

## Will We Get a Productive Budget?

Episode release date: 18 November 2025

Host:

- **Bart van Ark**, Managing Director of The Productivity Institute and Professor of Productivity Studies at The University of Manchester

Guests:

- **Tera Allas**, Honorary Professor at Alliance Manchester Business School
- **Louise Hellem**, Chief Economist at the Confederation of British Industry
- **Stephen Millard**, Deputy Director of the National Institute of Economic and Social Research

**Bart:** A new fiscal event is on the horizon. Will the chancellor's budget bring higher taxes, deeper cuts, or more borrowing? Does the budget really matter for productivity? And how does productivity shape the budget? We're going to find out. Welcome to Productivity puzzles.

Hello, and welcome to the fourth season of Productivity Puzzles, your podcast series on productivity, brought to you by The Productivity Institute. My name is Bart van Ark and I'm a professor of productivity studies at the University of Manchester and the Director of the Productivity Institute, a UK wide research body on all things productivity in the UK and beyond.

Welcome to Productivity Puzzles, the second episode of the fourth season. Budget day is around the corner, and with it comes a new fiscal event for economists to sink their teeth into. But this isn't just about the numbers, it's also about Britain's collective purse. The Chancellor and other government leaders have repeatedly said that productivity is a key priority for the UK's growth agenda.

But the question is, will the budget help or hinder that ambition? Will public spending rise or fall? Will taxes move, and in which direction? And if after all the deficit and the national debt grow, what does that mean for borrowing cost lending and business investment? In this episode, we'll start with the big picture.

Why does the budget matter for productivity and why does productivity matter for the budget? And then after a short break, we'll dig into the details where public spending and investment should go. And the toughest question of all: how do we pay for it? And for this, I'm being joined by three fantastic guests who know the matter in and out.

First, I welcome Louise Hellem, chief economist at the CBI, the voice of UK business on policy matters, like the budget, and a member of TPIs governing council. Hi Louise, thanks for joining.

## Will We Get a Productive Budget?

**Louise:** Hi there. Good morning.

**Bart:** Second, we're joined by Tera Allas, who's an honorary professor here at Alliance Manchester Business School, and the chair of TPIs Advisory Board.

And Tera has a broad experience with policy and business positions and is well situated to look at productivity in the budget from different lenses. Hi, Tera. Welcome.

**Tera:** Thank you, Bart. Great to be here.

**Bart:** And our third guest is Stephen Millard, Deputy Director of the National Institute of Economic and Social Research.

The think tank is, of course, best known for its economic forecast, but also conducts thorough analysis of economic and social policy issues, including the impact of the budget. Great to have you on.

**Stephen:** Good morning Bart. Good morning everyone. It's a pleasure to be on.

**Bart:** Okay.

Of course, when we think about budgets, we think about the usual suspects, taxes, spending deficits, and surpluses and debt.

But first I want to step back and ask a bigger question. Why is the budget important for productivity?. Louise, in October the CBI submitted its views and priorities for the budget, and we'll provide a link to that, of course, in the show notes.

And, yes, as you say, some of that is about taxes, and we'll come back to that later. But what really caught my eye were the broader issues that you highlighted in that comment showing that the meaning of the budget goes well beyond just how much we tax and how much we spend.

**Louise:** That's right. I mean, I think if we go back to that question that you posed about why the budget matters.

So the primary mission of government is to increase growth. You know, the budget is the main event that the Treasury as an economic and fiscal ministry can use to think about its policy to increase growth. And, I think when we are talking about growth, what we really care about is about productivity.

And to do this, we know that we need to increase investment across the economy. So one of the things that we are really calling for in our submission, as you outlined,

## Will We Get a Productive Budget?

is some of those broader measures that can help increase productivity, increase investment across the economy.

And a couple of the big areas for that. Firstly, primarily thinking about actually how we can move quicker across the economy, around infrastructure spending. And it does appear to be over the last few years that it feels like we've forgotten how to build things in the UK. There's still a lot of bottlenecks in the system.

The government, I think, to their credit, have already done quite a lot in this space, but it's a very big issue in the UK and so we want to see measures in the budget for them to go further on that, particularly around reducing some of the barriers and bottlenecks in the planning system.

I think one of the other big areas is really about how to improve the skill system as well, and I think that is really important. Again, think about how we can increase the productivity of individuals in the labour market. And also really importantly, I think, tackle some of the issues we've got in the UK of actually bringing more people back into the workforce that are perhaps inactive at the moment. And that, again, is really important.

The third thing I'd mention, again at a kind of a high level, is whilst in the UK we've got some great areas where the UK has got some fantastic use of technology and AI, we are actually quite poor across the economy in diffusing that and making sure every business, you know, whether large or small, has got access to that kind of technology. So one of the other areas that we are calling for is a kind of national tech adoption strategy to really have a big push on that from the government and support for every business.

And the final thing that I talk about as well is in terms of enabling businesses to invest. Like you say, will perhaps come on to talk about taxes later, but some of the other costs that businesses are facing at the moment that squeeze their ability to invest.

And one of the examples of those is, is really high energy costs at the moment as well. So we want to see action from government on that. And that would also really. Increase our competitiveness in the UK compared to some of our international peers, particularly the EU.

**Bart:** That's a really big agenda, but what really sort of strikes me in the UK compared to other countries, that when the budget comes it really becomes much bigger than just, you know, the fiscal picture. And that's quite striking. In other countries it would just be setting the scene for the fiscal side and then plans would be developed here.

But it seems here the budget is a big event for the economy as a whole. Any reason why you think that is for the UK?

## Will We Get a Productive Budget?

**Louise:** So I think it's quite interesting where the kind of treasury sits in that government apparatus in the UK that it really is seen as that kind of central government department, is the one who obviously holds the purse strings for a lot of the spending and the investment that needs to happen.

So I think that's where obviously lots of announcements come outside of budget events. And actually this year we've had quite a lot from government in terms of big macro strategies like the industrial strategy. But the budget often is the kind of pivotal event where particularly I know the treasury - and having sat on that side of things in a previous life as well - really tries to look across its policy on kind of growth across the board and tries to make some of those decisions where they're balancing some of these different options as well. So I think that's where it becomes that kind of central decision making body.

**Bart:** So, Stephen, let's bring you in. Louise emphasised the importance of the budget for infrastructure, for skills, for technology, diffusion, for competitiveness. Is that the sort of things that you would also be looking at. Or do you see other things as well where the budget really matters for the productivity agenda that we have in the UK?

**Stephen:** It was good to hear Louise emphasizing the importance of public investment. That's something we've strongly emphasized over the past few years. And in particular, the extent to which public investment can crowd in private business investment. And business investment, we definitely need more of that in the UK if we're going to get higher productivity growth.

And another thing, of course, that really affects business investment is uncertainty. And we are very much hoping that this forthcoming budget can actually reduce the amount of uncertainty that we've seen of late. And the chancellor can do that we think by creating a bigger buffer against her fiscal rules so that she won't then have to make policy changes mid-year, as has been the case so far.

**Bart:** Yeah. So Tera, let's pick up on that topic of uncertainty because you talk a lot about that, how important it is for businesses to, you know, see that kind of stability in the government agenda. Do you want to build a little bit on that, on how to what extent the budget can help to create that?

**Tera:** Yes, and first of all, I think it's in exactly the ways that both Louise and Stephen have already outlined. If there's a credible long-term plan to raise the productive output of the country, then that sort of seeps into the tone on the business environment and the sort of sentiment within which businesses then make decisions about investments.

I would like to add a couple of nuances though. So in terms of public investment, totally agree that where we can remove growth bottlenecks and crowding private sector investment, that's incredibly powerful for productivity.

## Will We Get a Productive Budget?

But it is a very granular job, so it's not just any kind of transport investment, or any kind of energy investment, or any kind of digital investment, or any kind of skills. The UK, like any other country, is extremely place-based. You know, businesses and workers are based in specific localities and geographies.

And there needs to be an exercise that really targets the investment into those places where there is growth potential or where there growth bottlenecks and really delivers quickly, as Louise says as well, with credibility and with sort of a determination. So one of the things about the industrial strategy that I think is really promising, it takes a 10 year view and therefore it should provide this kind of stability and a clear plan.

But it now needs to be delivered. So if - I think they said they have 150 different measures across 20 departments - if they somehow start stumbling in terms of delivering all of those measures, then the credibility will be gone.

And so taking a step back to the budget here, I think it really sets the tone for whether the government is actually delivering on what it's saying and being growth focused. Or whether there are lots and lots of other objectives in the mix as well. And if the latter is the case, then we are not going to end up with a clear narrative and a clear impetus for investment.

**Bart:** Louise, do you think there is enough confidence that, for example, an agenda like industrial strategy, which Tera just referred to, is sufficiently tied in with the budget? Or is the budget still too much short-term looking where some of the other government plans, to Tera's point, are much more long-term oriented?

**Louise:** So I think they are complimentary. I think the budget to some extent will be a little bit more short term focused. But I think where our big message to the government is around seeing all the decisions that they make at the budget through the growth lens, then that does obviously mean they need to think about what is the impact of the decisions that they make on the long term.

I mean, I think an example of that we saw in the last budget, where the chancellor faced a similar dilemma about how to make the kind of fiscal position add up, was that she continued with, and actually increased that capital investment from the public sector. And now, that is something in previous years when chancellors have faced this dilemma, they have cut. That has meant that it's easier to make those sums that up on the day of the budget. But we know that has a negative long-term impact on exactly the type of thing we're talking about on investment, on productivity.

And so I think that if we can see more decisions like that where actually perhaps they're taking a decision that might be harder in the short term, but it's positive for that long-term growth and long-term investment, then I think that, you know, that is what we want to see.

## Will We Get a Productive Budget?

But that is quite difficult to do given some of the political and fiscal challenges that she's going to face.

**Bart:** Yeah. Just very quickly before we move on. There is this issue, of course, that the chancellor, right, is concerned about that, you know, this might influence the debt situation of the UK, which is gradually creeping up. To what extent - and obviously she is concerned about that also from a perspective of the markets - to what extent would rising debt be an issue for investment. Stephen, would you want to comment on that - and therefore, for productivity?

**Stephen:** The channel works through interest rates. So as debt increases in the financial market, participants get a little bit more worried. They increase the premium, the interest rates on government debt, and that then feeds through to interest rates throughout the economy. It raises the cost of capital, it means investment is more expensive and again, less investment in the corporate sector in the business sector, less productivity growth in the longer run.

**Bart:** It's a difficult balancing act, that's for sure. Now let's move on to the other part of the story here, and that is why is productivity important for the budget?

And, normally we don't really think too much about this. But this time it's getting a lot of attention because the Office for Budget Responsibility, which is the government's independent forecast, is expected to revise downwards its projections on productivity growth. And that seems to matter a lot. A lower productivity outlook would mean less fiscal headroom for the chancellor, and that could really shape the choices that are going to be made for the budget.

So, Stephen, can you walk us through this a little bit? Why do these productivity forecast makes such a big difference? What does that mean for the numbers behind the budget and what's your own outlook at NIESR? And we'll make a link to your own outlook as well in the show notes. How does that actually look at that compared to what the OBR is predicting?

**Stephen:** If I get to the OBR and NIESR, it's worth just thinking about what government debt sustainability means. We were talking about the debt-to-GDP ratio creeping up and the financial markets reaction just a minute ago. But a good way of bringing down the ratio of debt to GDP is for GDP to grow.

The faster GDP grows, the easier it is to get that debt to GDP ratio down. And so that's why growth is really important. And also from the point of view of the budget deficit: if growth is higher tax revenue will be higher and the government will find it easier to fund the spending that they want to do.

Now, the OBR back in March forecasted growth in the latter half of this parliament of 1.8%. That's GDP growth. Many commentators including us thought that was a little



## Will We Get a Productive Budget?

bit too optimistic. And indeed it appears that the OBR themselves now think that that's too optimistic and they're likely to revise it down.

And that really matters. If you're trying to calculate what the budget deficit is likely to be at the end of the parliament, which is the fiscal rule that the government has set itself. So calculations that we've done, others have done, suggests that for each 0.1 of a percent of GDP growth in that sort of latter half, if you like, of the parliament, that translates into something like 10 billion higher deficit.

**Bart:** And a lot of that decline in GDP growth is driven by lower projections on the underlying productivity performance, right?

**Stephen:** Exactly. So you can think of, just in an accounting sense, GDP growth comes from growth in the labour force and growth in labour productivity.

So growth in the labour force, we pretty much rely on the ONS's best predictions for population growth, which we understand quite well. And for immigration, which we understand less well, but you know, we have a calculation for that.

But the rest of GDP growth comes from labour productivity growth. So if you revise down your view of labour productivity growth, you get lower GDP growth, you get a higher budget deficit five years out from now.

**Bart:** Wow. And then for every 0.1 percentage point, 10 billion, that makes a huge difference.

Now, Tera, how confident are you about these productivity projections? I think I've been a little bit in this business as well myself and, you know, projecting and forecasting GDP - and Stephen knows this himself - is hard. But forecasting productivity is even harder. And the stakes are very high. So to me there, it feels a little bit uneasy that we're making these adjustments without exactly knowing whether we're doing this right or wrong.

So how much confidence do you have?

**Tera:** So you're quite right. It is incredibly difficult to forecast productivity because it is influenced by so many different factors globally and locally. Technology policy, even sentiment have big implications for whether people invest and change their business processes or not.

However, I think in this case, when the OBR forecast for 2029 is around 1.3% and what we've actually seen, 0.5% productivity growth for the whole decade between the financial crisis and COVID. And since COVID, essentially you could argue we've seen either zero or negative productivity growth. A 1.3 number just doesn't feel a sensible anchoring point.

## Will We Get a Productive Budget?

Now, there are all kinds of reasons why you might think: OK, productivity growth very recently has been very bad, but it should bounce back. There are all sorts of arguments for why that could be the case. But we are not seeing extra investment flowing into the economy at a degree or at a quantum that would allow us to believe that it's really going to be 1.3.

The one wild card is around AI and technology. And I actually do think that in the kind of medium-long run, it will be absolutely transformational for labour productivity, and it will drive creative destruction as well in a way that will allow more dynamism and better productivity growth. But is it going to be in the next five years, which is roughly the OBR forecast horizon? I don't think we can be reliant on that.

So realistically a downgrade, I think has been overdue. And as Steven has said, it has huge implications for the budget. But really, honestly, the government and its advisors should have known that already like literally years ago. We've seen this kind of issue with the OBR forecast for years now, and so that should have kind of been part of their thinking already.

**Bart:** Building what Tera is saying. I'm sure a lot of your business members would indeed agree and say: look, this is really weird. In this sort of era of huge technological change and AI and everything else. Lots of businesses are saying we're actually massively raising our productivity and there's lots of opportunities.

Is this the right time to adjust the budget downwards? Now, to some extent it's a matter of numbers. I think Tera is right: the gap is very big between 1.3% productivity to 0.5. So maybe it has to come down. But again, the stakes are high. The implications are big for investment if we adjust it downwards too much.

So how are your business members looking at this? I mean, when they hear the government saying, we're going to bring our productivity forecast down? Do I feel good about that?

**Louise:** Well, no, I don't think anyone feels good about it. I mean, I think it is ironic in a way, as Tera says that, you know, I think there is hope that after this very long period of low productivity, there is perhaps hope on the horizon that things will pick up again. Particularly if we are able to take advantage of those developments in AI and in technology.

But as she said, those are not going to come, you know, tomorrow or within the next year. That, you know, is a longer build thing. And as she said, I think, you know, we have known about this problem of low productivity in the UK for a long time. It's, you know, it's been relatively stagnant since the financial crisis.

So in many ways, again, it's a kind of bad luck almost for the chancellor to be the one in the hot seat when, when the kind of music stops on this. But it has been a known issue, uh, and I think it's something that the OBR has been looking at for a



## Will We Get a Productive Budget?

number of years. And I think this is obviously the budget where they are going to make that change, and it is going to make things much more difficult for the chancellor.

And it has created that mood of kind of lower confidence across the business community because they know that it means that we are looking at either more spending restraint or, what is most probable, those rise in taxes, which potentially could hit them and make it harder to do the investment that we know is needed to increase productivity.

**Bart:** So Stephen, how much would you now expect the trend growth, as we call this, it's the long-term growth prediction of the economy. How much do you expect it to be downward adjusted? And what would that mean then for the fiscal space the Chancellor has?

**Stephen:** Yeah, well, I mean our view is that trend productivity growth will be around about 0.6 or 0.5, something like that moving forward. As Tera said, the OBR were at 1.3. I don't think the OBR will come all the way down to us. I think politically that will be very difficult for them. And you know, they will run an argument along the lines of: we are beginning to see a little bit of a pickup with AI, et cetera.

So I reckon they'll probably pull down to about one. That'll be a 0.3 percentage point move. And that represents 30 billion in terms of extra money that the chancellor, if you like, has to find. It would move, for other things equal, from having 10 billion pounds headroom to being 20 billion pounds short against a fiscal rule.

Now, on top of that, we very strongly feel that the chancellor needs to build up much bigger headroom than she had. And indeed the fact that the OBR's change in their trend rate of growth, the fact that that's had such a large effect is partly because the chancellor has so little headroom against her fiscal rules to begin with. If she'd have more headroom, she would've been able to absorb more of that downgrade of growth.

**Bart:** Yeah. So, and that's actually a really nice segue into what we're going to talk about after the break, because it means she will have to take action one way or another in terms of dealing with her spend and her taxing plans.

So we're going to talk about that a little later. But before that, let's first take a moment to hear what else is happening at the Productivity Institute.

**Ad:** The Productivity Institute aims to pinpoint why UK productivity has flatlined and how to create the foundations for a new era of sustained and inclusive growth. Visit our website at [productivity.ac.uk](https://productivity.ac.uk) to find research covering topics such as business investments and innovation skills and further education, foreign direct investment and trade.

## Will We Get a Productive Budget?

And the transition to net zero on our website, you can find deep dives into how leaders can improve productivity within their firm or public sector organization. While you're there, sign up to our newsletters for regular updates on what productivity means for business workers and communities, as well as the latest on how productivity is measured and how it truly contributes to increased living standards and wellbeing.

The Productivity Institute is a UK-wide research organization funded by the Economic and Social Research Council.

The Productivity Institute: Productivity Together.

**Bart:** Welcome back to Productivity Puzzles, and in this episode we're discussing the upcoming budget with Louise Hellem, Tera Allas and Stephen Millard. Now as promised let's go into some of the details, and let's start with the spending side.

We've talked a lot in previous episodes about the importance of investment because it is well evidenced that Britain has chronically underinvested in almost everything from physical to human capital and so on. And that has a huge impact on productivity. And public investment, which is basically within the chancellor's purview, in health, in education, infrastructure.

It all clearly matters, but perhaps it's not just about throwing more money at the problem. So, Tera, let's go to you first. What's your take on public investment and spending. And if we need to increase spending, how should it be prioritised?

**Tera:** Yes. Extremely important question. I think this is more about the mix of what we spend, how we spend it and where we spend it, than it is necessarily about increasing the total amount. Because we are hitting up against some thresholds there in terms of being able to, you know, growth enhancing ways to raise more money.

Taking the total government expenditure in the last year of the Spending Review, and looking also at what might be spent on the so-called annual managed expenditure - which is the less easily forecasted expenditure - the government's capital investment is only about 12% of that total. And to me that feels like there's, you know, essentially too much money being spent on day-to-day and too little money being spent on investing in ways that would drive up that trend rate of growth that we talked about.

And then even if we look at the CapEx, that is going to be spent or is being planned to be spent, quite a lot of it is for important objectives like defence or for health, that are not directly necessarily going to enhance growth. And as we discussed earlier, the sort of things that typically enhance growth directly are things that take away growth bottlenecks from private sector businesses. And that's typically things like housing and transport, digital infrastructure, energy infrastructure. And only about a

## Will We Get a Productive Budget?

third of the CapEx in the spending review is expected to go towards those kinds of things.

So the mix of investment is important. And then as you used the word prioritisation: even within each of those categories that I mentioned, there are going to be places in the UK where allocating some money will absolutely unleash massive private sector investment and growth because there's potential there. There's almost like a bottleneck or, you know, growth is being held back by other barriers. And then there will be other places where it isn't going to do that. And it's going to be critical to be quite disciplined about that prioritisation.

The final point I'll make is, of course, none of this is enough if you don't also take away bottlenecks in the planning system and in the permitting system and in the regulations. So you want to sort of package of things which include both more investment in growth enhancing things, and then more deregulation, such that all of that private sector investment can come forward quickly as well.

**Bart:** So, Louise, when I heard you talk earlier in the podcast about the priorities for the budget, it also sounded to me that you were more focused on the delivery than on the necessity to invest a lot more. I mean, as much as you would like to invest more, the priorities you gave on infrastructure and skills and everything sounded to me also much more like you want better delivery. Is that correct?

**Louise:** Yeah. I mean, I think obviously both are important, but I think one of the issues that we've got in the UK is, even when we pledge that spending is going to happen or investment is going to happen both from the public and private sector, that we are quite slow to actually see that delivery on the ground.

And a lot of that, like we've just talked about, is around bottlenecks in the planning system. So I mean, one of the very practical asks at our budget submission is to have more planners within kind of local authorities to make sure that we get applications in quicker through the system. Actually, again, that's potentially another area for kind of a simple request, the way you could bring AI in to help with some of those bottlenecks as well, potentially.

And I think one of the other important things in this space is thinking about where perhaps the government's finances are constrained. Where can we have those opportunities for more kind of public-private sector partnerships as well where you can crowd in private sector investment to help achieve some of the government's aims and ambitions.

And, actually, that was one of the things again, that the government said it was open to thinking about more in the 10 year Infrastructure Plan, particularly in kind of revenue generating areas of infrastructure spend. And we think actually there is more scope for those kind of agreements going forwards. And a lot of that is about

## Will We Get a Productive Budget?

just having the right contracts, having the right balance of risks across the public and private sector to make sure money is coming in to the most kind of productive areas.

**Bart:** Stephen, let's quickly pick up on this crowding in, crowding out. It's come around a couple of times and we, economists, love to talk about this stuff. But it's tricky, right? Because the OBR is actually assuming that in the first few years, public investment is actually crowding out. So it's actually reducing private investment and only later on it's crowding in.

So what you're thinking about that kind of argument, how confident can we be that that public investment does lead to more private investment to the public-private partnerships and so on that Louise is talking about. What's the evidence?

**Stephen:** Yeah. I mean, the evidence such that it is, is mainly based around infrastructure spending. They, the things Tera and Louise were talking about, where it's transport infrastructure and housing infrastructure has all been developed together in such a way as to make it easier for firms to do business, to, to grow, et cetera. That's where the evidence is.

But the problem is that it takes time. And, you know, the current fiscal rules, which are based around bringing the debt-to-GDP ratio down in five years, act as a disincentive to public investment. Because the crowding out effect, if you like, of higher interest rates, that will happen within that five years. Whereas the crowding in typically is much longer.

As Louise said, if we can speed up the process of public investment, that will help. But even then, even if you build an airport in three years, it will still take more years for the big benefits to arrive.

I talked a little bit about this in my chapter in The Productivity Institute's *Joining Up Pro Productivity Policies*, which actually I would recommend to anybody to read. A lot of very good ideas. My suggestion there was that to deal with this sort of bias, if you like, against public investment, and Tera's point about public investment being a too small a proportion of total government spending, is to actually set a minimum of say 15 or 20% of public spending has to be investment spending. But then of course you also need to make sure that it's the right kind of infrastructure spend.

**Bart:** Yeah, so Tera, Louise mentioned the need for speeding up planning approvals, particularly at the local level. That's one way to actually get that crowding in earlier. Do you have other ideas about how can we that crowding even happen faster. Because, you know, we have no time as we have already been discussing in terms of all the downward adjustments, we need to get to growth up sooner rather than later.

**Tera:** I think an awful lot of it is about the delivery and confidence points that we've already made. Businesses will invest if they see an opportunity and there are not,

## Will We Get a Productive Budget?

you know, unnecessary or kind of unreasonable barriers in front of them. And an awful lot of business investment actually has less to do with, you know, what's happening with interest rates and and so on, and more to do with just the confidence that the market is going to be growing.

And so I think, here government already has various different levers that it does pull. It can use procurement, for example, as a way of signalling the sort of pipeline of investment it's going to do. And that then creates demand for businesses further down the supply chain. It can use export promotion to get more businesses to think about exports. because of course that size of the global market is massively bigger than the size of the UK market. So for businesses in services or goods that are exportable, there are opportunities there.

So there are actually quite a lot of levers that government can potentially pull. I think the idea in the industrial strategy was to try and align all of those levers so it can be a bit more focused around a couple of sectors and a couple of specific types of businesses where the UK has a comparative advantage. And that seems to be imminently sensible. We should build on our strengths and really amplify them and turbocharge them, if I use that terminology.

But now it comes to actually delivering it all. I think the government could also just talk about it a bit more. I have a feeling that they are delivering on some of these things. They're delivering on a bunch of some of the reforms that they've mentioned and many things in the industrial strategy. Well, talk about it so we all know about it and other businesses know about it too. Because that is there to build that long-term confidence in the economy.

**Bart:** Yeah. But it does indeed come back to, and you know, Stephen referred to the Joining Up Pro Productivity Policies document that we did. It comes to joining up of these various policies and the extent to which we are actually able to do this. And that's quite challenging

Now, Tera, before we move on, you are also co-chair of the Health Foundation's Productivity Commission for the NHS. Now that's a big part. A lot of that is spending, not necessarily investment. But again, this is a top priority for government. It will be important for growth. You just published a piece there on productivity. Any insight from that will be useful messages for the budget process.

**Tera:** I think this broad idea that we need to spend more on the NHS is misleading and is potentially quite dangerous. What we know about NHS and the general kind of health sector productivity is that it has done even worse than the overall sort of aggregate productivity in the UK. And the ONS for example, says that productivity in 2024 was 7.8% less than in 2019. That's a huge drop and it's continued to decline in 2025.

## Will We Get a Productive Budget?

So here too, I think it's about the mix of how we spent the money, not adding more money. And, in fact, some of the problem over the last five years is that we've spent more money and we've procured more inputs into the system, but they have not turned into better outputs or better outcomes. So that by definition means we've worsened productivity by adding more inputs without actually then figuring out ways to turn that into outputs and outcomes.

We do know from our work, and many other people's work, that capital investment in the NHS has been much too low relative to what you would expect to be a kind of optimal point. And so, by definition, if nurses and doctors, and administrators in their NHS don't have the right equipment, don't have the right estate, don't have the right IT to work effectively and efficiently, then their productivity is going to be dragged down. So probably there too, there's a mixed issue of a potentially spending more on capital and then, again, spending it on the right kind of capital in the right places where the bottlenecks are in the system.

**Bart:** Prioritisation, is again an important topic here and maybe we should do a separate podcast on productivity in the NHS.

But let's go to our last segment and that's really trying to tackle the big question, and that's how do we pay for all of this. If the chancellor ends up with a bit more fiscal headroom, which would be good, but at the same time a lot of challenges in terms of growth, what does that mean for taxes and spending?

And Louise, nobody loves taxes, certainly business not. Who does? But some taxes hurt more than others. Which ones will have the biggest impact on business performance and what would perhaps be a little bit more growth friendly, or perhaps even a growth enhancing tax system look like? And how would the mix be improved to support productivity in your view?

**Louise:** Yeah, so I think it's almost inevitable that we are going to see some tax rises in this budget. I think recognising that difficult fiscal position that the chancellor faces and the importance of making sure we do have the public finances on a sustainable footing, and what that means for kind of market confidence.

I think that the conversations that we've had with the chancellor and with the wider treasury team when it comes to taxes, are really about having a coherent strategy. Not just kind of raising revenues in the short term, but really thinking about the impact of their decisions.

But also where you can kind of tell that story of what they're trying to achieve. You know, why is it that we've got the taxes that we have in the kind of system that we have, which at the moment is a very overly complex system. So it's thinking about any increases that they have, can you do it at the same time as maybe taking that wider approach to the system.



## Will We Get a Productive Budget?

And thinking about how you can simplify things and align people's incentives more to the behaviour that you want to see. Like making sure that you don't take any decisions that damage their investment incentives. And I think that's particularly why we are concerned at the moment about the level of tax on business, about the level of cost that they're facing on the back of particularly the increases in national insurance contributions. Last year in the budget, we have seen a reduction in confidence for businesses. We have seen them pause or pull back on investment decisions. And those increases meant that we've got tax rates at kind of a 25 year high for businesses.

So, I think what we should really do is think about those areas of the tax system that we know, again, are very overdue for reform. Some of these issues within the tax system are well known, particularly around property taxes. And again, in terms of the speculation that's out there, many people will have heard things around stamp duty, around council tax. You know, business rates is a big issue for us and our members as well around some of the distortions in the systems there. So I think the best thing that we can do is to think about how we can improve that system and remove some of those distortions.

And I think then, in terms of if there is more revenue that needs to be raised, it is thinking about how you can do that in the way that has the least distortions possible. And I think, unfortunately for the chancellor one of the areas that we think she should be considering is probably around income taxes being a very kind of broad based measure. But obviously that comes up against the government's manifesto commitments to not increase income taxes as well as around VAT as well. So I think, again, that's where there is quite a lot of difficult decisions here.

And I think quite often people talk about weighing up the kind of economics and versus the politics on this, and I can understand why people say that. But actually I think it is around weighing up that in the short term versus the long term. Because actually if you make some of these decisions in the short term that you think might be politically easier, but have that kind of more negative economic impact that is going to make everybody worse off in the longer run.

When you look at the government's primary objective around increasing growth, increasing living standards, you know, that will be harder to achieve in the long run if they perhaps don't make some of these more politically difficult decisions in the short run.

But, yeah, I think that there's not an easy set of choices there, particularly when they do look at increasing taxes that will have impacts throughout the system.

**Bart:** Stephen, you did some really interesting analysis in the last economic outlook on how different taxes are impacting on on growth. So can you quickly take us through where we might see the biggest damage or the biggest plus from these changes in the tax system that Louise is asking for?

## Will We Get a Productive Budget?

**Stephen:** Louise has said absolutely everything I would say on this. What the chancellor will need to do, she'll need to raise quite a bit of money. The most efficient way of doing that is to raise income tax. And we found in our analysis that actually rises in income tax over the medium to longer term do not have such a negative impact on GDP, particularly versus raising taxes on businesses which has a very bad long-term effect, and raising VAT, which via its effect on inflation leads to higher interest rates in the short run, has a very bad effect in the short run, but also is extremely regressive and so from a political point of view would not be good at all.

So we would very much argue that if you need to raise a lot of money, you do it via rises in income tax and the GDP hit resulting from that would not be so bad. The real worry in our heads is that she will attempt to raise as much as possible by making the tax system more complicated by taxing a little bit more here, a little bit more there, and that, as Louise said, in the long run just makes a complicated system even worse.

**Bart:** So, Tera, let me throw the really difficult question at you. As we've said, there's economics here and we find it fairly easy to agree on that. I'm sure you do on what Louis and Stephen said. And there's politics and there's vested interests and all those kind of things.

So if you were the advisor to the chancellor, what would you advise her to sort of navigate this? There's clear economics. There's politics which are unavoidable and there's lots of vested interests. Nobody likes taxes, but there are different groups in society that don't like particular taxes that do like them. What's the way forward?

**Tera:** That is indeed a really challenging question. I think Stephen and Louis have already hinted at a lot of the elements of it. Having a clear strategy of reform that explains what you're going to do, why you're going to do it, how long it's going to take, and when you will see the benefits is the first starting point.

Especially, being honest about the fact that in the short term, there will be people who might not like those changes. That's inevitable. That's the nature of human life. That's the nature of any democracy. And I think over and above of that, thinking about whether you can think, come up with kind of packages of reforms that ease that pain a little bit.

So I used to be Chief Economist at the Department for Transport. I think there definitely is a kind of deal with the motorists to be had, which both stabilizes tax take from roads, road usage, car usage, you know, future electric vehicles, and doesn't make that change so terrible in the short term.

But somebody needs to work through that package. It's not going to be a single thing of, yet again, you know, not raising the fuel duty or changing something about electric vehicle taxation. It needs to be a kind of whole package of reforms aimed at,

## Will We Get a Productive Budget?

both in the long run having a sustainable tax take from those activities, and in the short term helping people over what's going to be a potentially painful change.

**Bart:** Yeah. Surely what we've heard throughout this podcast is, you know, long-term stability, clarity and transparency, a bit of incentives, a bit of sticks and carrots. It's all part of the package and it's an incredible challenge for a government having to cover so many policy dossiers to really deal with that.

But I think with the three of you, we made some really good progress to work ourselves through some those arguments and see how important this budget is for productivity. And you can now see why we, productivity specialists and economists, are so interested in what will be in it.

So it's a few more nights sleep, and some of you may listen to this after the event, so there you may know more than we do now. But whatever the outcome, the budget will be one of the steps in getting towards a more conducive fiscal environment for productivity. What we need is a long-term focus, stability, other elements that reduce uncertainty and give firms more confidence to invest and to work on their true productivity drivers.

That is in the end what will provide productivity growth, and that is ultimately what we would see in our projections, creating more room for this more virtuous cycle of growth and a healthy government purse. So let's see what happens.

Big thank you to Tera, to Louise and Stephen for your very helpful remarks. Fantastic.

Our next podcast on productivity puzzles will be shortly after the holiday break in January, and we're not quite sure yet what the next topic will be but stay tuned for that and you'll find out. Meanwhile, you can sign up for the entire productivity puzzle series for your favourite platform to make sure you also don't miss any future episodes.

If you'd like to find out more about our upcoming shows or any other work by the Productivity Institute, please visit our website at [productivity.ac.uk](https://productivity.ac.uk) or follow us on Blue Sky and LinkedIn.

Productivity Puzzles was brought to you by The Productivity Institute and this was me again, Bart van Ark from The Productivity Institute. Thanks for listening and stay productive.