DOES BORROWING PAY FOR ITSELF?

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November 2017

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John McDonnell, the shadow chancellor, recently claimed that further debt incurred under his treasury would "pay for itself", optimistically assuming that the fiscal multiplier would cover the interest and principal through higher tax receipts. Government borrowing has to be funded and if capital is not attracted domestically (reducing private spending), it has to be attracted from overseas. This increases the exchange rate and reduces exports.[1]

When Labour's manifesto and other spending commitments announced before and after the 2017 general election are tallied up, billions of taxpayers' money will be needed to pay for their programme: at least £273 billion would be spent on servicing the debt over the course of the parliament.

Key findings:

- Labour would spend an additional **£100 billion** in 2017-18 (on top of the current government's spending plans) and **£329 billion over the course of this parliament** when tax rises are included.
- By 2022-23, debt interest on Labour spending commitments would come to **£7.4 billion**. Over the six year period, Labour's extra spending would mean **£25 billion in additional debt interest payments**.
- Total debt interest would be **£272.5 billion** between 2017-18 and 2022-23.
- Debt interest per household over this period would come to **£9,461**.

Table 1: Labour Party additional spending commitments

Labour spending commitments	Annual spending (2017-18, £bn)
National Transformation Fund	25.00
Schools (Apprenticeship Levy change)	0.15
School counselling	0.90
Children's Health Fund	0.25
NHS	6.00
Social care	1.60
National Care Service	3.00
Cultural Capital Fund	1.00
Arts pupil premium	0.16
Scottish Investment Bank	4.00
National Investment Bank	35.00
National Education Service	5.60
Education Maintenance Allowance	0.54
Further education fees (adults)	1.40
Tuition fees (England)	9.00
Higher education maintenance grants	1.70
Extension of free school meals	0.80
Public sector pay rise	4.05
Total	**100.15**

[1] Booth, P., Hammond ditches the good bits, and keeps the bad bits of 'Osbornomics', Institute of Economic Affairs, 3 October 2016, https://iea.org.uk/hammond-ditches-osborne-shame-its-the-wrong-osborne-hes-ditching/

Table 2: Projected Labour Party tax changes, spending commitments and debt interest

	2017-18	2018-19	2019-20	2020-21	2021-22	2022-23
Inflation forecast (CPI, calendar year)	2.68	2.36	1.85	1.98	2.00	2.00
Extra spending	100.15	102.51	104.41	106.48	108.61	110.78
Extra taxation	48.10	49.24	50.15	51.14	52.16	53.20
Extra borrowing	52.05	53.28	54.26	55.34	56.45	57.57
Cumulative extra borrowing	52.05	105.33	159.59	214.93	271.38	328.95
Effective interest rate	2.38	2.24	2.19	2.16	2.19	2.24
Additional debt interest under Labour	1.24	2.36	3.50	4.64	5.94	7.37
Central government debt interest, existing plans	40.90	39.80	39.90	40.40	42.20	44.30
Additional debt interest	**1.24**	**2.36**	**3.50**	**4.64**	**5.94**	**7.37**
Total Labour and forecast central government debt interest	**42.1**	**42.2**	**43.4**	**45.0**	**48.1**	**51.7**

Methodology

- Spending commitments were derived from the Labour's 2017 general election manifesto and announcements about a National Transformation Fund, ending the public sector pay cap and a National Education Service.
- The effective interest rate, CPI inflation and central government debt interest figures are derived from the OBR's Economic and Fiscal Outlook November 2017 and Autumn Budget 2017.
- The extra taxation figure used is based on the Institute for Fiscal Studies' assessment of changes to tax receipts in Labour's 2017 manifesto.
- Extra spending and extra taxation figures are increased by the OBR's forecast changes to CPI inflation (calendar year).
- Public sector pay figure was the total public sector paybill in 2016 and increased by CPI inflation (calendar year).

Sources

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