **The announced path for fully unwinding QE means that the stock of gilts held by the Bank of England is higher than expected by the OBR**

Stock of Bank of England gilt purchases: UK

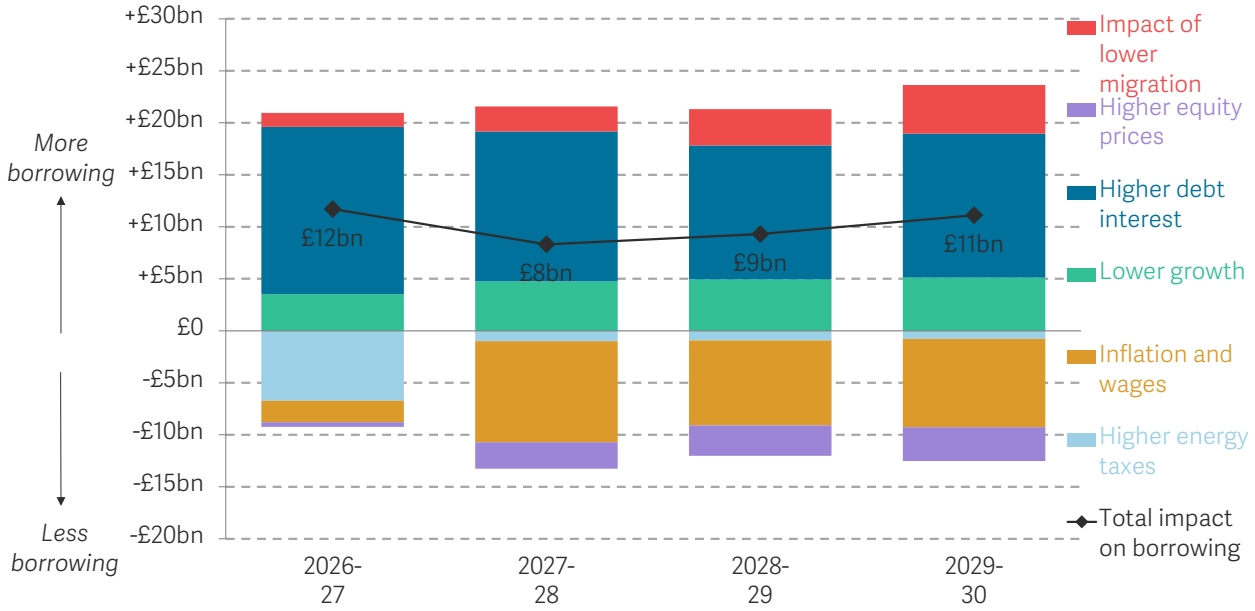


NOTES: Market expectations are taken from the Bank of England's September Market Participants Survey. Diamonds are median expectations, and the error bars reflect the range of expectations from the 25th to 75th percentile.
SOURCE: OBR, Economic and Fiscal Outlook, March 2026; and Bank of England, Asset Purchase Facility Quarterly Reports, Results and usage data & Market Participants Survey results.

Bringing that together with the impact of broader economic developments, we estimate that borrowing will be around £11 billion higher in 2029-30 than at the time of the Spring Forecast. Our estimates are shown in Figure 8. Debt interest costs are by far the biggest single factor pushing up on borrowing (by around £14 billion). As discussed above, while GDP has surprised to the upside early this year, this is not expected to last, with growth somewhat weaker in the near term given the impact of higher energy prices. Higher inflation will also push up on tax revenues, however, as we assume that workers are somewhat successful in bargaining for higher money wages. Welfare spending is also higher as a result of higher inflation, in line with the usual uprating of benefits. Overall, the effects of weaker growth and higher inflation essentially offset each other, with a small downward contribution to borrowing in 2029-30. As discussed above, lower net migration pushes up on borrowing by around £5 billion by 2029-30, but higher equity and energy prices together reduce borrowing by around £4 billion in 2029-30. So summing together everything other than higher interest rates nets out to a £2 billion improvement.

FIGURE 8: **We estimate that 'pre-measures' headroom has been halved since the Spring Forecast to £12 billion**

Estimated changes to the OBR forecast for public sector net borrowing since the Spring Forecast: UK



NOTES: Chart shows the impact on borrowing of changes in asset prices in the 10 days to 18 September combined with estimates of the impact of changes to the economy outlook. Excludes policy announcements since the Spring Forecast.
SOURCE: RF analysis of OBR, Economic and Fiscal Outlook, various; and Bank of England, Monetary Policy Report, July 2026.

The Government has a fiscal target of bringing day-to-day spending into line with tax receipts in 2029-30. In March, there was headroom of around £24 billion against that rule, and our estimates imply this 'pre-measures' headroom has fallen to around £12 billion.[21] But there is substantial uncertainty around this estimate. For example, if the OBR uses more recent data for debt-interest costs, borrowing will be higher due to recent increases in yields. And, as discussed in previous work, the OBR's forecast for wage growth remains noticeably weaker than the Bank of England's with only small increases in that forecast having a large effect on borrowing.[22] Given that data on tax receipts and public-sector borrowing has been broadly in line with the forecast since March, we have not factored in any changes to the forecasts for individual taxes or spending beyond those driven by the wider economy, though there may be particular risks around forecasts for revenues from Capital Gains Tax (CGT). A record amount of capital gains were recorded in 2024-25, in part reflecting gains brought forward ahead of Autumn Budget 2024.[23] If the OBR now judges that more of this surge was forestalling

21 Note that totals may not sum due to rounding.
22 H Aldridge et al., Stairway to headroom: Putting the Autumn Budget 2025 decisions on tax, spending and borrowing into context, Resolution Foundation, November 2025, https://doi.org/10.63492/gad912.
23 HMRC, Capital Gains Tax statistics, August 2026.

than assumed in March, it would lower the base from which future liabilities are projected, reducing the CGT forecast in later years.[24]

Despite the uncertainties, the broad contours of changes in the outlook are clear: a large rise in borrowing costs means that the fiscal outlook has deteriorated significantly. So, as the Government contemplates new measures for the Budget, the room for manoeuvre is limited and a key priority should be taking steps to repair the public finances, reducing the risk of further destabilising financial-market volatility. As we turn to next, this means facing two big challenges: how best to support families struggling with the cost of living in the near term, and how much of the deterioration in borrowing to attempt to restore in the medium term. We discuss these below.

Key challenge one: support for families struggling with the cost of living should be targeted and consistent with borrowing falling

Pressures on families have been building for six years and war in the Middle East means they are set to intensify once again

Our recent work on the cost of living crisis analysed the triple-whammy effect of post-pandemic supply chain inflation, Russia's invasion of Ukraine, and now the ongoing energy shock in the Middle East.[25] These successive crises have meant that the UK has experienced the equivalent of 13 years' worth of 'normal inflation' in just five, leaving prices nearly 30 per cent higher than their July 2021 levels and reducing real non-pensioner incomes by £2,900 compared with pre-pandemic forecasts. The impact of this huge hit to living standards has not been shared equally, however, as lower-income households have been hit hardest by the rise in the cost of essentials which takes up a larger share of spending by poorer families. By mid-2026, costs had risen by one sixth more for those in the bottom tenth of the income distribution than in the top. The effect of such a bottom-heavy increase in inflation, combined with the inability to call on other margins of adjustment, has been for hardship to be concentrated among poorer families. For example, an extra 1.7 million households were unable to keep their homes adequately warm in 2022-23 compared with 2021-22, of which 950,000 were among the poorest 40 per cent of families. And almost one-in-five households in the poorest half of the country is already behind on at least one priority bill.[26]

The response to these inflation shocks has almost entirely been poorly targeted and very expensive. The Energy Price Guarantee introduced by Liz Truss capped the rise in bills

24 A King, It seems there'll be no shortage of multi-billion-pound headaches for the new Chancellor, LinkedIn post, accessed 11 October 2026.
25 M Brewer et al., Counting the cost: The impact of five years of high inflation on living standards, Resolution Foundation, October 2026, https://doi.org/10.63492/vxy3542.
26 M Brewer et al., Counting the cost: The impact of five years of high inflation on living standards, Resolution Foundation, October 2026, https://doi.org/10.63492/vxy3542.

at £2,500 for everyone, but with no effort to claw back support from better-off families and an eye-watering price tag of £24 billion. Rishi Sunak's Cost of Living Payments were targeted at those on means-tested benefits (£11 billion). More recent interventions have returned to the theme of universal support, albeit on a smaller scale. These have taken the form of Keir Starmer's removal of some policy costs from energy bills and Andy Burnham's move to a zero rate of VAT on electricity bills. Rich households use more electricity, so 25 per cent of the VAT cuts go to the richest fifth of British households, compared to 16 per cent going to the poorest. With the Government's finances stretched, it is important that this costly and untargeted approach to intervention is not repeated.

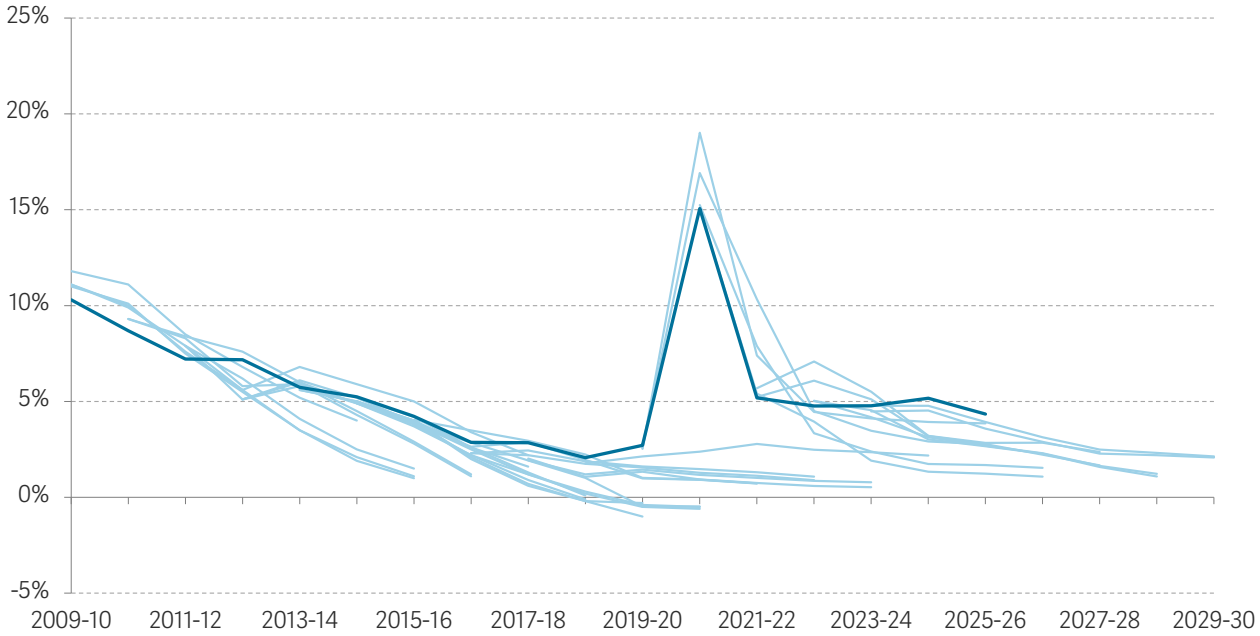
The Government should provide targeted support in a way that is consistent with continuing to bring down borrowing

The Government is caught between pressure to spend money to support households, and pressure to limit increases in borrowing and therefore further rises in interest rates. So a key question, then, is how much extra borrowing to do in the near term in order to provide that support. Here, we judge that the Government should strike a compromise to ensure that borrowing continues to fall in the current financial year compared with the last one.[27] With borrowing forecast to fall by roughly £17 billion in 2026-27 at the time of the Spring Forecast; and given our estimate of a nearly £12 billion increase in borrowing in that year, the Government does not have a lot of room for manoeuvre. Any increase in borrowing would partially reverse the progress made last year, when the deficit fell by nearly 1 per cent of GDP. Prioritising the delivery of lower borrowing in the current financial year would be a significant achievement and would signal commitment to repairing public finances tangibly today, rather than putting off adjustment to the future. Indeed, a key feature of recent years has been continued over-promising and under-delivering on deficit reduction. This is shown in Figure 9 which compares outturns for borrowing to forecasts made by the OBR since its inception. It is important to keep in mind that this period has contained some significant economic shocks, but the pattern of repeated disappointment in getting borrowing down is clear.

27 R Curtice & J Smith, Crowd-pleasing cost of living measures risk being self-defeating, Resolution Foundation, September 2026.

FIGURE 9: **Successive governments have promised far more fiscal consolidation than has been delivered**

Public sector net borrowing, forecasts and outturns, proportion of GDP: UK



SOURCE: OBR, Historical forecast database.

Repeating the 2022 approach of borrowing large sums to provide blanket support simply fans the flames of higher interest rates by increasing demand, piling pressure on the Bank of England to raise rates, which in turn feed through into a higher cost of debt for the Government and families alike. The reality is that a jump in energy prices when inflation is already high, fiscal policy is loose, and financial markets are retreating from sovereign debt, are exactly the circumstances in which significant extra borrowing should be avoided.

There are those who would argue that now is the time for more large-scale universal support that also acts to bring down inflation in the hope that this will reduce pressure on interest rates, making it easier to fund. What such arguments miss is that, even if the Bank of England is unusually focused on headline inflation right now given the risk of a wage-price spiral emerging, such a policy would still pump more money into the economy when the Government is close to doing too much of this already. Indeed, as discussed in Box 3, the stance of fiscal policy was close to its long-run average in 2026-27 based on the OBR's forecast in March. That means a large expansion in borrowing to pay for blanket energy support would exacerbate inflationary pressures and put more upward pressure on interest rates. Moreover, while it's true that direct measures to reduce prices would lower headline inflation in the very short run, any effect this might have in limiting wage demands and hence broader inflationary pressure would be small and overwhelmed by the whipsaw effect when the support is withdrawn, pushing up inflation at the crucial

one-to-two-year horizon that the MPC focuses on when making interest-rate decisions. This means temporary energy-price measures could easily backfire and end up putting more upward pressure on interest rates – a double whammy for the public finances once their cost is factored in. Permanent support would not whipsaw prices but, without tax rises to pay for it, would put even more upward pressure on rates (the Treasury has previously estimated that additional borrowing of 1 per cent of GDP – around £30 billion – can increase rates in the short-term by 50 to 125bps).[28]

BOX 3: Higher borrowing at the Autumn Budget would leave fiscal policy loose by historical standards

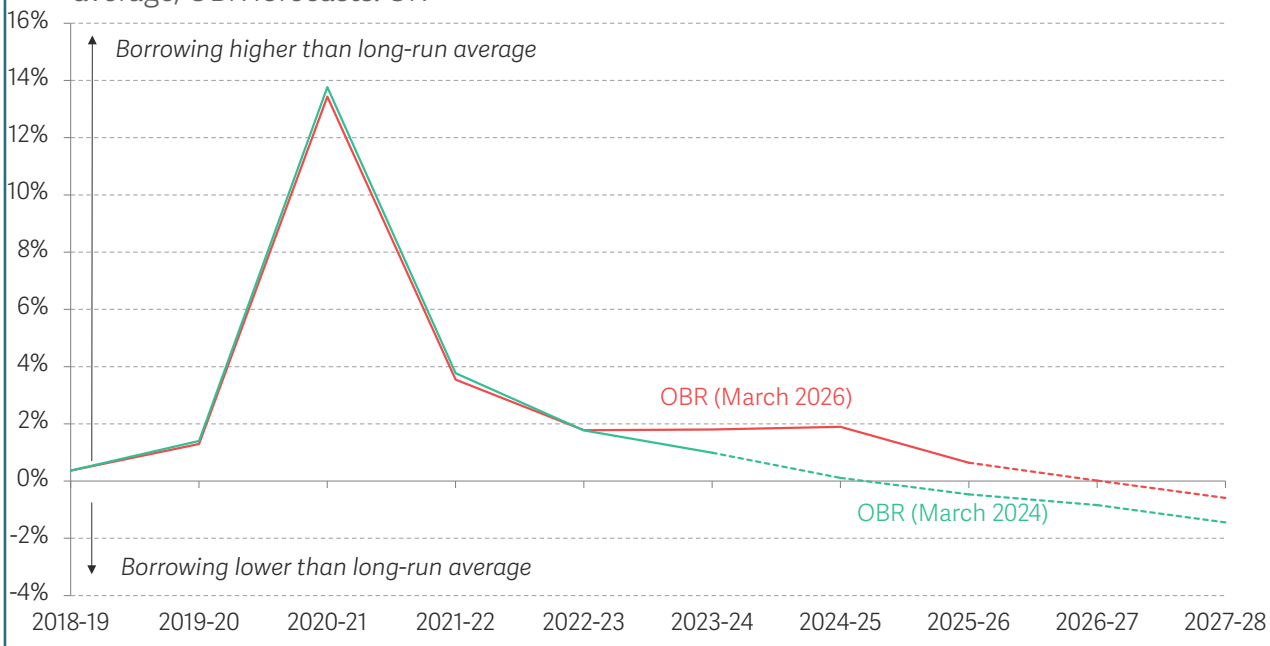
The standard approach to thinking about fiscal policy and the economic cycle is that it should be 'loose' – that is, spending a bit higher than normal and/or taxes a bit lower – when the economy is in a downturn; and 'tight' – spending lower and/or taxes higher – when the economy is in a boom. Decisions on the exact stance of fiscal policy should also depend on what rate setters at the Bank of England are doing, but the basic idea that fiscal policy should lean against the economic cycle should be a guiding principle for the Chancellor.

This basic approach is complicated by energy shocks which add to inflationary pressure but also slow the real economy. At such times, fiscal policy is likely to be in tension with monetary policy as governments looks to support families facing hardship and policy rates rise to curb inflationary pressures. The key to a good outcome is for fiscal policy makers to pay attention to the level of interest rates. When short- and longer-term rates are particularly high, as they are at the moment, governments should be wary of running a loose fiscal policy. In this context, then, it is a concern that the stance of policy – as measured by the 'structural' deficit (excluding debt-interest payments – also known as the cyclically-adjusted primary balance), is very close to its long-run historical average in 2026-27 and has loosened significantly relative to the plans Labour inherited in 2024 (Figure 10). So we judge that, in the current context, a further loosening in policy would not be warranted as it would unhelpfully add to inflationary pressures and so put further upward pressure on debt-servicing costs.

28 HM Treasury, Annex: The impact of borrowing on interest rates, December 2023.

FIGURE 10: **At the Spring Forecast, the stance of fiscal policy was close to its long-run average in 2026-27 suggesting it would be hard to justify further loosening**

Cyclically-adjusted primary borrowing as a proportion of GDP relative to long-run average, OBR forecasts: UK



NOTES: Historical average is from 1980 to 2007.
SOURCE: RF analysis of OBR, Public sector finances databank, various.

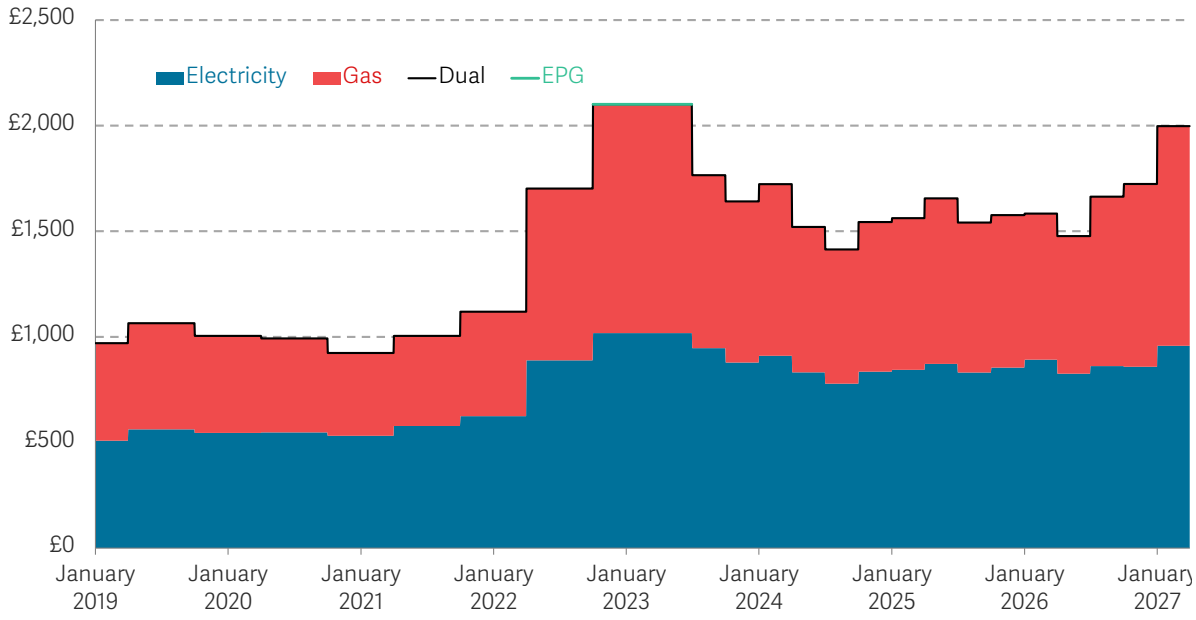
So support should be temporary and targeted, prioritising helping poorer families with high energy bills this winter

With limited means, then, the Government must decide whom to support, and how. The latest price cap forecasts predict the return of annualised costs in the region of £2,000, up 16 per cent from levels in Q4 2026 and the highest levels since the throes of the 2022-23 energy crisis (see Figure 11) for the roughly two-thirds of households not on fixed tariffs whose prices will rise in January.[29] This jump will land at the coldest time of the year and the period in which household gas use is at its highest: 46 per cent of domestic gas use takes place in the first quarter of the year.[30]

29 Cornwall Insight, Default Tariff Cap (Price Cap) Predictions & Insights, accessed 6th October 2026.
30 M Brewer et al., A Chilling Crisis, Resolution Foundation, August 2022.

FIGURE 11: **Energy bills are set to rise again in January**

Historical and forecast annualised default tariff cap levels, direct debit customers with typical consumption



NOTES: Assumed typical domestic consumption values in line with Ofgem's July 2026 update. Q1 2027 data is based on forecasts made at the end of September 2026. Does not include the Energy Bill Savings Scheme.
SOURCE: RF analysis of Ofgem; BEIS; Cornwall Insight.

Many households are already being pushed to the limit by high energy costs. Families are making deep cuts to consumption, with the number saying they are unable to adequately heat their homes increasing by 1.7 million from 2021-22 to 2022-23, while debt on bills has more than tripled in real terms since 2018.[31] And despite energy crises blighting living standards for four years, it seems that the Government has made scant progress on measures to target support at those most in need: families with both unavoidably high levels of energy use and low incomes from which to pay these elevated bills.

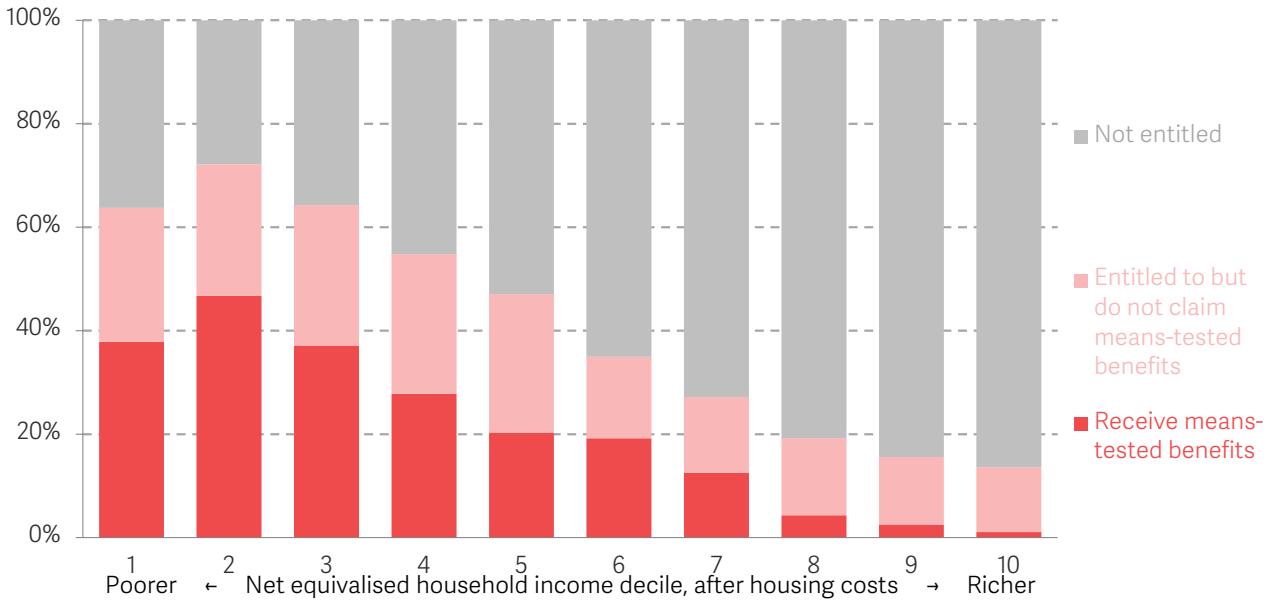
It has been reported that the Government is looking at deepening support via the Warm Home Discount (WHD), a policy that currently provides a flat £150 discount on electricity bills during the winter months to households on means-tested benefits (a doubling in generosity would cost in the region of £900 million).[32] There is clear merit in this approach: the WHD is a functioning mechanism and would be able to help households this winter. In 2025-26, 96 per cent of WHD rebates were paid through data matching without requiring an application, easing pressure on energy bills for 5.5 million households during the cold, winter months.[33] But the fact that the WHD is currently

31 M. Brewer et al., Counting the cost: The impact of five years of high inflation on living standards, Resolution Foundation, October 2026, https://doi.org/10.63492/vxy3542.
32 O. Wright et al., John Healey searching for buffer against energy price rises, The Times, 24 September 2026; J. Elgot & K. Stacey, Chancellor plans major intervention to help poorer UK households with rising energy bills, The Guardian, 6 October 2026; https://www.gov.uk/the-warm-home-discount-scheme, accessed 8 October 2026.
33 DESNZ, Warm Home Discount statistics, 2025 to 2026, June 2026.

passported from receipt of means-tested benefits implies that any additional generosity would reach only about a quarter of households, missing the roughly 7 million low-income families in the bottom two income quintiles not in receipt of these benefits, as Figure 12 shows. Further, an expanded as-is WHD would see eligible households on fixed tariffs receive a larger discount even though their bills will not increase in January.

FIGURE 12: **Passporting support via receipt of means-tested benefits misses the majority of poor households**

Proportion of households entitled to and in receipt of means-tested benefits, by equivalised after housing costs income decile: GB, 2024-25



NOTES: Means-tested benefit passporting shows households reporting means-tested benefit receipt in the Family Resources Survey. This is likely to be slightly underestimated due to known issues with underrepresentation of low-income households in the survey. The number of households entitled to but not claiming means-tested benefits is estimated by modelling full take-up using the IPPR tax-benefit model and subtracting those in receipt in the Family Resources Survey; this is therefore likely to be a slight overestimate. SOURCE: RF analysis of DWP, Family Resources Survey, including use of the IPPR tax-benefit model.

Despite missing many needy households, the Government may think that a larger WHD payment is the best approach this winter. If so, it should address some existing issues with the WHD first. To begin with, the WHD is currently funded through a levy on household energy bills, adding around £40 to the cost of the typical dual fuel bill (and reducing the net value of the discount accordingly to those in receipt).[34] Any additional expenditure should be met from public funds, thereby avoiding piling yet more upward pressure onto energy bills. Second, WHD eligibility is fixed by benefit receipt on a single qualifying day (23 August this year), so those who start claiming shortly afterwards miss

34 In April 2026 the cost of the WHD moved from gas and electricity standing charges to unit rates, further penalising households with high levels of energy consumption. Resulting higher gas prices will also have a negative welfare impact.

out while those who stop claiming still receive the rebate. This has always been a feature of the scheme, but becomes harder to accept the larger the payment becomes.

Any expansion of the WHD should be accompanied by a top-up to the Crisis and Resilience Fund (CRF), the discretionary fund that councils in England can use to help low-income households facing a financial shock. This would allow local authorities to help families who narrowly miss out on the WHD but who face real hardship this winter. Such crisis payments are not limited to benefit recipients, with councils deciding what counts as low income in their area, and CRF guidance explicitly allows payments to households facing hardship due to higher energy costs.[35] But it would be a mistake for the Government to rely solely on the CRF: it cannot do the same job as broader targeted help because it largely relies on families being aware of the scheme and applying, support varies between councils, and payments are designed for acute, short-term needs. But it could catch some of those who fall through the cracks of the WHD this winter.

These shortcomings should make clear that the Government's infrastructure for targeting vulnerable households is still not up to scratch.[36] Recent media reports also suggest that the Government is, finally, taking a longer view, which is very welcome indeed following years of unacceptable inaction, as high bills are currently expected through 2027.[37]

In this context, two options are reportedly being developed, although not in time to be announced at the Budget: a social tariff, which would give lower-income households a discounted price for each unit of energy they use, and a 'rising block tariff', which would give every household a block of cheaper 'essential' energy and charge more for consumption above it. Of the two, a social tariff is far better suited to helping the families most exposed to high bills. As we have argued previously, energy need varies far more within income groups than between them, so support must target the intersection of low income and high consumption, not just one or the other – which a social tariff would achieve by discounting unit prices.[38] A rising block tariff, by contrast, has drawbacks. Most obviously, by offering the same block of cheaper energy to every household, it functions as a flat cash transfer to all – in effect, a Warm Home Discount for everyone. Much of that money would go to households for whom higher bills are an inconvenience rather than a hardship. There is also a secondary set of problems about how to decide on the size of the discounted amount: if it's the same for every household, then it offers little more than the Energy Bill Support Scheme introduced while Rishi Sunak was Chancellor, which offered households a flat £400 regardless of need or income. And if the cheaper 'block' is paid for by charging more for energy used above it, households with

35 DWP, Crisis and Resilience Fund: Guidance for local authorities in England (1 April 2026 to 31 March 2029), April 2026.
36 The Government's 2026 WHD consultation response opened the door for better targeting, committing to explore 'better data-sharing' and increased eligibility. DESNZ, Continuing the Warm Home Discount, January 2026.
37 EDF, Energy price cap predictions, accessed 9 October 2026.
38 M. Brewer et al., A chilling crisis: Policy options to deal with soaring energy prices, Resolution Foundation, August 2022.

unavoidably high energy use could end up paying more. If instead the size of the block varies with household size or need, then the Government would need to avail itself of such information for around 28 million households – which it currently does not hold.

So, a government looking to relieve hardship in the most effective way possible should commit to building a system of Targeted Energy Discounts. We have previously set out how one could work.[39] In particular, support would be paid automatically to households receiving means-tested benefits, as with the WHD. It would also go to households passing an income test based on the highest individual income in the household, assessed over the three months before the scheme begins. A threshold of £24,000 would reach around 40 per cent of households, covering 75 per cent of those in the poorest four income deciles. A £2 billion scheme, funded from general taxation rather than yet another levy on bills, could provide an average discount of £175 per eligible household. Alternatively, it could be tiered to give around £220 to those with incomes below £18,000 and £85 to those earning less than £24,000. Once built, the system should be kept ready and switched on at the quarterly price cap reset whenever prices spike. That way ministers would no longer have to fall back on costly universal support.

Lower-income tenants urgently need support to catch up with rent rises

The Government's other priority for cost of living support should be restoring the value of housing support for low-income private renters. Local Housing Allowance (LHA), which caps how much housing support private renters can receive through the benefit system, has been frozen since April 2024. Over 900,000 private tenant households on Universal Credit now pay more in rent than their LHA, with a family renting a typical two-bedroom home facing a shortfall of £158 a month.[40]

The average gap between the help available and where it would be if it were unfrozen has already passed 20 per cent and will imminently reach record levels.[41] Continuing to freeze LHA may create savings for DWP, but it shunts costs onto local authorities who have to provide temporary accommodation to those in the most acute need, something that cost councils in England £2.9 billion in 2025-26.[42]

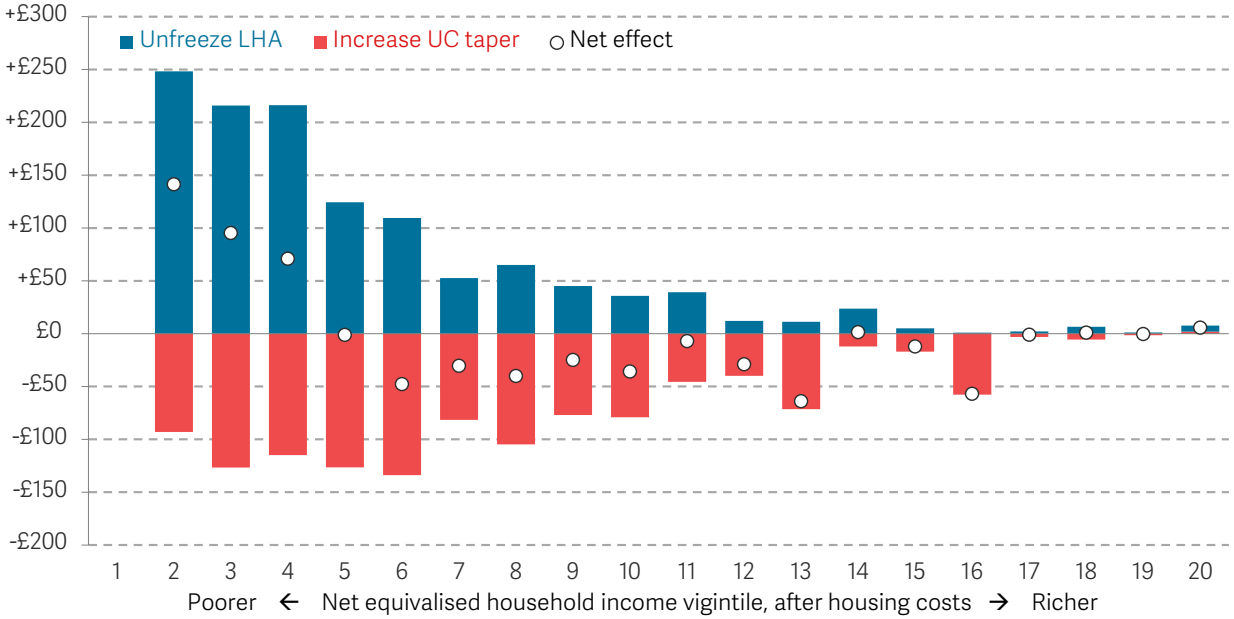
Relinking LHA to the 30th percentile of local rents and keeping it pegged to that level thereafter would cost £2.3 billion in 2029-30. It would have only a small impact on rent

39 M. Brewer et al., Billing me softly: How to design targeted energy discounts, Resolution Foundation, August 2026, https://doi.org/10.63492/acb5514; M. Brewer et al., A chilling crisis: Policy options to deal with soaring energy prices, Resolution Foundation, August 2022.
40 H Aldridge et al., Saving private renters: Why the Government should unfreeze Local Housing Allowance, Resolution Foundation, September 2026, https://doi.org/10.63492/xjbc2944.
41 H Aldridge et al., Saving private renters: Why the Government should unfreeze Local Housing Allowance, Resolution Foundation, September 2026, https://doi.org/10.63492/xjbc2944.
42 Shelter, Councils spend more than £8 million a day on temporary accommodation, September 2026.

levels and a big one on the living standards of cash-strapped tenants.[43] If necessary, such a change could be paid for by making savings within the benefit system itself. Increasing the UC taper rate – the amount by which benefits are withdrawn when earnings increase – from 55 per cent to 58 per cent, for example, would raise enough revenue to cover the cost of unfreezing LHA.[44] Figure 13 shows how these two changes combined would affect households across the income distribution. There are three points to highlight here. First, unfreezing LHA is a well-targeted policy, benefiting those at the bottom of the distribution most. Second, the impact of a higher taper rate is spread much more widely across the bottom half of the income distribution. Third, if both policies were applied, the loss from increasing the UC taper would be more than countered by increasing LHA among the poorest fifth of households. Further up the income distribution the net impact on incomes is negative, but the size of the losses among the second fifth are much smaller than the size of the gains in the bottom fifth.

FIGURE 13: **Unfreezing LHA could be funded by increasing the UC taper which would, on balance, benefit the poorest households**

Average change in annual household income (after housing costs) as a result of unfreezing LHA and increasing the UC taper (2026-27 prices), by income vigintile: UK, 2029-30



NOTES: The chart models the impact of increasing the UC taper from 55 per cent to 58 per cent. We assume that unfreezing LHA would mean rebasing rates to the 30th percent rent level measured in the 12 months to September of the previous year.
SOURCE: RF analysis of DWP, Family Resources Survey using the IPPR Tax-Benefit Model; ONS, Price Index of Private Rents.

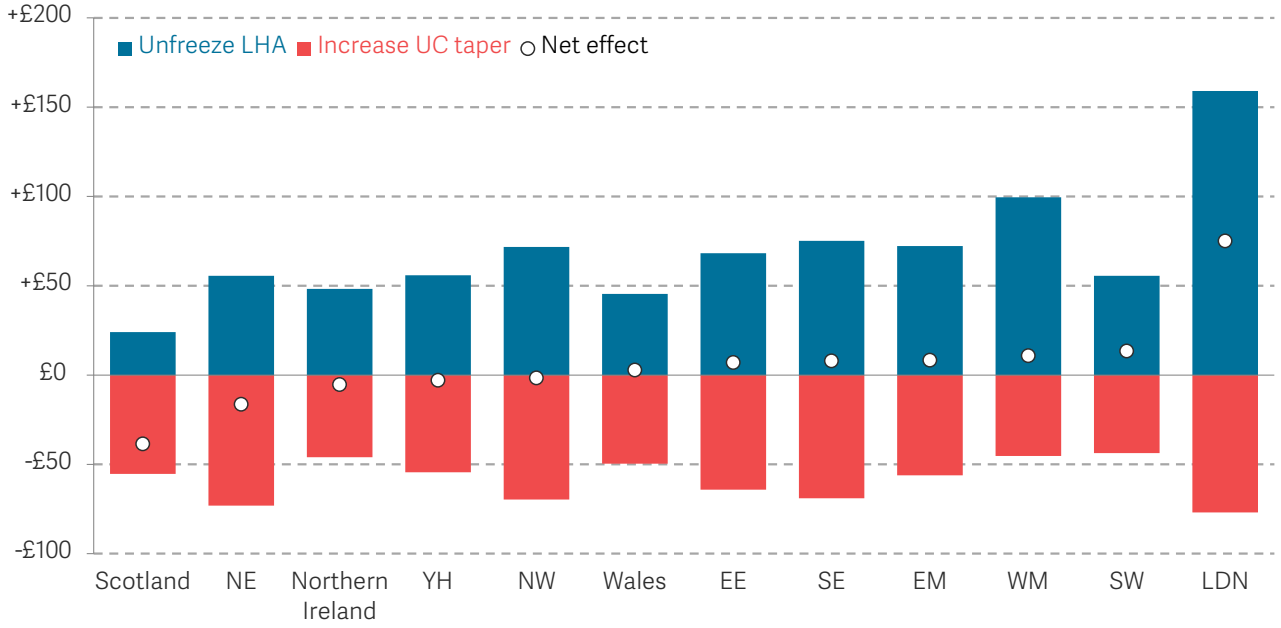
43 H Aldridge et al., Saving private renters: Why the Government should unfreeze Local Housing Allowance, Resolution Foundation, September 2026, https://doi.org/10.63492/xjbc2944.
44 Increasing the taper rate to 58 per cent would slightly weaken work incentives, but the taper would still be much lower than it was in 2021 (when the rate was reduced from 63 per cent to 55 per cent); and in 2017 (65 per cent).

Naturally, relinking LHA to actual rents has a greater impact in areas where a high number of lower income households rent privately (which determines the number of households affected), and the gap between LHA and market rents is bigger (which determines the amount by which affected households stand to benefit). Both factors mean that cities such as London, Manchester, Liverpool and Birmingham benefit most from unfreezing LHA. Figure 14 shows that households in London would gain on average £160 a year by 2029-30 if LHA were unfrozen. But they would also see the biggest losses from increasing the UC taper, bringing the net gain down to £75 a year. In all other places bar Scotland and the North East, the two changes largely offset one another.

Places across the UK would benefit from LHA being unfrozen. Manchester, Tameside, Reading and Bournemouth are all among the areas seeing the biggest cash shortfalls between what LHA is now and what it would be now if the freeze were not in place (a gap of over £175 per month for a two-bedroom home). Continuing the freeze on LHA simply prices out lower-income renters who are unable to access social housing in the postcodes where rents and the broader economy are growing the fastest.

FIGURE 14: **Those in London see the biggest gains from unfreezing LHA, but also the biggest losses from increasing the UC taper**

Average change in annual household income (after housing costs) as a result of unfreezing LHA and increasing the UC taper (2026-27 prices), by nation and region: UK, 2029-30



NOTES: The chart models the impact of increasing the UC taper from 55 per cent to 58 per cent. We assume that unfreezing LHA would mean rebasing rates to the 30th percent rent level measured in the 12 months to September of the previous year.
SOURCE: RF analysis of DWP, Family Resources Survey using the IPPR Tax-Benefit Model.

Other measures should be targeted to support those who have faced the greatest hardship

Targeted Energy Discounts and LHA uprating are the most powerful interventions that a government looking to provide targeted support can make, but they are not the only measures that would benefit the lower-income families most affected by the cost of living crisis. If resources allow – that is, subject to getting borrowing falling this year – the priority beyond these interventions should be to provide support in areas that can be most beneficial to families suffering the greatest hardship. This could include further reducing bus fares – which are used disproportionately by lower-income families – for example by making buses free for young people – or through cutting water bills, where the same sort of arguments around targeting support apply.[45]

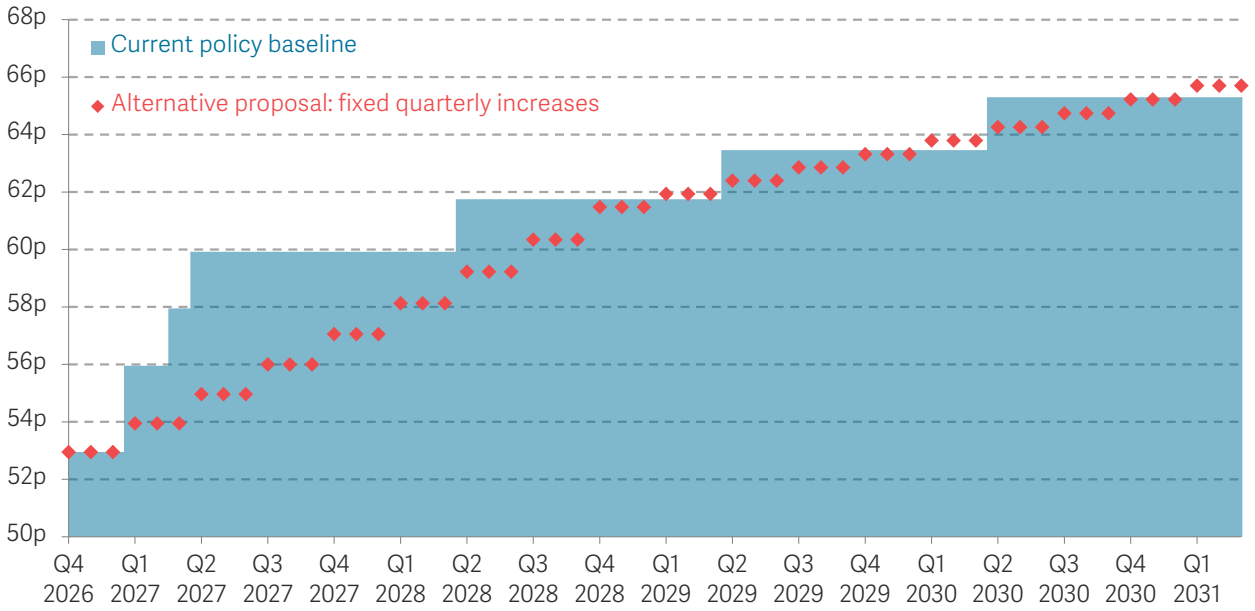
In contrast, extending the Fuel Duty freeze is not a well-targeted measure and so should not be a priority.[46] Despite recent rises, fuel costs remain below historic highs.[47] Moreover, higher-income households tend to spend more of their income on petrol and diesel than lower-income households.[48] And a prolonged period of cuts have eroded the revenues from driving and distorted the incentives to use fossil fuels. Successive governments have abused the requirement for the OBR to forecast on the basis of announced policy by repeatedly promising to raise Fuel Duty and then consistently implementing temporary cuts or freezes. The flipside of this is that raising it will not lead to a forecast improvement as this is the default policy. However, though the Fuel Duty forecast may be based on a fiscal fiction, the dividend from the bond market on seeing an increase enacted will be real.

So how can the Government actually deliver a rise in Fuel Duty? In this context, it is not encouraging that current plans imply that it will rise by around 13 per cent between now and April. The idea that such a large rise is coming, particularly if petrol and diesel prices remain elevated, is unrealistic. A more credible and deliverable alternative then would be to shift to a system of small quarterly increases. For example, as shown in Figure 15, if over the coming years there are steady rises reversing the 5p cut and then of, say, 3 per cent a year, this would cost money in the short term relative to the current policy – likely over £1 billion in 2027-28 – but would be broadly revenue neutral by 2029-30, the year against which the fiscal rules are assessed.

45 A. Corlett et al., Getting the green light, Resolution Foundation, October 2024, https://doi.org/10.63492/uhie438.
46 A. Clegg et al., Power struggle: Assessing the options for supporting families with the rise in the cost of energy, Resolution Foundation, March 2026, https://doi.org/10.63492/xda2494.
47 Since January 2011 – when Fuel Duty rates last increased – real petrol prices have been higher than they were in the last week of September in around a third of weeks, and real diesel prices in around a quarter.
48 A. Clegg et al., Power struggle: Assessing the options for supporting families with the rise in the cost of energy, Resolution Foundation, March 2026, https://doi.org/10.63492/xda2494.

FIGURE 15: **Regular, fixed Fuel Duty increases would be a more realistic, and therefore more credible, policy**

Nominal main rate of Fuel Duty per litre, by policy scenario: UK



NOTES: The current policy baseline uses RPI projections from the OBR's March 2026 Economic and fiscal outlook for the longer-term projection and the ONS outturn for August 2026 as the indicator of the scheduled uprating in April 2027.
SOURCE: RF analysis of OBR, Economic and fiscal outlook, March 2026; ONS, RPI, August 2026.

One of the things set to feature in the Budget is Your First Home, Labour's version of Help to Buy: an equity loan scheme to help people to buy new build homes and stimulate housebuilding at the same time. The scheme aims to target those currently unable to buy and will be funded via developer contributions and within existing departmental budgets. While it will lower the subsequent mortgage repayments of first-time buyers who use Your First Home, it will not help the poorest renters as they will not be in a position to get a mortgage even with the scheme in place (see Box 4).

BOX 4: Help for First Time Buyers

Your First Home will allow first time buyers (FTBs) with a minimum 2.5 per cent deposit to purchase a new build home with a 20 per cent equity loan from the government.[49] This will make it easier for potential buyers to get a mortgage by lowering both the savings and income barrier to homeownership.[50]

Your First Home would also ease cost of living pressures for FTBs by reducing mortgage payments. The cost benefits are two-fold, FTBs will have a smaller balance to pay off over the length of their mortgage term and benefit from a lower interest rate that is offered on lower loan-to-value mortgages.

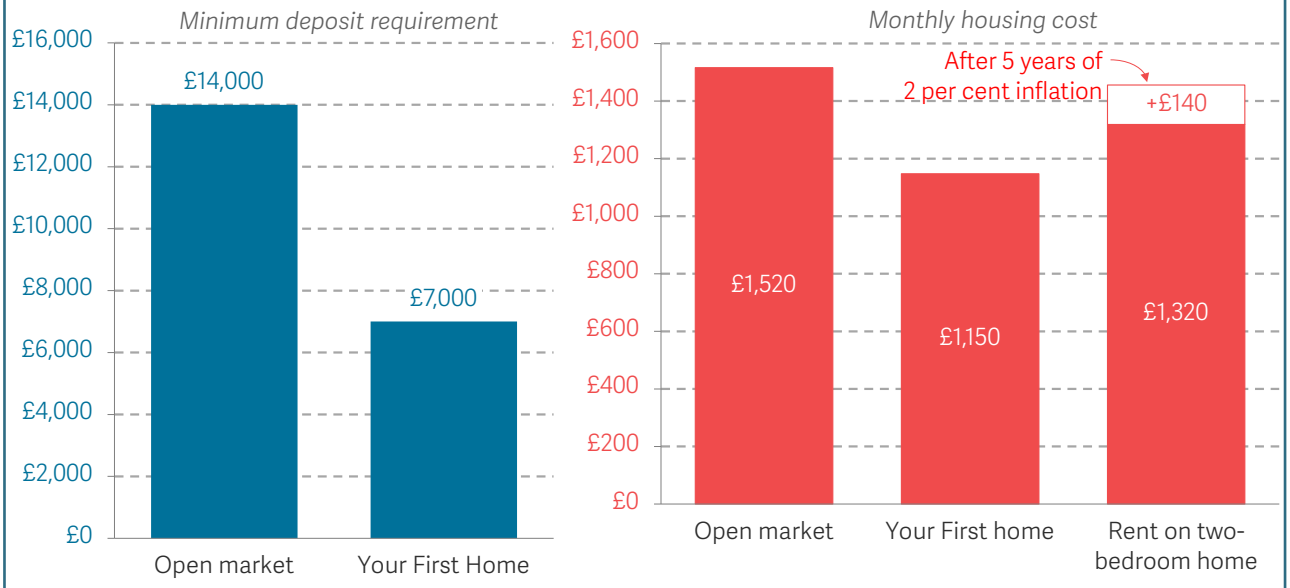
Figure 16 shows the impact the scheme would have on the cost of buying a home worth £280,000 – the average FTB purchase price in Q2 2026. It halves the deposit requirement from £14,000 to £7,000 and lowers mortgage repayments by 25 per cent, from £1,500 a month to £1,150. But for FTBs the better counterfactual is the rent they are already paying. A family paying the average rent on a two-bedroom home in England in Q2 2026 (£1,320 a month) could lower their monthly housing costs by £150 if they bought a £280,000 property via Your First Home. Further, this saving would grow over time as the average rent level is likely to increase by £140 over five years while mortgage repayments remain the same.

49 Ministry of Housing, Communities and Local Government, New first-time buyer scheme to be confirmed at Budget, September 2026.

50 The saving barrier is halved because FTBs would only need a 2.5 per cent deposit compared to a 5 per cent deposit required by mainstream mortgage products. The income threshold is lower because FTBs can only borrow up to 4.5 times their total income (rising to 6 times for higher income buyers) and they would only have to borrow 77.5 per cent of a Your First Home property, compared to 95 per cent otherwise.

FIGURE 16: **Your First Home would halve deposit requirements and reduce mortgage repayments by 25 per cent for first time buyers**

Minimum deposit requirement (left panel) and monthly housing costs (right panel) on a home worth £280,000 with and without the Your First Home scheme, and a two-bedroom rented property: England, Q2 2026



NOTES: The deposit requirement is 5 per cent in the open market scenario and 2.5 per cent in the Your First Home scenario. Monthly housing costs include interest and principal repayments. The chart shows the cost for a £266,000 loan at an interest rate of 5.45 per cent over 30 years in the open market scenario and a £217,000 loan at an interest rate of 4.78 per cent over 30 years in the Your First Home Scenario. Rent for a two-bedroom home is the average in England in Q2 2026. The rent inflation scenario assumes a 2 per cent increase for five consecutive years.
SOURCE: RF analysis of Bank of England, Bankstats; ONS, House price data: quarterly tables; ONS, Price Index of Private Rents (PIPR).

The advantages that Your First Home offers potential buyers are clear. But the difficulty will be making sure the scheme reaches those who are unable to buy otherwise. Indeed, one of our criticisms of Help to Buy was that it was poorly targeted and allowed those already able to buy a home to purchase a more expensive one with a larger deposit.[51]

The Government has said that this scheme will be targeted at those who would not currently be able to buy via a household income cap and property price caps, the details of which are expected in the budget.[52] The difficulty is that new build homes tend to command a premium because they are more energy efficient and meet modern building standards. If price caps are set too low, it will not be viable for

51 Just 37 per cent of households using Help to Buy as of December 2018 could not have bought a property without the scheme. Source: National Audit Office, Help to Buy: Equity Loan scheme – progress review, June 2019.
52 O. Gill, 'Households earning over £110,000 excluded from revived help to buy', The Times, 10th October 2026.

developers to build. If they are set too high, the FTBs who could afford them could also afford a pre-existing property. The same balance needs to be struck with the income caps; they will need to be high enough for FTBs to be able to secure a 77.5 per cent loan-to-value mortgage. But the higher the income cap, the less targeted the scheme becomes. We have previously called for a deposit cap as a way of targeting support to those without access to the Bank of Mum and Dad. But, when the benefits of the scheme are enough to reduce monthly mortgage payments by 25 per cent, those with enough savings to buy now would be better off using the scheme and investing surplus savings elsewhere.

As Your First Home is exclusively for new build properties, it seems inevitable that some families who could buy a cheaper home now will be eligible for the scheme. (This will include families only able to afford homes requiring costly renovations and supporting them to buy something more suited to their needs is far from a bad outcome). At the same time, the deposit requirement of 2.5 per cent will still be too high for many modest-income families facing high rents who struggle to save.[53] Setting that aside, Your First Home should stimulate developers to build starter homes and make buying possible for those just shy of being able to do so now, lowering their housing costs at the same time.

Key challenge two: the Government should rebuild headroom to at least £20 billion

Our estimates suggest that headroom against the fiscal rules will have halved to around £12 billion in 2029-30. The decision about how much of this medium-term deterioration to allow or repair is separate to the short-term decision about cost of living support. Our view is that the Government needs to rebuild headroom to at least £20 billion.

The counterargument is that headroom is there to offset shocks – a buffer you can't use isn't really a buffer. But a buffer of £12 billion in three years is too small for three main reasons. First, the Government has committed to increasing defence spending but not said how. Growth rates for total departmental spending already looked tight for the next Spending Review and the Government has made other priorities, such as housebuilding, clear too. Second, bond markets are charging the UK Government relatively high interest rates in part because it doesn't have a long track record of fiscal consolidation and in part because it expects that the Bank of England will need to cool the economy (as discussed in Box 3). Too thin a margin of error could prompt still higher interest rates and borrowing

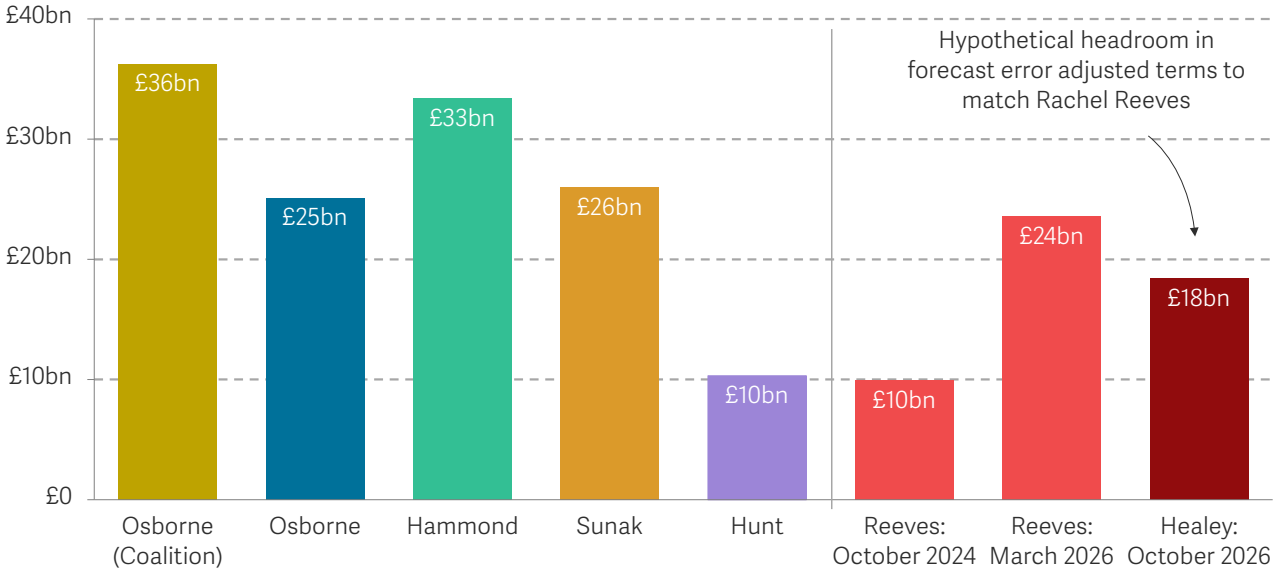
53 Of the 1.1 million non-owning families in England who would lower their housing costs by buying but would not be able to get a mortgage in the open market, almost three-quarters have less than £1,500 in savings, and 84 per cent have less than £3,000. See: H Aldridge, S Pittaway & J Smith, Credit where credit's due? Unpacking the distributional impact of Britain's mortgage lending rules, Resolution Foundation, March 2026, https://doi.org/10.63492/udgn419.

requirements, while renewed consolidation will take pressure off the Bank. And third, Governments of both parties have a bad habit of overshooting their borrowing forecasts (see Figure 9 above).

Why £20 billion? Although there is no magic number here, it's worth recognising that the 2029-30 target will now refer to the third year of the forecast rather than the fourth. Bringing the target forward in this way means somewhat less uncertainty about the forecasts, suggesting that headroom could reasonably be somewhat smaller. Past forecast errors three years out have, on average, been around a fifth smaller than those four years out, so headroom of around £18 billion against a year-three target offers roughly the same protection as the £24 billion held by Rachel Reeves at the Spring Forecast – as Figure 17 shows. The (absolute) average variation in borrowing between forecasts for the third year is £16 billion so headroom above that is resilient to one dose of 'average' bad luck. Given the circumstances discussed above, we judge that credibility requires every effort is made to restore headroom to at least £20 billion in 2029-30.

FIGURE 17: **John Healey would need £18 billion of headroom to maintain an equivalent buffer in 2029-30 to that Rachel Reeves had**

Average headroom held against fiscal rules by previous Chancellors and by the current Chancellor at set points in time: UK, June 2010 – October 2026



NOTES: Previous headroom estimates have been taken from the chart "Probability of meeting and headroom against fiscal mandate" in previous OBR Economic and Fiscal Outlook reports. The hypothetical estimate for John Healey is calculated by scaling Rachel Reeves' £24bn headroom in year four of the March 2026 forecast with an error-adjusted ratio for year three of the forecast.
SOURCE: RF analysis of OBR, Economic and Fiscal Outlook, March 2025, November 2025 and March 2026.

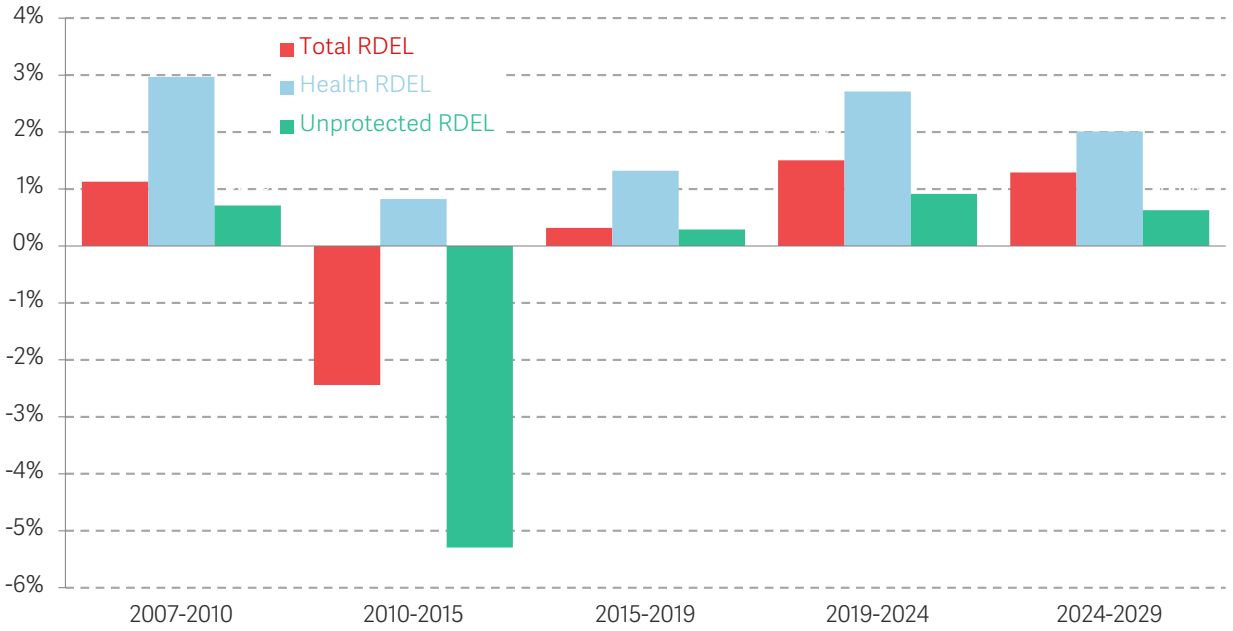
So the Government should respond to the hit to the public finances from the war and put in place measures that rebuild headroom. Below we discuss how this could be achieved through spending and tax measures.

The Government should absorb immediate pressures in its existing spending envelope

The backdrop to spending decisions in this Budget is a Parliament that has, so far at least, seemed a generous one. The 'tax and spend' Budgets of 2024 and 2025 undid the huge cuts pencilled in by Jeremy Hunt – including annualised contraction of spending in unprotected departments of 1.9 per cent a year. Total real day-to-day departmental spending (that is, resource departmental expenditure limits, or RDEL) spend per person is set to grow at 1.3 per cent a year between 2024-25 and 2029-30, just below the 1.5 per cent a year of the last parliament. This modest growth is a far cry from the settlements in austerity years, and similar to those seen under Brown in the late 2000s and the Covid-era Johnson Government. On the other hand, the lion's share (three-fifths) of this has gone to health and defence, meaning unprotected department spending (all those aside from health, defence, education and devolved governments) will grow by only 0.6 per cent a year – as we show in Figure 18.

FIGURE 18: **Day to day spending growth is set to be steady this parliament**

Annualised real per capita RDEL growth rates by parliament, total and unprotected: UK



NOTES: Assumes that immediate pressures from the Defence Investment Plan and higher teachers' pay, among other policies shown in Table 1, are funded through a higher spending envelope. Unprotected RDEL includes all spending aside from that on health, education, defence and devolved governments. Where spending envelopes have not been set, we assume education spending grows in line with inflation and pupil numbers, health spending grows by 2.6 per cent above inflation, defence spending grows in line with inflation, and devolved Government settlements grow in line with Barnett consequentials for other protected departments.
SOURCE: RF analysis of OBR, HMT, various.

However, this somewhat rosy picture hides a plethora of pressures for the Chancellor. In particular, the above chart assumes that the £3.7 billion of spending commitments announced since March – mostly during Keir Starmer's time as Prime Minister – do not come from within existing spending totals. This total comprises a broad basket of policies, but the big-ticket items are the Defence Investment Plan (at £1.7 billion in 2029-30) and a higher-than-expected settlement for teachers pay (£1.6 billion).[54] Funding these within existing spending totals would leave unprotected departments to pick up the bill, squeezing spending growth in that unluckier part of government to 0.2 per cent a year this Parliament, a settlement lower than that given over 2015-2019. And that doesn't account for higher inflation since March, which will push down on the real value of nominal totals. Failing to maintain the real value of 2029-30 RDEL settlements would leave all departments overall £9.7 billion poorer than planned in March, based on the latest Bank of England inflation projections.[55]

On top of that, Andy Burnham has set out an ambitious agenda for a new National Care Service, possible nationalisation of utilities, and the biggest council house building programme since the post-war era. These are long-term commitments and we do not expect the Budget to attempt to fund them. Adjusting the triple lock to remove the ratchet effect in the next Parliament is an important improvement in the public finances, particularly in the long-run, and this move was announced to at least partially pay for the new National Care Service. Questions remain about how the new service will be funded in its earlier years, but it is not clear those will even be answered in the next Spending Review. More generally, the new Prime Minister and Chancellor will need to grapple next year – when the Spending Review is due – with how to reconcile their ambitions for public services with the money set aside.

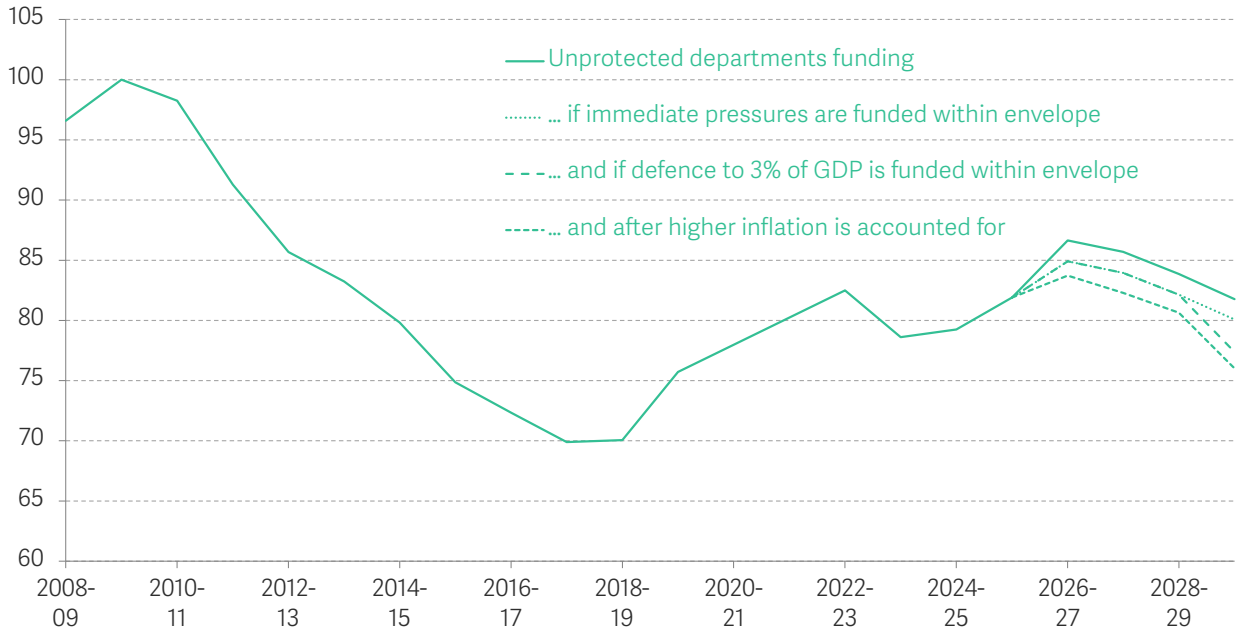
One of the most immediate pressures is coming from the previous Government's commitment to raise defence spending to 3 per cent of GDP by the end of this Parliament – and to 3.5 per cent by 2035. The Defence Investment Plan is only the first step to this goal, and day to day spending must rise by a further £6 billion, and capital spending by another £4 billion to meet the 3 per cent interim goal. It is as-yet unclear how keen John Healey – who resigned from the Defence brief over what he judged as inadequate spending just four months ago – is on inheriting Starmer's commitments now he is in Number 11. But the size of the problem makes it better to decide soon, including how it's funded. Asking unprotected departments to pay for it all would require cuts in day-to-day spending, amounting to £9 billion in real terms between 2028-29 and 2029-30 (or 5.5 per cent, more than a typical austerity year). If nominal spending limits are not topped up to account for higher inflation projections that would increase to £11 billion,

54 For a full list of policies see Annex 2
55 These forecasts also don't consider any changes in population forecasts since the Spring 2026 forecast. Lower migration would put upwards pressure on real per capita spending, offsetting the effects of higher inflation.

a 7 per cent cut. Figure 19 shows that unprotected funding has recovered substantially since 2018-19, but absorbing all of these spending pressures via unprotected departments would mean reversing most of that growth in just three years.

FIGURE 19: **Funding defence within the existing envelope could make life very difficult for unprotected departments**

Index of real per capita RDEL for unprotected departments (2009-10=100), by scenario



NOTES: Immediate pressures total £3.7 billion in 2029-30 and mainly comprises the Defence Investment Plan and higher than expected teachers' pay. Each scenario includes the pressures from preceding one, for example the defence to 3 per cent of GDP also includes higher teachers' pay.
SOURCE: RF analysis of OBR, HMT, various.

Funding defence spending with tax rises would limit the damage – real cuts would be just £3 billion and, on a per person basis, funding would remain above 2024-25 levels. Given the size and speed of cuts shown in Figure 19, a broad and progressive tax rise is a fairer way to share the burden than a return to austerity era cuts.[56]

There is undoubtedly a difficult balancing act in deciding the totals within which departmental settlements for the next Spending Review will need to be made. Given the high level of public spending, recent history of tax raising budgets, and an ambitious future programme to fund, the Chancellor needs to demonstrate an ability to control departmental spending and absorb some pressures there, by avoiding any additions to planned totals beyond those needed for defence. Amid these tough and uncertain conditions, the Chancellor should use the opportunity to reduce uncertainty around the UK's fiscal position by setting out a spending envelope that is intended for spending review at this Budget.

56 M Cavanagh & J Smith, Thin end of the wedge: Putting the tax burden on middle earners in an international and historical context, Resolution Foundation, September 2026, https://doi.org/10.63492/ytx9262.

We cannot expect benefit cuts to ease other pressures at the Budget

Despite rhetoric to the contrary, we do not have a 'runaway' benefits bill in the UK. A decade ago, in 2016-17, benefit spending as a share of GDP stood at 10.4 per cent; in 2026-27, the figure is 11.1 per cent.[57] There is little fat to trim from the overall spend without damaging living standards, risking a political backlash or both.

But there is scope to rebalance it. This process has begun with the Government's recent announcement that it would adjust the triple lock on the State Pension from 2030-31. But welcome though this is, it does not help with the short-term spending pressures the Government faces at the Budget.[58] Further changes to the social security system are likely, but not at this Budget, not least because both the Milburn Review (examining how the benefit system could better support young people that are not in education, employment or training (NEET)) and the Timms Review (examining how the Personal Independence Payment could best be reformed) are yet to report.

Tax rises may be needed to deliver stronger public finances

With headroom falling to around £12 billion, rebuilding it to £20 billion while staying within the existing spending envelope would require raising around £8 billion of revenue. That would be a sizeable tax rise, although much smaller than those in either of the Budgets delivered by Rachel Reeves, and not unusual by historical standards.[59]

It is strongly rumoured that the Chancellor is looking to find additional revenue from the banking sector.[60] There are many ways this could be achieved. Given strong bank profits performance, driven in part by higher interest rates, increasing the Bank Surcharge would be a straightforward option. Prior to April 2023, banks paid an 8 per cent surcharge on their profits on top of Corporation Tax.[61] When the main rate of Corporation Tax increased from 19 to 25 per cent, the surcharge decreased from 8 to 3 per cent. This meant banks' combined rate rose by just 1 percentage point, while other large businesses saw a 6 percentage point increase. At the current rate of 3 per cent it is forecast to raise £1.4 billion in 2029-30.[62] A large increase could be counterproductive leading to a reduction in the flow of credit to the real economy just as growth seems to be picking up.

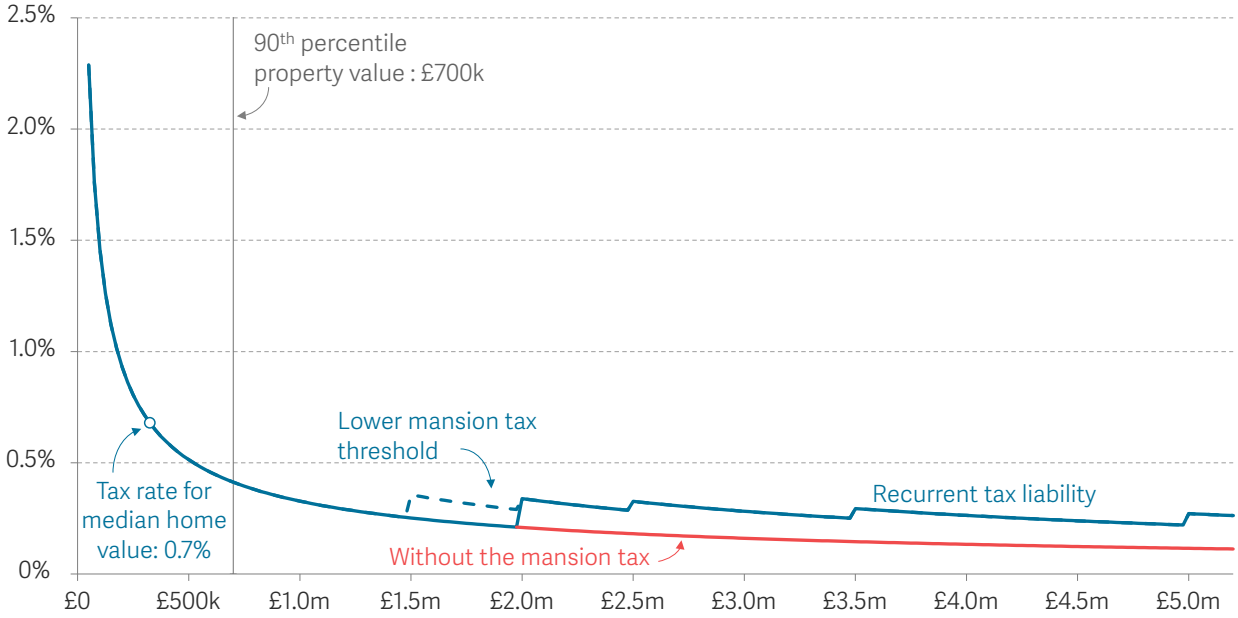
Another rumoured change is a lowering of the threshold at which the High Value Council Tax Surcharge (better known as the 'mansion tax') is applied.[63] Figure 20 shows how this

57 RF analysis of DWP, Expenditure and Caseload forecasts, Spring Forecast 2026; Scottish Government, Economic and Fiscal Forecasts update, January 2026. Figure represents Great Britain.
58 R Curtice & P Pandya, Why nobody knows how much we'll save from the triple lock announcement, Resolution Foundation, October 2026.
59 For the historical context, see Figure 6 in H Aldridge et al., Stairway to headroom: Putting the Autumn Budget 2025 decisions on tax, spending and borrowing into context, Resolution Foundation, November 2025, https://doi.org/10.63492/gad912.
60 L Almeida, JP Morgan boss Jamie Dimon warns UK chancellor not to hike taxes on banks, The Guardian, 17 August 2026.
61 HMRC, Amendments to the surcharge on banking companies, October 2021.
62 OBR, Economic and fiscal outlook, March 2026.
63 A Marsh, One in four London houses could be caught by mansion tax, The Telegraph, 21 September 2026.

could look in the context of England's recurrent taxes on residential property (i.e. Council Tax and the mansion tax combined). Here we illustrate the impact of a new band where properties worth £1.5 million to £2 million are charged £1,500 a year. While this would roughly double (to 320,000) the number of properties within scope of the mansion tax in 2029-30, only around 1 per cent of homes would be affected. The vast majority would remain well below the mansion tax threshold (90 per cent of homes in England are worth less than £700,000).[64]

FIGURE 20: **Even after a mansion tax extension, owners of higher value homes would have a lower effective tax rate than the median**

Median annual recurrent property tax liability as a proportion of property values, by property price: England, 2029-30



NOTES: Illustrates what an additional HVCTS band of £1,500 a year on properties worth between £1.5 million and £2.0 million.
SOURCE: RF analysis of Land Registry, Price Paid data; MHCLG, 2024 Market Value Survey; OBR, Economic and Fiscal Outlook March 2026; DWP, Family Resources Survey, including use of the IPPR tax-benefit model.

We estimate that an additional mansion tax band could raise £170 million in tax revenue in 2029-30 – hardly a solution to the Government's fiscal woes. It would, however, move our property tax system in a slightly more progressive direction, by increasing the effective tax rate for the high value homes affected. But that rate would still be about half the effective tax rate faced by the typical household in England in 2029-30, of 0.7 per cent on a home worth £325,000.

Extending the mansion tax would be a welcome tiptoe in the right direction, as it requires more homes to be revalued by the state for the first time in England since 1991. The

64 RF analysis of MHCLG, 2024 Market Value Survey and OBR, Economic and Fiscal Outlook March 2026.

Chancellor should set the ball rolling on wider property tax reform by announcing a full revaluation of all homes in England – a prerequisite to tackling our broken property tax system.

Together, doubling the Bank Surcharge and adding a new mansion tax band might raise around £1.5 billion – well short of the £8 billion required. But there are a number of options for the Chancellor to increase tax revenues as part of a strategy for tax reform that will improve the wider system. The four policies set out below would raise around £9.5 billion a year by 2029-30, and a switch from employee National Insurance (NI) to Income Tax could take that total to around £15.5 billion. Each measure addresses a case where the tax system treats similar incomes, people and firms very differently for no good reason, or lets some people side-step tax altogether. The principle behind these measures is simple: similar economic activity should be taxed similarly.

First, treating partners the same as employees. At present, a receptionist at a successful law firm attracts employer NI, but a partner at the same firm on £2 million a year does not. Closing this gap should be a priority – certainly for Limited Liability Partnerships, but there is a case for equalising rates across all partnerships. The Centre for the Analysis of Taxation estimates that applying an equivalent of employer NI to all partnership profits would raise £2.1 billion in 2029-30, with 98 per cent of the revenue coming from those in the top income decile and 58 per cent from the top 0.1 per cent alone.[65]

Second, lowering the VAT registration threshold. The current VAT regime incentivises firms to hold down their turnover so it does not go above the VAT registration threshold of £90,000. The threshold encourages firms to stop trading part way through the year or to stop expanding from one year to the next, holding back growth. Across 32 major European countries, the UK has the fourth highest VAT registration threshold.[66] Moving the threshold gradually to £30,000 would raise around £2 billion a year, ensuring fair treatment across firms, improving competition between them and removing a blocker to growth.[67]

Third, closing loopholes in Capital Gains Tax (CGT). When someone sells an asset that has risen in value, they pay CGT on the gain. But if they die while still holding the asset, or leave the country before selling it, they are not liable for CGT on those gains. We estimate that ending these exemptions would raise around £4 billion.[68] Those benefiting

65 A Advani, H Hughson & A Summers, Taxes at the top: Understanding what high earners pay and options for reform, Centre for the Analysis of Taxation, September 2026. The measure of total income includes realised capital gains. If the 2p tax switch measure – discussed below – is implemented, then the increase in the tax rate required to bring the rate on partnership income up to that of wages at the higher and additional rates would be lower.

66 A Mengden & J Graack, VAT Exemption Thresholds in Europe 2026, Tax Foundation, June 2026. The ranking is based on the annual revenue threshold adjusted for purchasing power parity.

67 A Corlett, Call of duties: Revenue and reform for Autumn Budget 2025, Resolution Foundation, September 2025, https://doi.org/10.63492/urc611.

68 This estimate is very uncertain and covered in more detail in: A Corlett, Call of duties: Revenue and reform for Autumn Budget 2025, Resolution Foundation, September 2025, https://doi.org/10.63492/urc611.

from the current exemptions are highly concentrated among the wealthy, and closing these loopholes would be a necessary first step in a wider reform of the CGT system.[69] Exempting gains on assets held until death encourages people to hold on to them, even where they could be put to more productive use. And not charging on exit creates a strong incentive to leave the UK before realising gains, which costs the Exchequer revenue and risks losing entrepreneurs, along with any future businesses they might build. Closing these loopholes should be a priority.

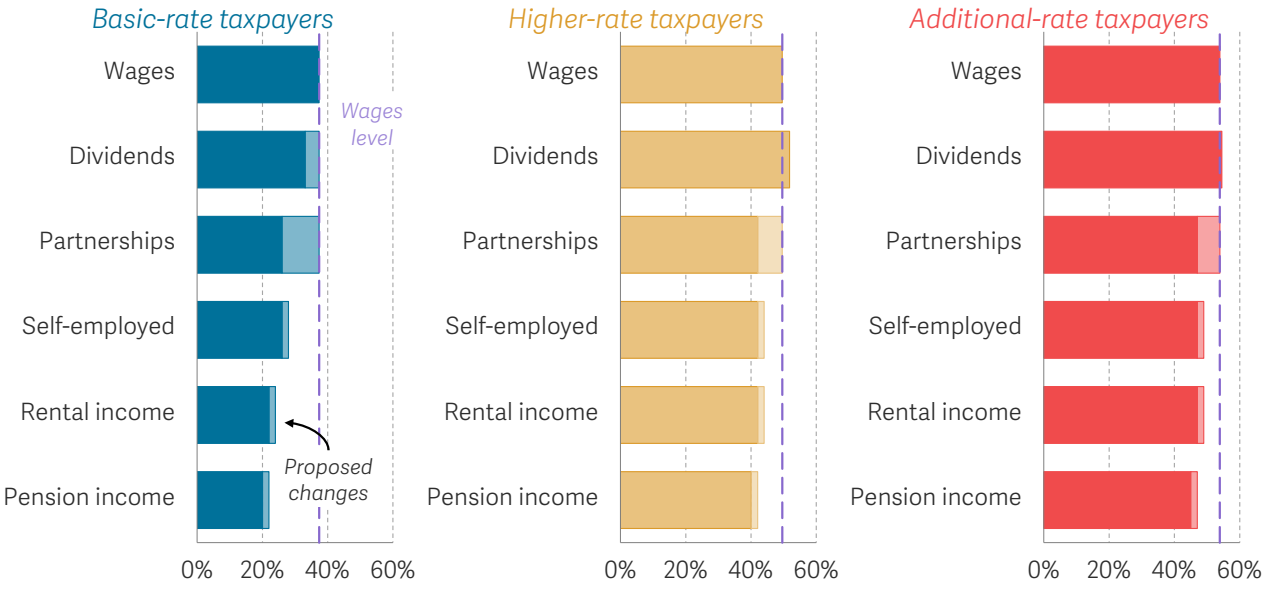
Fourth, increasing the basic rate of tax on dividends. Despite a recent increase in the basic rate of tax on dividends, when combined with Corporation Tax it remains lower than the basic rate of tax on wages. Consistent treatment requires raising this to (at least) 16.5 per cent.[70] This would help reduce incentives to devise artificial arrangements and ensure fair treatment across different income sources, while raising £1.5 billion.

Should the Chancellor choose to settle the question of how to fund higher defence spending in this Budget, larger sums will be needed, and the natural place to look is the tax that raises the most revenue: Income Tax. Employed workers face a specific tax premium, with the gap between tax on self-employment and employment reaching record highs.[71] Raising Income Tax rates by 2p and cutting employee NI by 2p would raise around £6 billion in 2029-30, while leaving tax rates on the earnings of working-age employees unchanged, arguably making the switch easier to sell politically.[72] Because Income Tax also applies to self-employment, pension and rental income, the switch raises revenue by asking more of the self-employed, landlords and pensioners with taxable income, all of whom currently face lower tax rates than employees on the same income (Figure 21). People receiving similar amounts of income should face similar tax rates, whatever the source of that income – and that is not the case now.

69 We set out our proposal for reform of the CGT system as part of the Economy 2030 Inquiry: M Broome, A Corlett & G Thwaites, Tax planning: How to match higher taxes with better taxes, Resolution Foundation, June 2023.
70 If profits were charged to the small profits rate of Corporation Tax, the basic rate of tax on dividends would need to be higher to ensure consistent treatment, but accounting for differences in rates paid would be complicated.
71 A Corlett, It's personal (taxation), Resolution Foundation, October 2025, https://doi.org/10.63492/vzw6992.
72 This would include increasing the rates of Income Tax charged on savings and property income by 2p. For further discussion of this proposal, see: A Corlett, Call of duties: Revenue and reform for Autumn Budget 2025, Resolution Foundation, September 2025, https://doi.org/10.63492/urc611.

FIGURE 21: **Wages for employees face higher taxes than other income sources – closing the gap will raise revenues**

Existing and proposed marginal tax rates 2027-28, including employer NI and Corporation Tax where appropriate: UK excluding Scotland



NOTES: For employee earnings we include the impact of employer NI. For dividends, we assume Corporation Tax has been paid at the main UK rate of 25 per cent. For pension income, the chart shows pension income from employer contributions. We show the impact of increasing the tax rates on partnerships to match those on wages; if the tax switch policy is implemented, then the increase in the tax rate required to bring the rate on partnership income up to that of wages at the higher and additional rates would be lower.
SOURCE: RF analysis.

The 2p switch is just one option for narrowing the gap between taxes on the wages of employees and income from other sources. There are other approaches the Chancellor could take to work towards that same goal: building on the changes made by Reeves in November 2025 and taking the new, separate rates for property income up a further 2p; targeting the gap between workers who are in employment and those in self-employment by increasing the rate of self-employed National Insurance (Class 4); and/or replicating the approach taken for property income and creating a separate tax rate schedule 2p higher than the standard rate for pension income.

The desire for a low-key Budget should not get in the way of dealing with the challenges of the here and now

There are tentative signs that the UK economy is becoming more resilient. But household and public finances are not, due to rises in energy prices and interest rates driven by war in the Middle East. The Chancellor must act.

The first challenge is the pressure on families facing a winter of energy bills touching £2,000 per year, a symbolic threshold close to that borne by households during the 2022

energy crisis. After 13 years of normal inflation in 5, everyone's living standards have taken a hit, with the typical family £2,900 worse off than if the economy had behaved as expected before the pandemic. But it is those most vulnerable, like the almost one-in-five households in the poorest half of the country already behind on at least one priority bill, who will truly enter this winter with trepidation. We have shown how the Chancellor can meet this challenge while keeping borrowing on a downward path.

The second challenge, looking further ahead, is a fiscal repair job. When the amount the government has to spend on servicing its debts rises, as it has done since March, there is simply less money for other things. Faced with such a shock the Chancellor's job is to tell us how they will meet the new reality – whether with lower spending or higher taxes. With a spending review due next year that is currently set to see 'unprotected' departments face a difficult 2.2 per cent real terms cut – or a huge 5.5 per cent one if we factor in defence spending rising to 3 per cent – it seems unrealistic for the Chancellor to promise cuts to aggregate spending at this fiscal event.

With spending set to be larger than it has ever been for a sustained peacetime period, the tax take must rise to a historic high too to avoid further deterioration in the parlous state of our public finances. Given the state needs to raise more, the costs of avoiding tax reform are only set to grow. The strategy for the revenue raising necessary at this Budget should be a focus on changes that improve the system, closing the gap between taxes on wages from employment and other forms of income, and dealing with cases where tax can be side-stepped altogether, while looking to the longer-term by starting the process of fixing a property tax system that manages to be both regressive and growth-sapping.

In this paper we have set out how the Chancellor can meet both of these challenges. By targeting cost of living support on energy bills and on low-income families he can alleviate the pressures for those most affected by the cost of living crisis. Tax measures are available that can both improve the fairness of the system and reliably raise revenue. By announcing them, alongside setting a timetable and a process for the spending review that provides reassurance the envelope for public services is set, the Chancellor could build confidence in financial markets that he is willing to face reality rather than duck it. It would not be the small Budget that the Government seems to want, but it would be one that would increase the UK's resilience in a volatile world.

Annex 1: Data citations

- Family Resources Survey:
  - Department for Work and Pensions, NatCen Social Research. (2021). Family Resources Survey. [data series]. 4th Release. UK Data Service. SN: 200017, DOI: http://doi.org/10.5255/UKDA-Series-200017

Annex 2: Spending commitments made since the Spring Forecast

Table 1 provides a list of policies that have been announced since the March 2026 forecast, their timelines, funding sources and impact on headroom in 2029-30.

TABLE 1: **There have been a number of new policy announcements since March that will add to the Government's spending challenges**

Current budget policies announced since the March 2026 Spring Forecast: UK

Policy	Cost and timeline	Funding source	Hit to headroom in 2029-30?
End rough sleeping	£442m over three years	From existing departmental budgets.	Assumed no. Government can add to spending plans temporarily without increasing total spending in 29-30, even if it is not clear why rough sleeping funding would end then.
£2 bus cap	£454m in 2027	From existing departmental budgets.	No, if temporary
Electricity VAT cut	£850m in 2026-27	Scrapping of the Digital ID programme.	No, if temporary
Business rates reduction	£100m a year from 2027-28	From reviewing business reliefs for anti-social businesses and cracking down on online marketplaces.	Yes
'Your First Home'	TBC	From existing departmental budgets, with contributions from developer fees.	TBC
Apprenticeship expansion	£100m over two years	From existing departmental budgets.	No, if temporary

Union Learning Fund	£15m	From existing departmental budgets.	No, if temporary
Inherited from the previous government			
Teacher pay deal	£1.6bn in 2029-30	Unclear	Yes
Defence Investment Plan	£1.7bn in 2029-30	TBC	Yes
Scrapping of Carbon Price Support	£200m a year	TBC	Yes
Extension of temporary cut to Fuel Duty	£210m in 2026-27	TBC	No, if temporary
Summer savings scheme	£300m in 2026-27	From closing oil and gas tax loopholes	No
	Potential hit to headroom:		**£3.7bn**

NOTES: Costs are as announced by the Government and have not yet been scored by the OBR. Headroom is measured against the stability rule in 2029-30. Measures marked "No" are either temporary or funded by reprioritising existing departmental budgets. The teacher pay deal was originally £1.1bn announced under Keir Starmer and topped up by £0.5bn under Andy Burnham.
SOURCE: RF analysis of HM Government, various; Economic and Fiscal Outlook, March 2026.

The Resolution Foundation is an independent think-tank dedicated to lifting living standards in the UK. We focus particularly on households with low and middle incomes; those on low pay or in precarious work; and those vulnerable to financial shocks. We also investigate fairness between the generations in our Intergenerational Centre.

We aim to provide rigorous analytical work, develop effective policy proposals, and use our expertise to affect direct change. We analyse the trends and outlook for living standards, including for different age groups, family types, and levels of household income and wealth, and seek to promote greater understanding of these. Our research focuses both on the specific areas of the economy that matter most for people's living standards, including work and housing; and on economic growth and productivity as the route to sustainably higher living standards. We also examine the role of government in improving living standards including through taxes, social security and public services.

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