The Chancellor's Challenge

Delivering a stimulus for post-pandemic recovery

Key findings

The progressive policy think tank

Key messages

- **Without a stimulus we risk being stuck in a 93 per cent economy, with large social costs.**

- **A £164 billion stimulus is needed in 2021/22 to return the economy to near potential by Spring 2022 and address much of the economic damage wrought by the pandemic.**

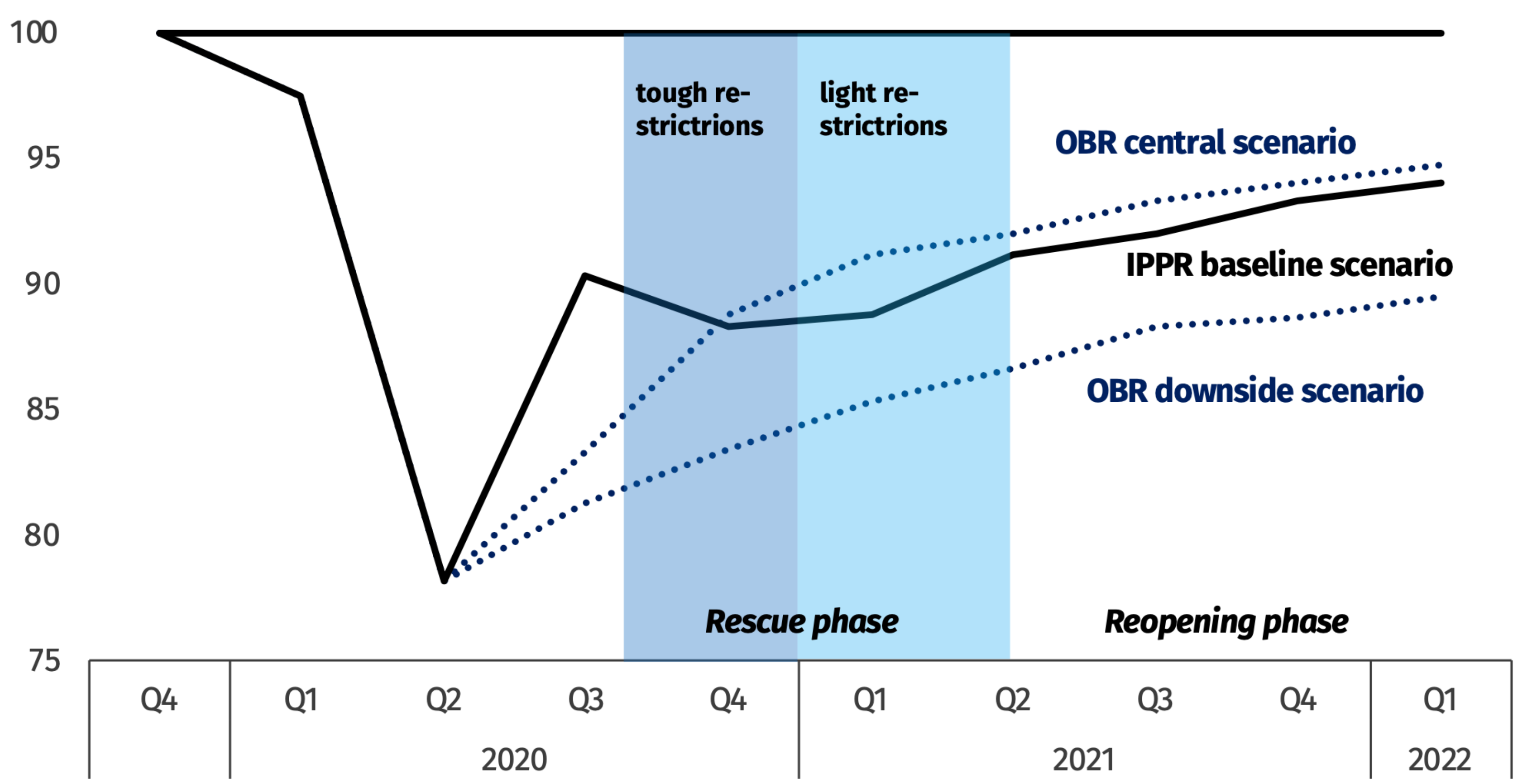
- **Through the stimulus, the government should invest in a fairer, stronger and green economy. Indeed, without this investment, the government will fail to achieve its own priorities on ‘levelling up’ and meeting the UK’s net-zero emissions target.**

- **Fiscal stimulus is fiscal responsibility. The proposed fiscal stimulus would pay off even in purely fiscal terms, with debt-to-GDP lower than without it.**

Growth will only recover slowly without support

Without further policy support the economy could remain more than 7 per cent below trend growth in 2021/22

Per cent of GDP (pre-crisis trend = 100)



Source: IPPR analysis of OBR (2020), NIESR (2020), IMF (2020a), Jung & Murphy (2020a).

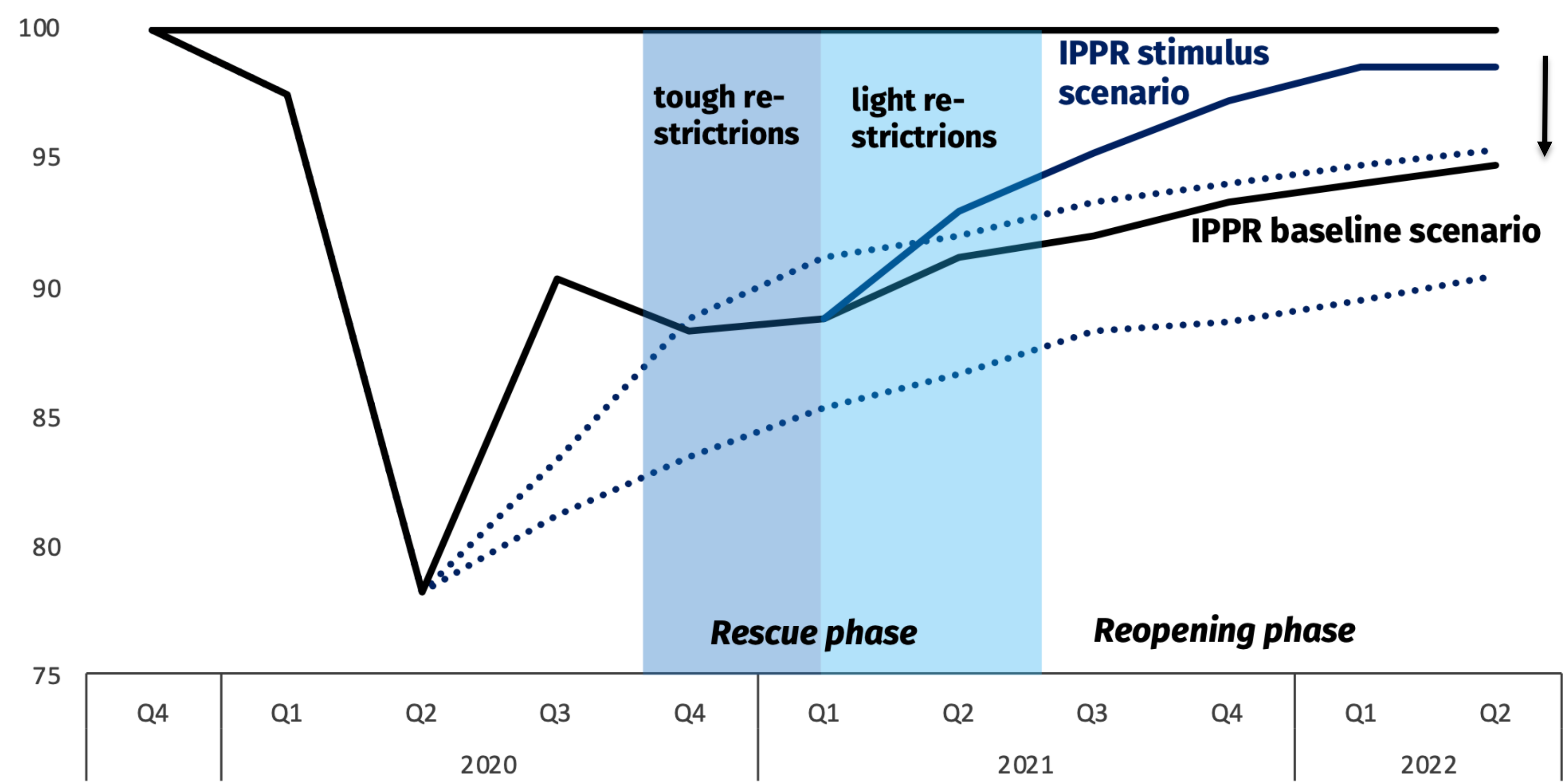
Without stimulus:

- Business investment and consumer spending will only recover slowly
- Scarring could mean economic potential remains significantly below pre-pandemic trend

Social and economic costs of inaction are high

A stimulus would return the economy towards potential much more quickly, producing jobs growth and tax revenues for the Treasury

Per cent of GDP (pre-crisis trend = 100)



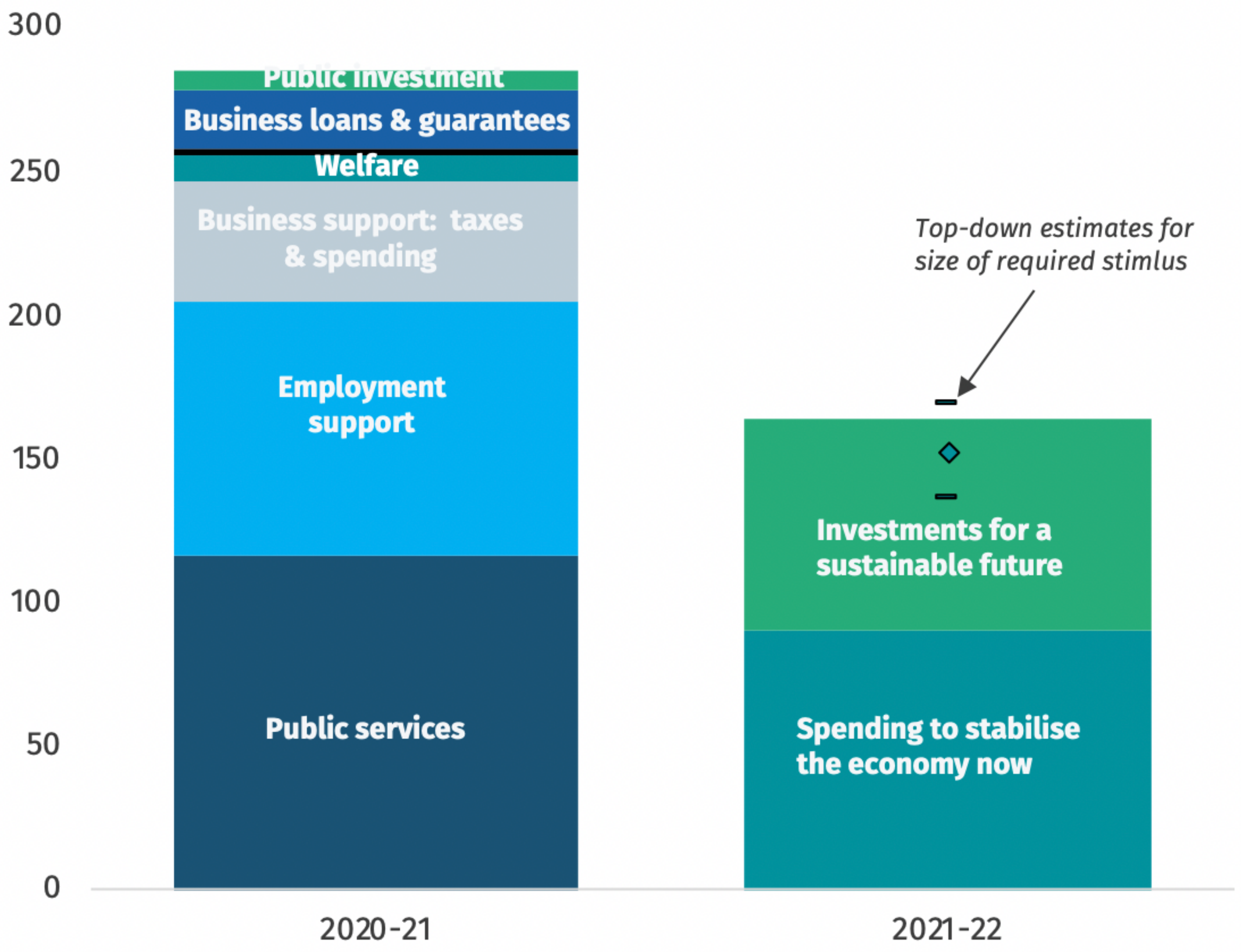
Without stimulus:

- 700k more children in poverty
- > 1 million more workers laid off
- Missed carbon emissions targets
- Debt 0.5 percentage points higher

A bold stimulus would have multiple benefits

Continued large stimulus spending will be needed to maintain GDP

Spending above March 2020 baseline (£ billion)

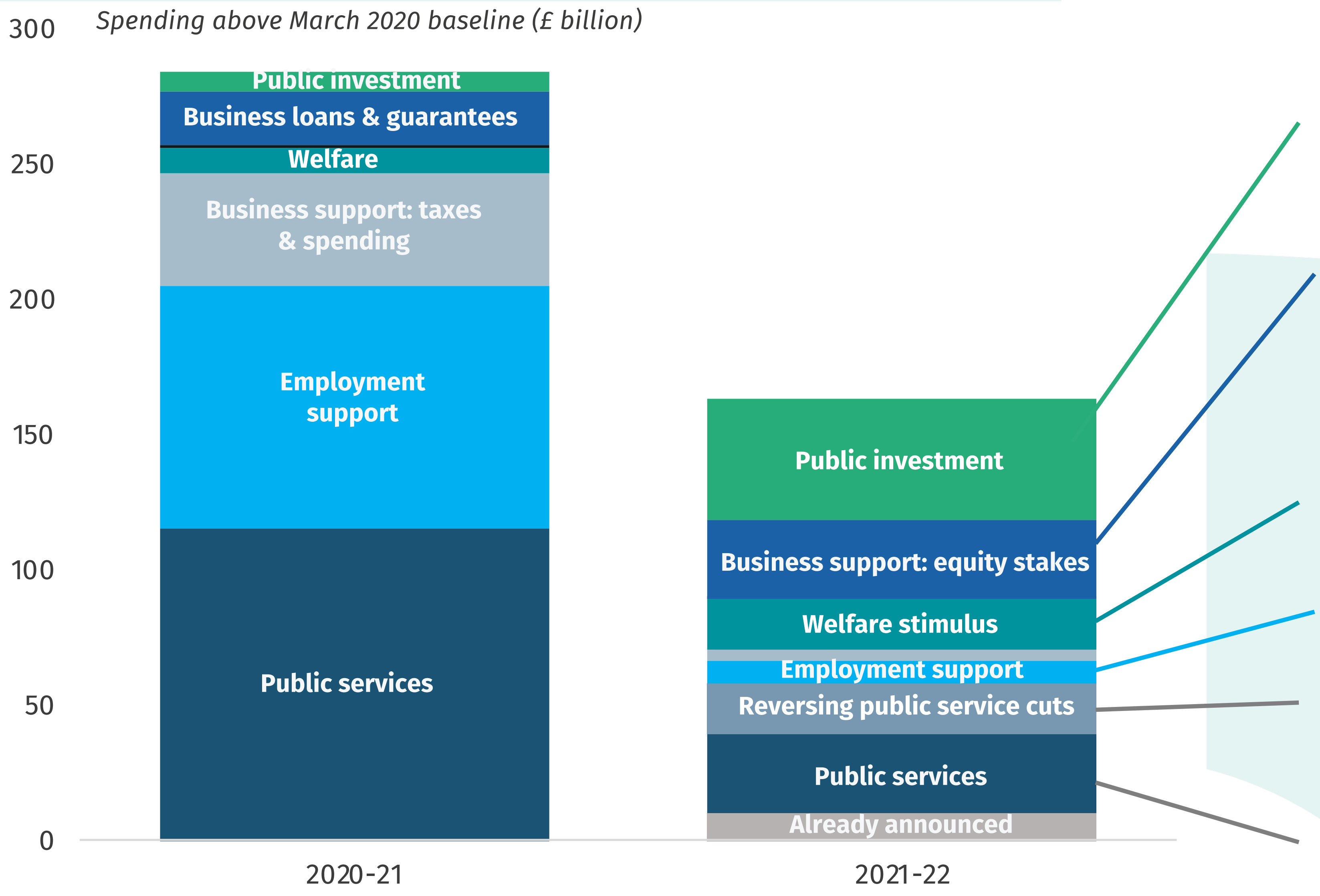


Source: IPPR analysis of IPPR baseline scenario (above), OBR (2020), IMF (2020a), HMT(2020a, 2020b, 2020c), Conservative Party (2019), Jung & Murphy, 2020, McNeil et al (2020).
Notes: The diamond marker on the right-hand side indicates the top-down estimate for the required size of the stimulus, based on the IPPR baseline scenario. The two other markers indicate how large the stimulus would have to be if growth in 2021/22 turned out one percentage point weaker (upper marker) or stronger (lower marker) than in the IPPR baseline scenario. As also shown in Figure 4, 'investments for a sustainable future' include public investment and public equity stakes, with 1-year multipliers below 1. 'Spending to stabilise the economy now' includes current spending with multipliers above 1.

A £164 billion stimulus would:

- Help bring GDP back towards pre-crisis trend
- Address scarring in the economy
- Put the economy on a sustainable trajectory, while preventing significant social hardship

A stimulus for a fairer, stronger & green economy



Invest in sustainable and social **infrastructure** to meet climate targets and boost long-term growth

Public equity stakes via **Project Birch,** to stabilise the balance sheet of viable firms

A **'family stimulus'** could lift 700k children out of poverty and raise GDP by 0.6%

A **work sharing scheme** to boost employment

Restoring resilience in public services by reversing cuts

Provide pandemic-related support for **health services, local government and devolved nations**

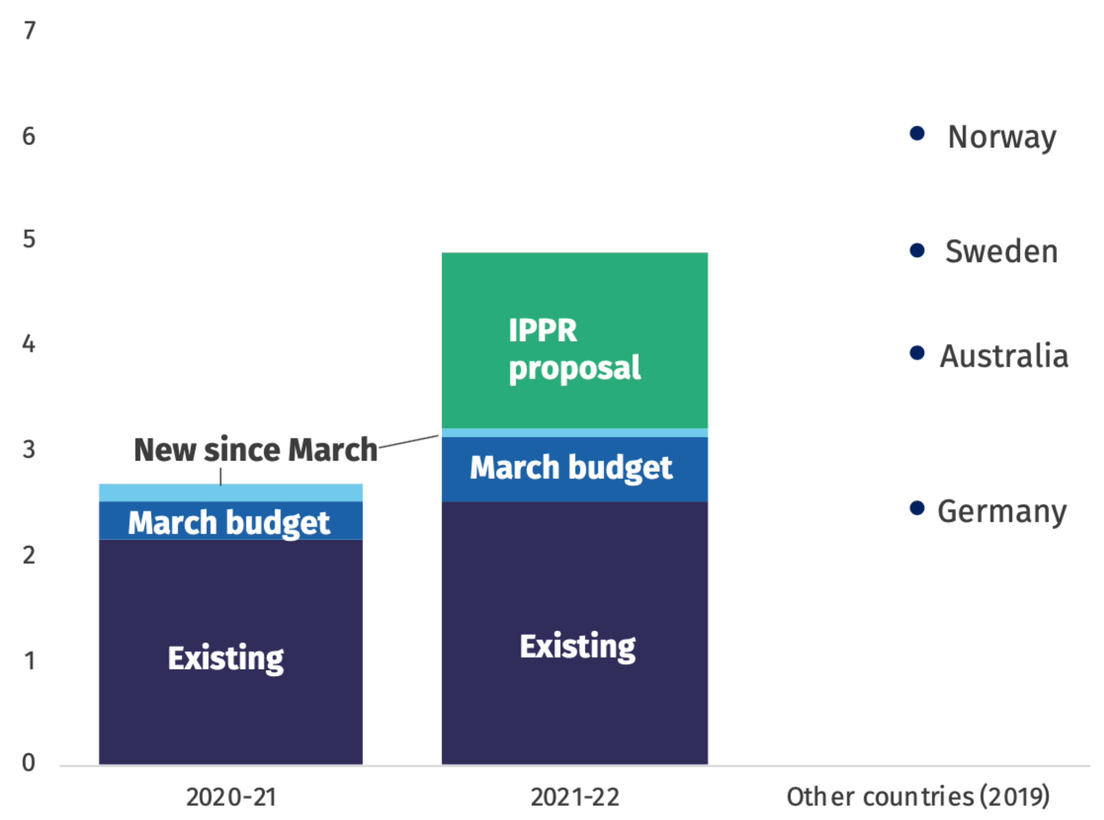
IPPR

The chance to usher in a new era of public investment

- **The UK could become one of the leading countries in high-quality public investment**
- Our proposed investment stimulus would add a further 1.6% of GDP in investment spending beyond already existing plans
- **Climate and nature areas of focus could be:**
  - Homes and buildings (£8 billion)
  - Nature restoration (£4.7 billion)
  - Transport infrastructure (£10.3 billion)
- **Beyond climate, the focus could be on:**
  - Investment in health and social care (£4.3 billion)
  - Pulling forward already committed funds on infrastructure and R&D (£6.5 billion)

UK public investment could rise to about 5% of GDP

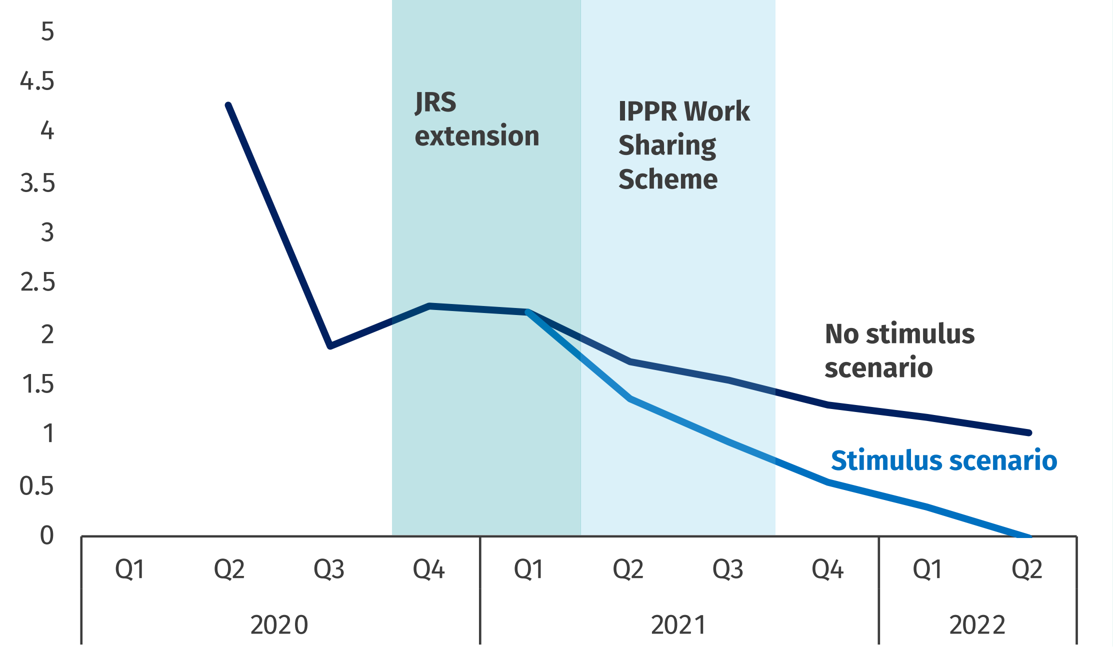
Public investment as a percentage of GDP



Supporting work sharing to boost the labour market

With a stimulus, the macroeconomic need for part-time work schemes would ebb in the second half of 2021

Workers requiring job support (millions)



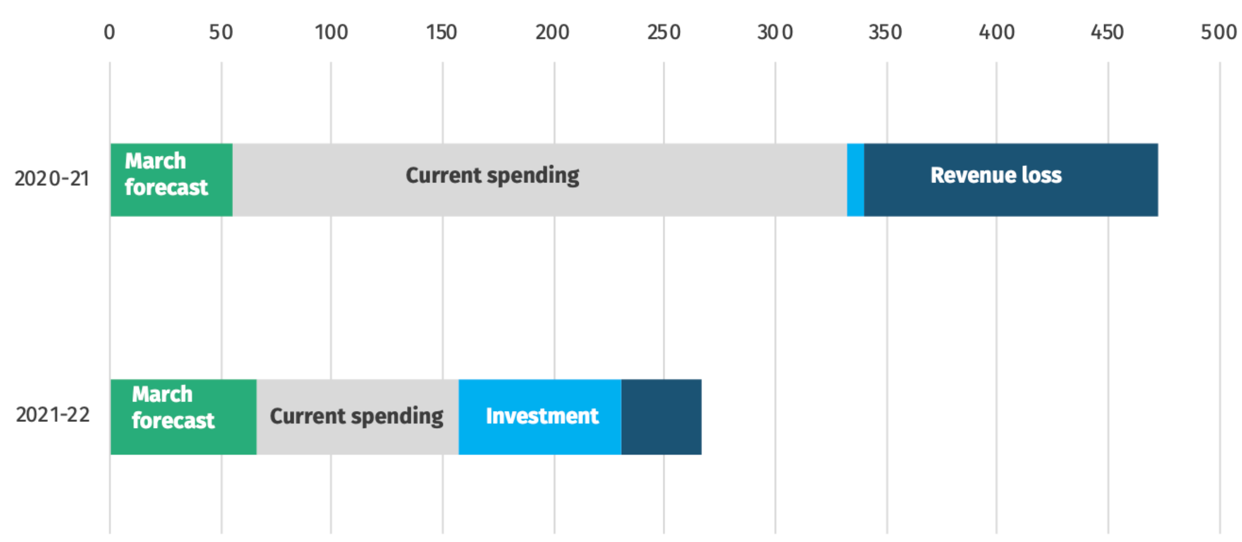
Source: IPPR analysis of HMRC (2020), IPPR baseline and stimulus scenarios and the methodology in McNeil et al (2020).

- **Introduce a part-time work subsidy of 10%, for all hours worked part time, in Q2 2021/22**
  - *This is based on economic first-principles: subsidise directly the activity that you would like to encourage (returning to active work on a part-time basis).*
- **Hours not worked would still be supported** as in the flexible JRS in September 2020, with 60% employer contribution
- **Open the scheme up to new firms, but introduce criteria for better targeting**
  - *Including minimum amount of hours worked*
  - *See McNeil et al (2020) - slide deck here*

IPPR

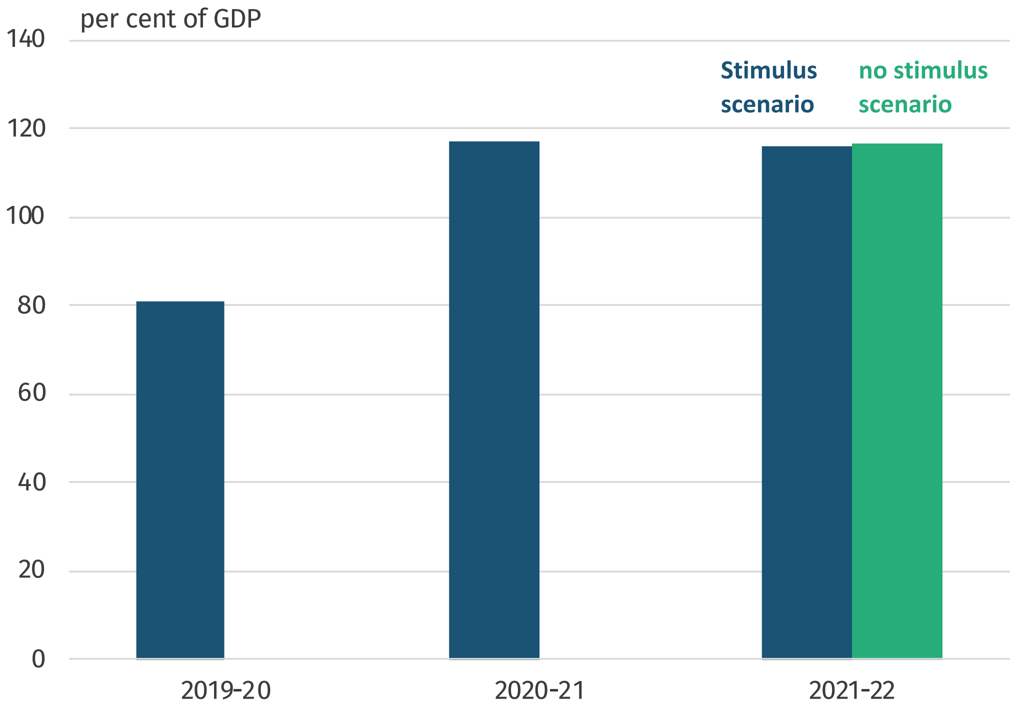
Fiscal stimulus is fiscal responsibility

In our stimulus scenario, overall borrowing is expected to decrease by 44% in 2021/22



Source: IPPR analysis of OBR FSR (2020) and same as figure 4.
Notes: The investment spending category includes public investment as well as public equity stakes.

A stimulus could leave the UK with a lower (not higher) debt-to-GDP ratio, as tax revenues and GDP will recover



The stimulus will have further fiscal benefits after 2021-22, as the investment multipliers rise significantly (to above 2.5) after 2 years, further increasing growth, according to the IMF (2020).