12th August 2025

The UK doom-loop and how it can be averted

We all remember last year's £22bn "black hole" in the UK's finances, which led to the highest tax hikes since 1993[1]. Fast forward one year, and we are yet again talking about a £18bn "black hole" due to a potential decline in GDP growth forecasts[2]. The UK is now facing a doom-loop, which can only be averted by major policy changes...

The OBR forecast

When comparing the Office for Budget Responsibility's (OBR) October 2024 economic forecast with its March 2025 forecast, there is a very strange dynamic going on. The OBR essentially says, 10yr Gilt yields are 40bps higher, inflation will be higher in 2025, but then lower at 2% thereafter, bank rates will remain around 30bps higher at 3.8% and finally real GDP growth, whilst lower in 2025, is expected to accelerate higher over the following years. In 2029, the OBR estimates that the UK will have 2% inflation, 5.2% 10yr Gilt yield and 3.8% overnight bank rates[3]. This is a very odd projection, and the OBR will either be wrong on rates or on inflation, but there is no way that real yields will remain above real GDP for five consecutive years. And the problem is perhaps not so much the OBR, but the Bank of England... projecting even 1.9% inflation rates from 2027 whilst keeping rates high[4].

The OBR forecast

Year	Bank Rate	10yr Gilt Yield	CPI Inflation	Real GDP Growth
2025	3.9	4.58	3.2	1.0
2026	3.8	4.74	2.1	1.9
2027	3.8	4.90	2.0	1.8
2028	3.8	5.06	2.0	1.7
2029	3.8	5.21	2.0	1.8

Source: OBR, https://obr.uk/economic-and-fiscal-outlooks/

[1] https://www.reuters.com/world/uk/uks-new-finance-minister-reeves-lines-up-tax-hikes-borrowing-first-budget-2024-10-29/
[2] https://www.telegraph.co.uk/business/2025/07/02/overly-optimistic-obr-blows-18bn-hole-reeves-budget/?ICID=continue_without_subscribing_reg_first
[3] https://obr.uk/economic-and-fiscal-outlooks/
[4] https://www.bankofengland.co.uk/monetary-policy-report/2025/may-2025

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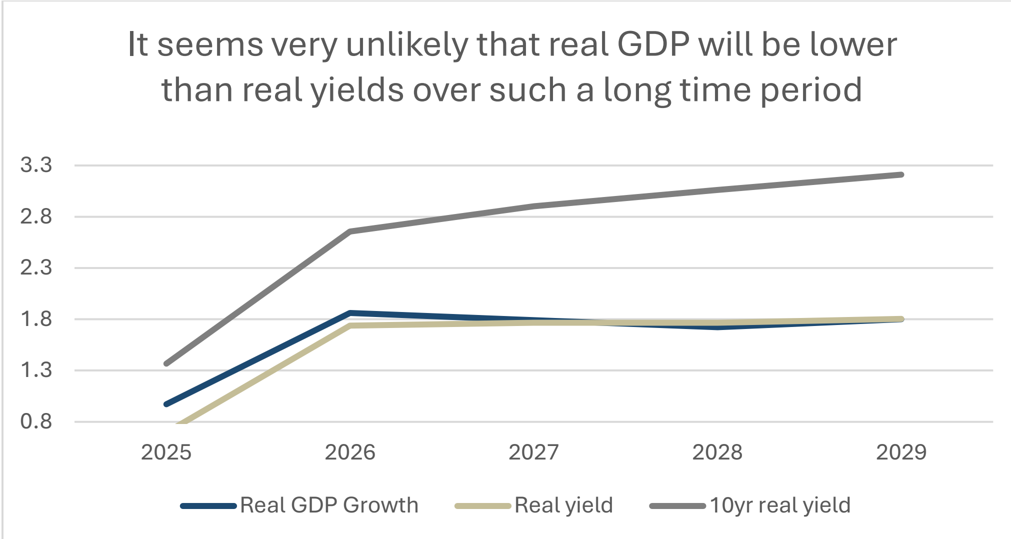

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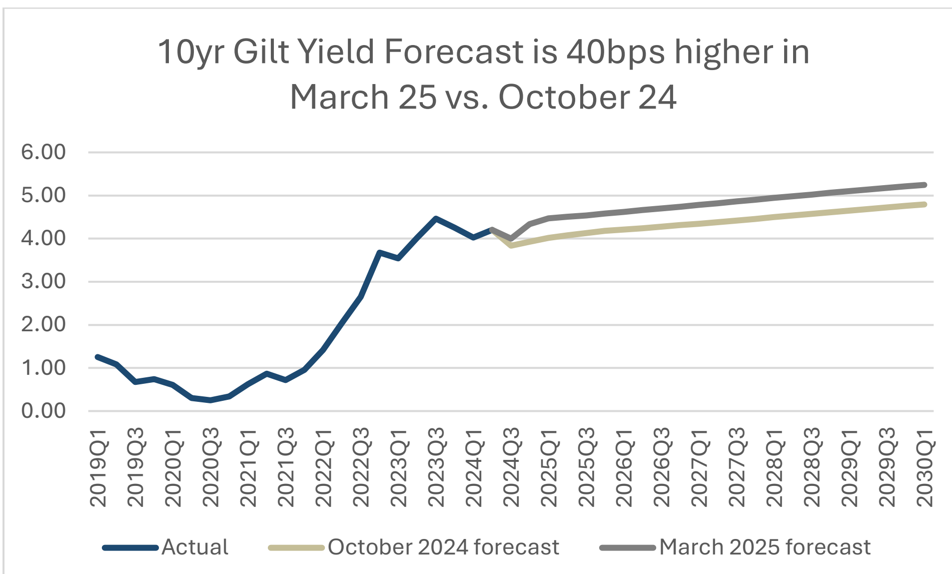

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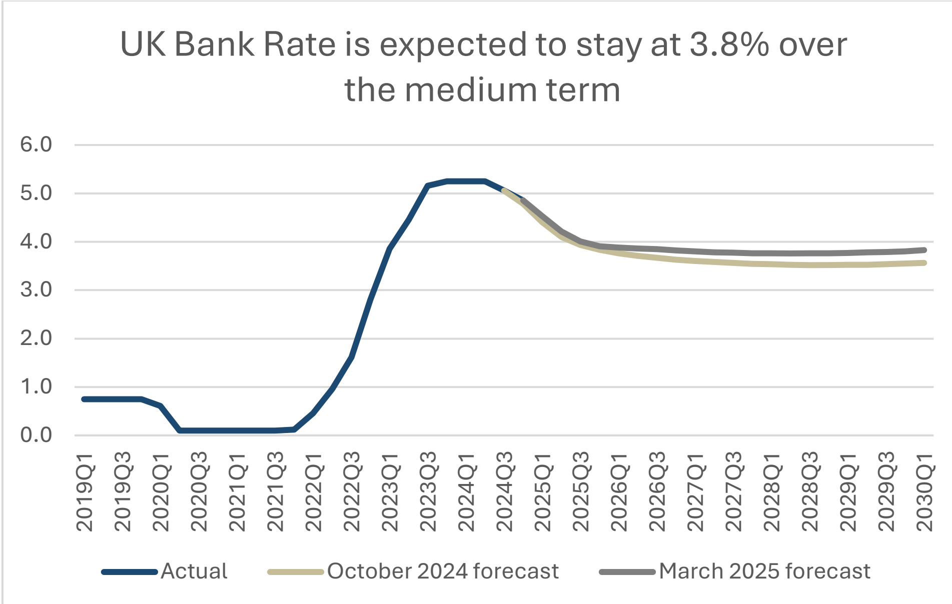

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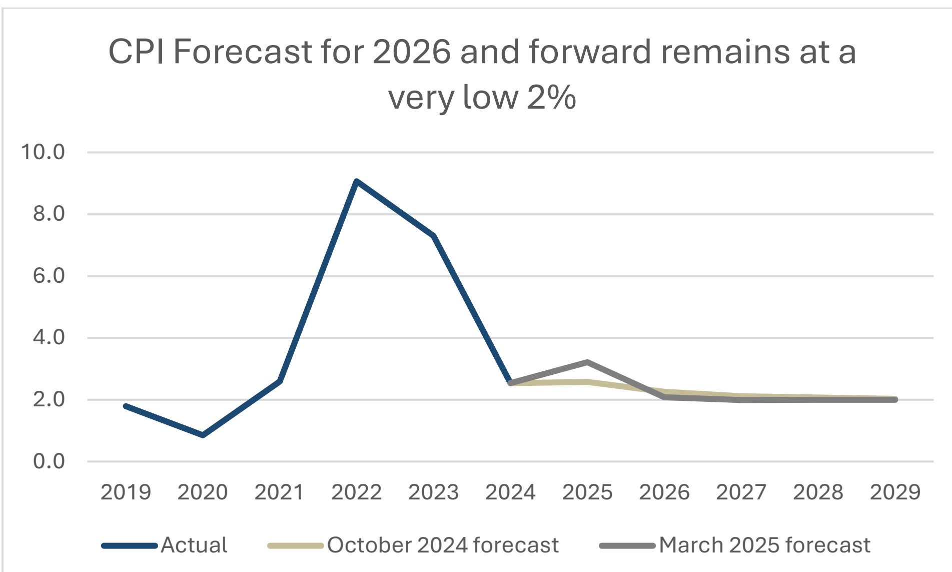

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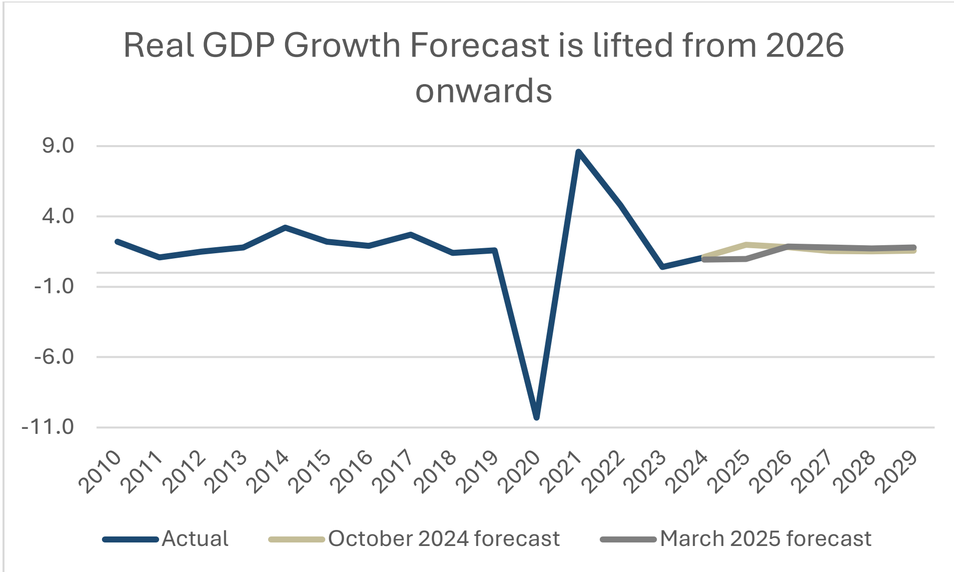
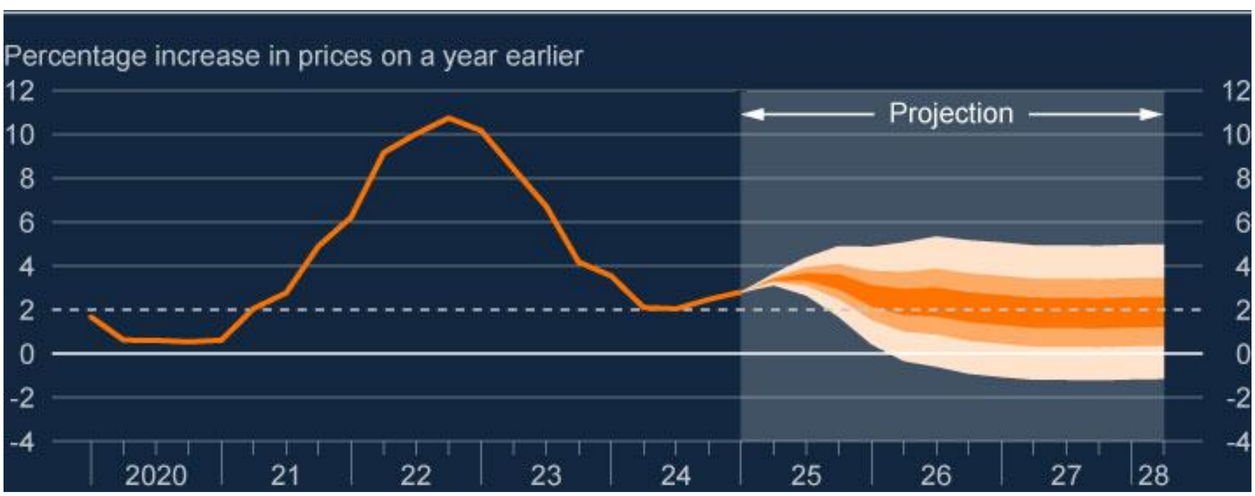


Source: https://obr.uk/economic-and-fiscal-outlooks/

<u>Bank of England inflation projection</u>



Source: https://www.bankofengland.co.uk/monetary-policy-report/2025/may-2025

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UK Debt Outstanding & Refinancing

The UK has around £2.861trn in debt outstanding as of 1st August 2025[5]. Of this debt, around 4% (£105bn) is in UKT-Bills, 31% (£899bn) in short- and ultra-short-dated Gilts (0-7 years excl. bills), 16% (£458bn) in medium-dated Gilts, 25% (£728bn) in long-dated Gilts, and 23% (£671bn) in index-linked Gilts[6]. Next to the ~£105bn UKTBs, the Debt Management Office (DMO) has planned to issue £299bn gross in Gilts for the FY 2025-26[7] and around £135.7bn in net issuance[8] – fairly similar to last year. However, to achieve a falling net debt/GDP ratio, the gross issuance needs to drop by over £80bn the next two years (helped by fewer maturities) and net issuance needs to drop by around £40bn a year. This seems like a difficult task considering the weaker GDP growth[9]. Based on an internal analysis on maturities vs. current market yields by maturity, from August 2025 to July 2026, the UK will spend around £3.15bn in additional interest expense purely from refinancing existing debt. In addition, the £136bn of net issuance would add another £6bn in annual interest expense assuming an average yield of 4.4%. The combined +£9bn is equivalent to 0.3% of UK's £2.85trn GDP[10].

UK Government Debt Outstanding by Maturity

Maturity/Type	As % of outstanding	£bn outstanding
Bills	4%	105
Short	31%	899
Medium	16%	458
Long	25%	728
Index-Linked	23%	671

Source: https://www.dmo.gov.uk/data/treasury-bills/treasury-bills-outstanding/, https://www.dmo.gov.uk/data/gilt-market/gilts-in-issue/

[5] https://www.dmo.gov.uk/data/treasury-bills/treasury-bills-outstanding/ , https://www.dmo.gov.uk/data/gilt-market/gilts-in-issue/
[6] https://www.dmo.gov.uk/media/afae3oen/opnot120623.pdf, page 6 in footer
[7] https://www.dmo.gov.uk/dmo_static_reports/currentremit.pdf as of 30th July 2025
[8] https://www.dmo.gov.uk/data/gilt-market/gross-and-net-issuance-data/
[9] https://www.ons.gov.uk/economy/grossdomesticproductgdp/bulletins/gdpmonthlyestimateuk/may2025
[10] https://commonslibrary.parliament.uk/research-briefings/sn02783/

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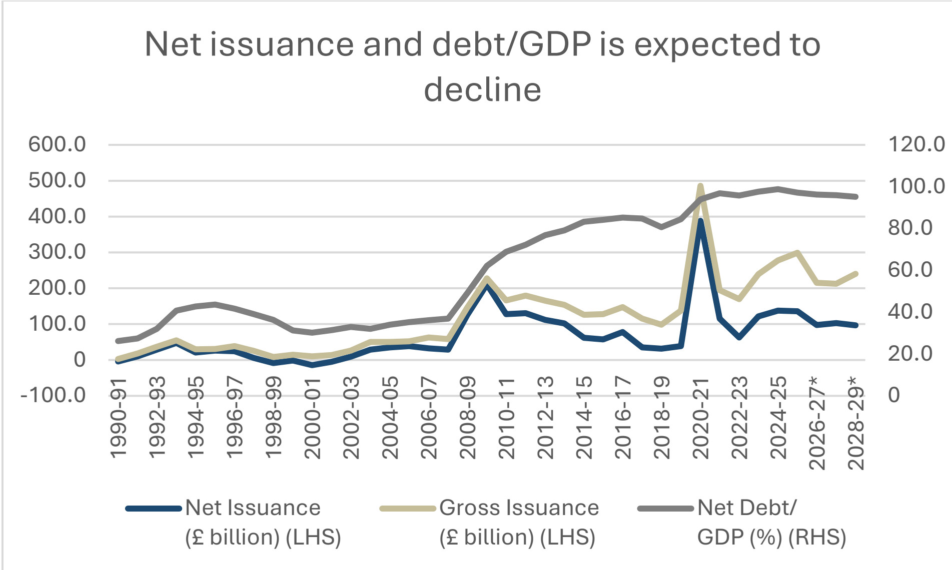

Source: https://www.dmo.gov.uk/data/gilt-market/gross-and-net-issuance-data/

UK Gilt Issuance FY 2025-26

Planned	Planned issuance (Apr-Mar 2025-26) (£bn)	Fixed Issuance (£bn) (Apr - Sep)	Remaining issuance (£bn) (Oct-Apr)	Remaining issuance, same % as Apr-Sep amount (Oct-Apr)
Short	121	65	56	85
Medium	90	39	50	51
Long	31	13	17	18
Index-Linked	33	11	21	15
Unallocated	24		24	
Total	298	129	168	

Source: DMO, own modelled data and assumptions

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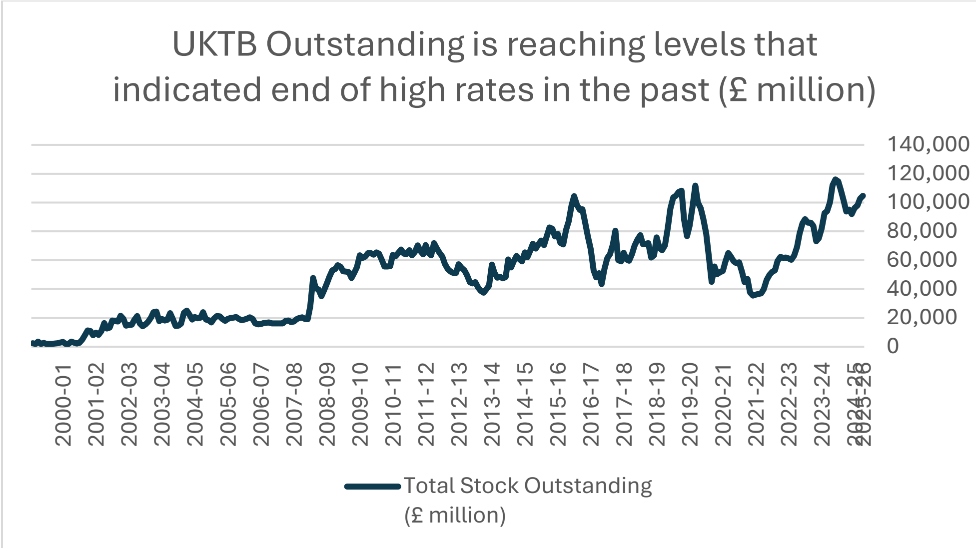
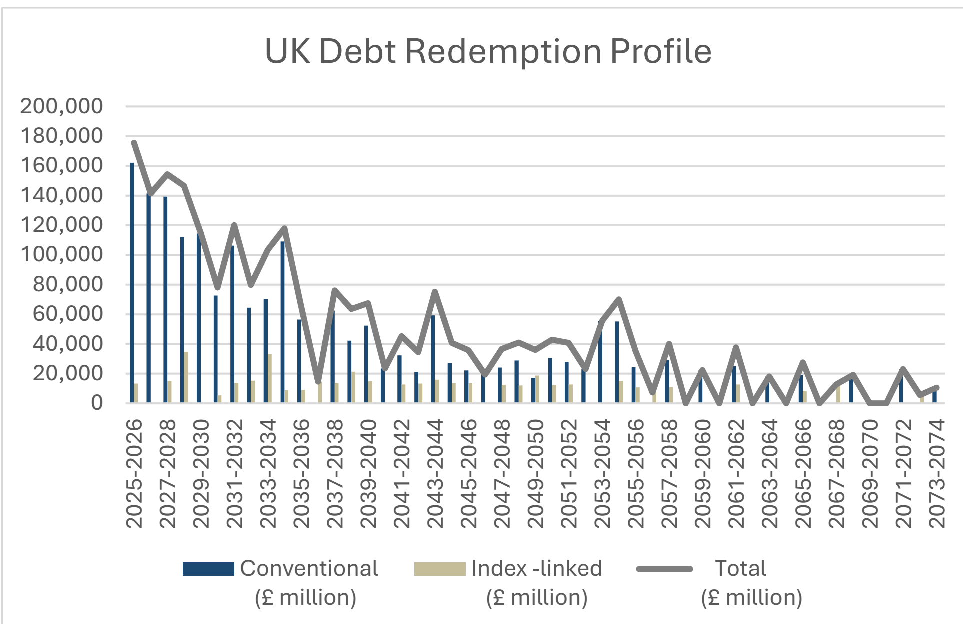


Source: https://www.dmo.gov.uk/data/treasury-bills/treasury-bills-outstanding/



Source: https://www.dmo.gov.uk/data/gilt-market/gilts-in-issue/

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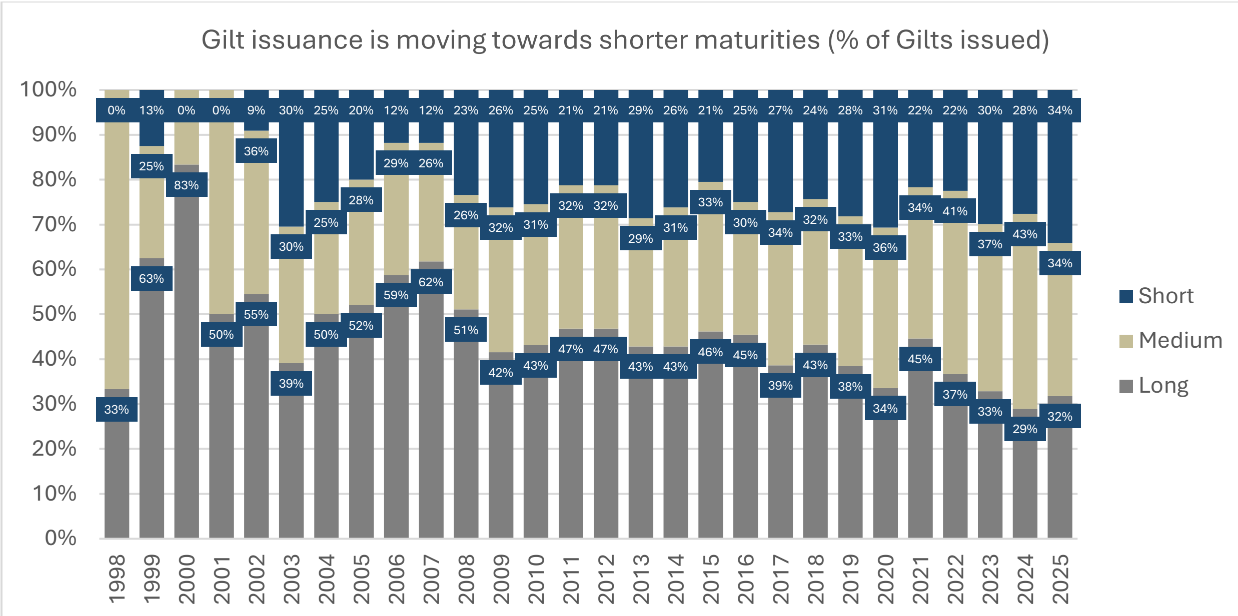

Source: https://www.dmo.gov.uk/data/pdfdatareport?reportCode=D2.1E

Lower rates, lower inflation = different ball game

According to own modelled analysis, if the entire yield curve were 1% lower, the UK government would only pay £4.6bn for the £136bn net issuance per annum (vs. £6bn) and the refinancing would go down to nearly zero (vs. £3.15bn), saving around £4bn in interest expense. Equally, if inflation were to come down, the interest expense on inflation-linked debt would reduce from the £27.1bn (30% of total interest expense) between July-24 and June-25 by a few £bn. To some degree, this doesn't seem all that much. However, in FY 2022-23, inflation-linked government debt cost the UK over £67bn compared to £40bn of nominal debt interest expense[11]. In other words, the UK has major incentives to keep inflation low to avoid a bond sell-off as it occurred in 2022. Whilst June 2025 cost the UK nearly £11bn in interest expense from linkers, this is all due to the Ofgem energy tariff, which is set quarterly and will come down again in October, potentially leading to a negative interest expense[12]. Yet, the policies in place are more ideologically than financially driven…

[11] https://www.ons.gov.uk/economy/governmentpublicsectorandtaxes/publicsectorfinance/bulletins/publicsectorfinances/june2023

[12] https://www.ofgem.gov.uk/energy-price-cap

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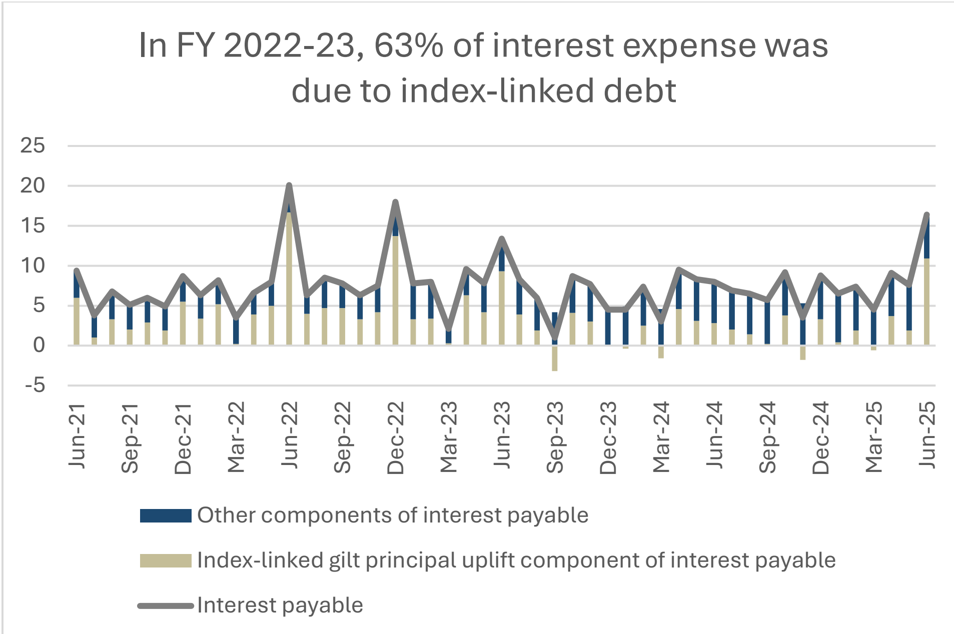

Source:
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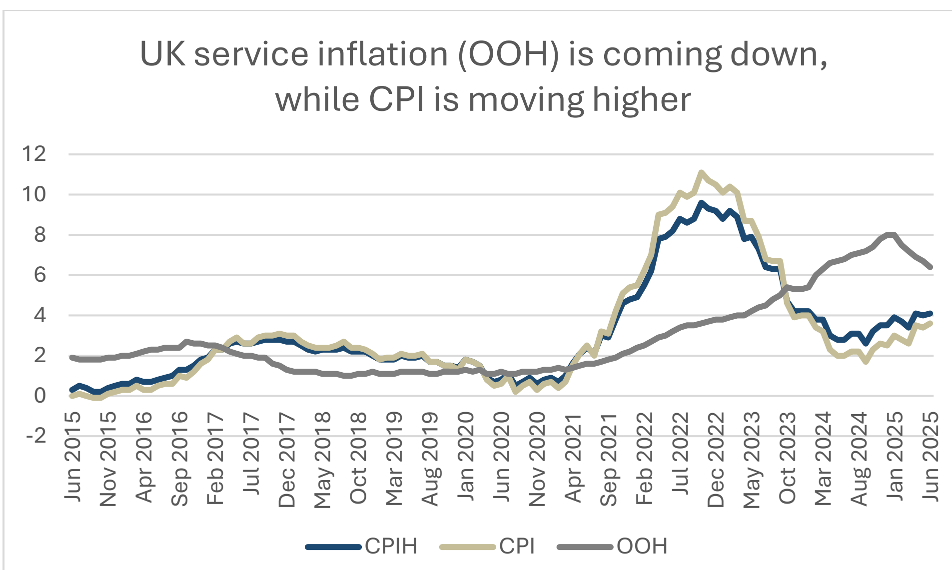

Source: https://www.ons.gov.uk/economy/inflationandpriceindices/bulletins/consumerpriceinflation/june2025

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All numbers in one basket

The Conservatives once ran on the five promises of halving inflation, growing the economy, reducing government debt, cutting NHS waiting lists and stopping the boats, which were at that time the top concerns of voters[13]. The new government is fighting the same problems and here are some of the numbers:

- Illegal migrants generally cost the UK £9bn a year before entering the society[14]
- The net zero electricity plans will require £80bn in grid investment by 2031 (while Sizewell C nuclear plant could face a cost overrun of £60bn[15]), which is expected to increase network costs of the OFGEM tariff by £104 per household[16] (5.8% at current Ofgem tariff)
- The electric vehicle mandate could eliminate £25bn in fuel duty tax revenue
- In a stark comparison, the UK is expected to generate £5.21bn from oil and gas tax revenue in 2025-26[17], while paying £1.9bn in subsidies to wind farms[18]. Norway, on the other hand, is expected to generate NOK 396bn (£29bn) in tax revenue from oil and gas[19]

In summary, soft migration- and inflationary energy policies are a very dangerous combination. Now, with the recent non-dom tax changes and generally higher taxes the country faces an exodus of wealthy individuals, intensifying a doom-loop. To make clear how important wealthy citizens for the UK are, the top 1% of the UK population contribute nearly 30% of total income tax, while the top 10% contribute over 60% and the bottom 50% only just about 9.3% of tax receipts[20].

Another important statistic: Around 16.1m people or 24% of the UK population are designated as disabled under the Welfare Bill. This figure considers that 45% of state pension age adults are

[13] https://www.aozorastep.com/The%20UK%20in%20crisis%20and%20what%20could%20be%20done%20to%20avert%20it.pdf
[14] https://www.gov.uk/government/publications/illegal-migration-bill-factsheets/illegal-migration-bill-overarching-factsheet
[15] https://www.ft.com/content/5f54592e-50ba-4a1e-8219-7a4eb01f74ed
[16] https://www.constructionenquirer.com/2025/07/01/80-energy-projects-unlocked-as-ofgem-backs-grid-expansion/
[17] https://obr.uk/forecasts-in-depth/tax-by-tax-spend-by-spend/oil-and-gas-revenues/
[18] https://www.bloomberg.com/news/articles/2025-02-13/uk-paid-record-1-9-billion-subsidy-to-offshore-wind-farms
[19] https://www.norskpetroleum.no/en/economy/petroleum-tax
[20] https://commonslibrary.parliament.uk/research-briefings/cbp-8513/

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disabled, 23% of working age and 11% children[21]. Disability benefits were forecast to be £39.1bn in 2023-24 and are expected to climb to £58.1bn in 2028-29[22]. It is highly questionable that 24% of the UK population can really be considered disabled, which raises the question of fraud. The politicians now face the problem of making the necessary adjustments, but at the same time could lose 24% of their voters – or even more, as the percentage of voting population designated disabled is even higher, excluding the children. Hence, changes in this respect are unlikely.

Ultimately, looking at all these numbers, it appears like the UK is in a doom-loop, which the country won't be able to escape from unless unpopular action is taken. Counting just some of these problems, the UK faces a cost or loss of tax revenue in the magnitude of £60bn a year (5.5% of annual tax revenue).

<u>£60bn in costs or lost tax revenue from dangerous policy making (5.5% of annual tax revenue)</u>

Type	£bn lost or cost due to dangerous policies
Lack of fuel duty	25
Illegal migrants	9
Disability cost change in 4 years	19
Lack of oil and gas revenue	5.2
Wind farm subsidies	1.9

Source: As per above paragraph – multiple sources

[21] https://commonslibrary.parliament.uk/research-briefings/cbp-9602/
[22] https://obr.uk/forecasts-in-depth/tax-by-tax-spend-by-spend/welfare-spending-disability-benefits

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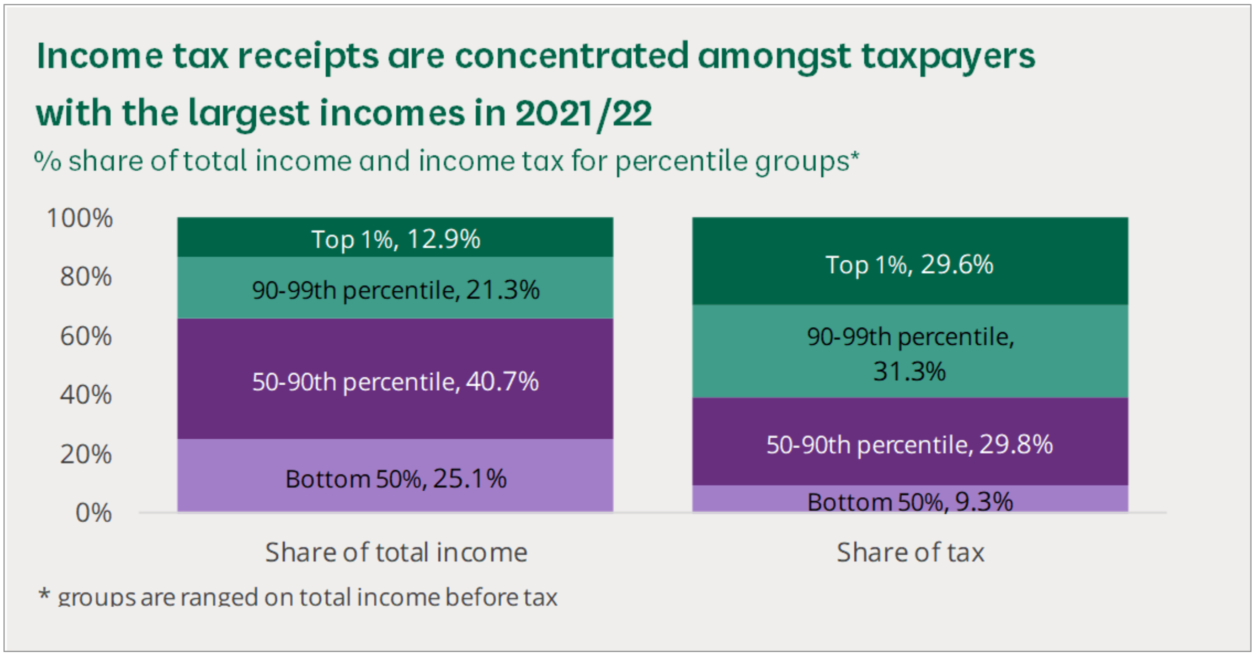

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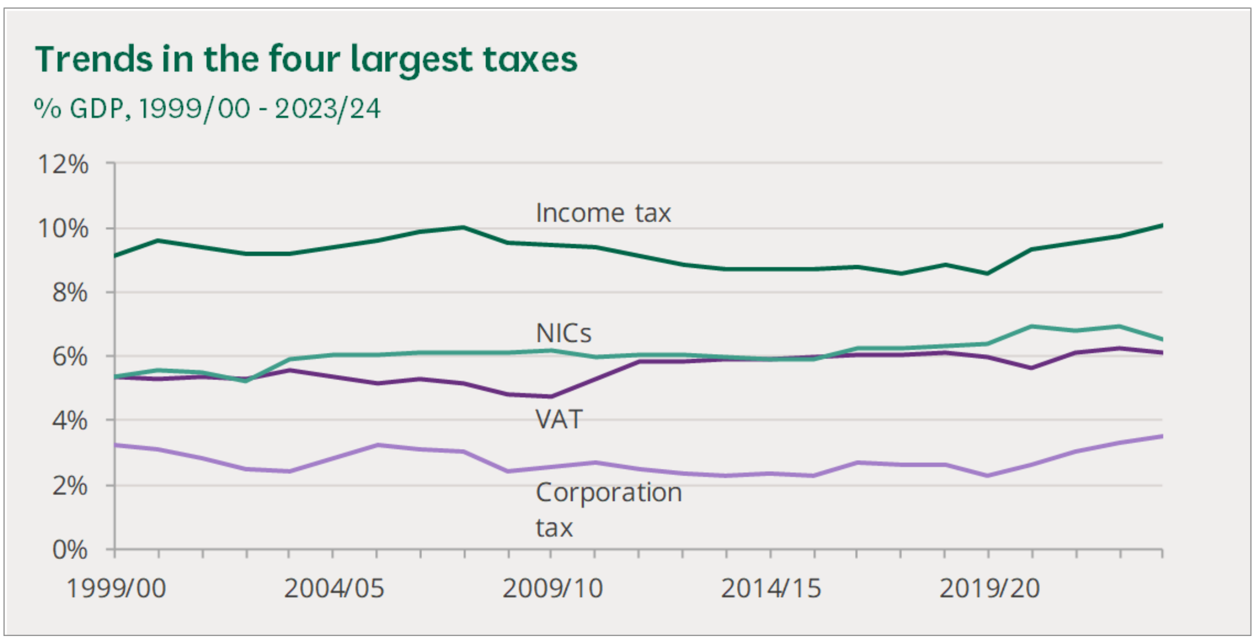

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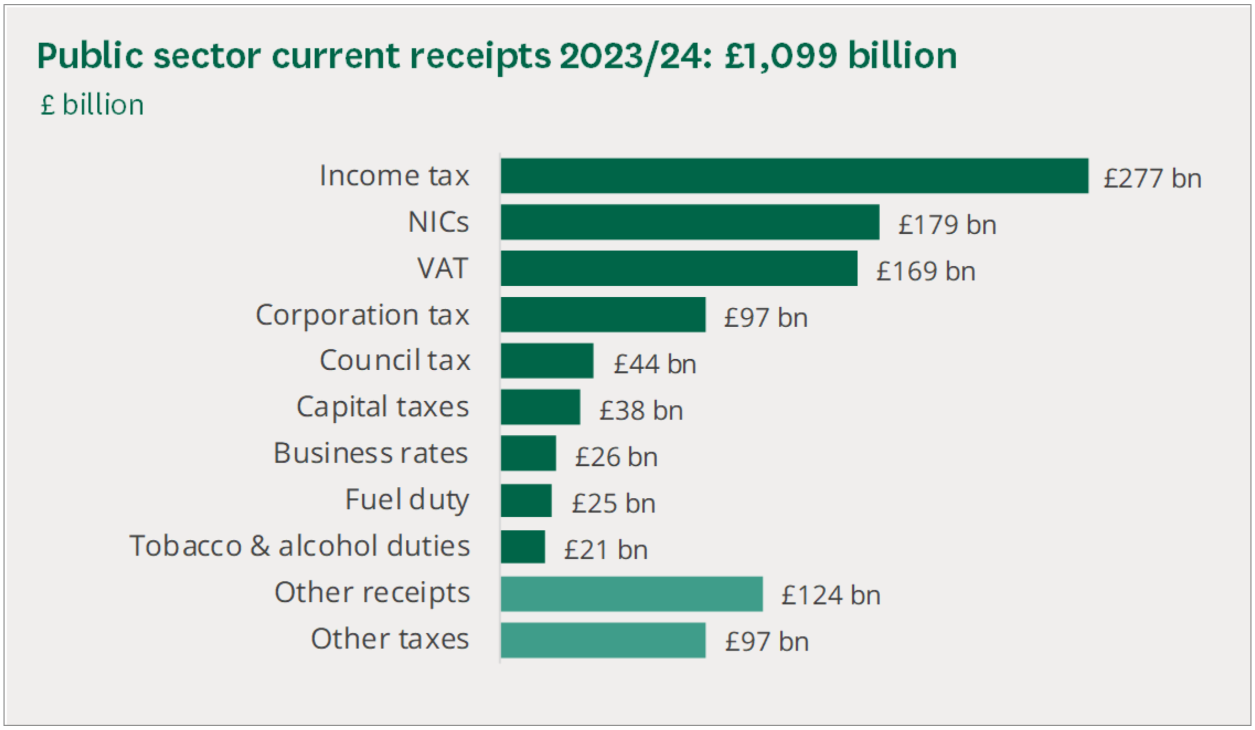

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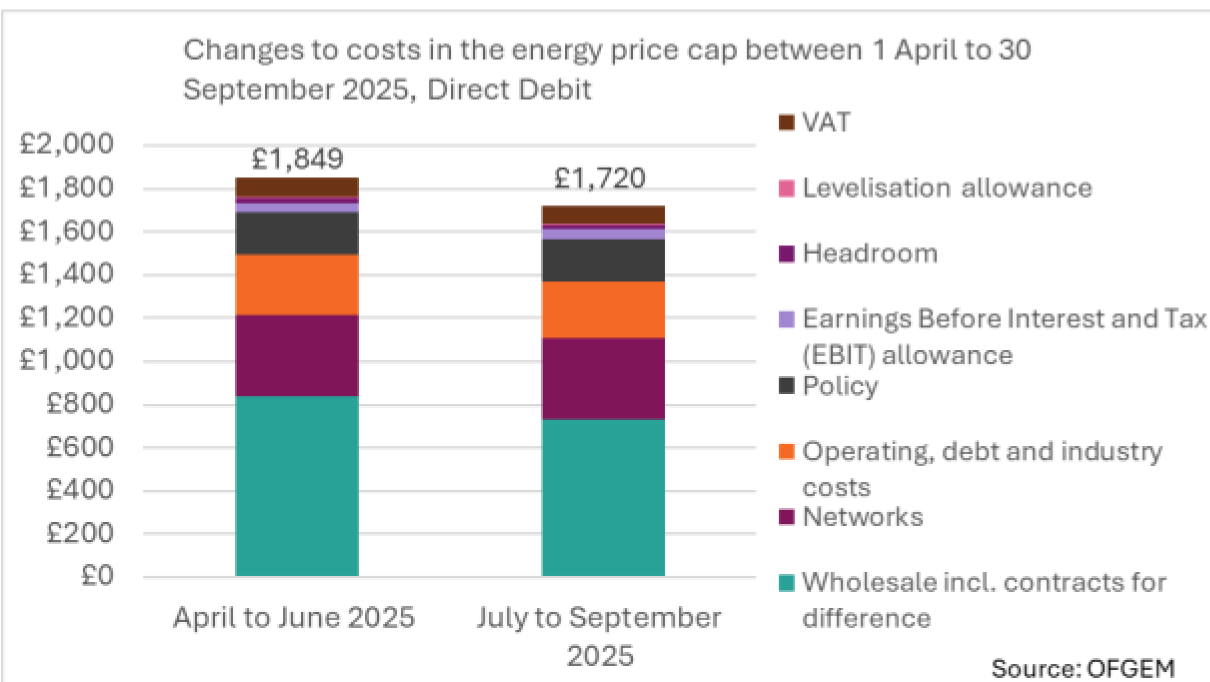
Network costs could climb from £372 a year to £1,488 a year



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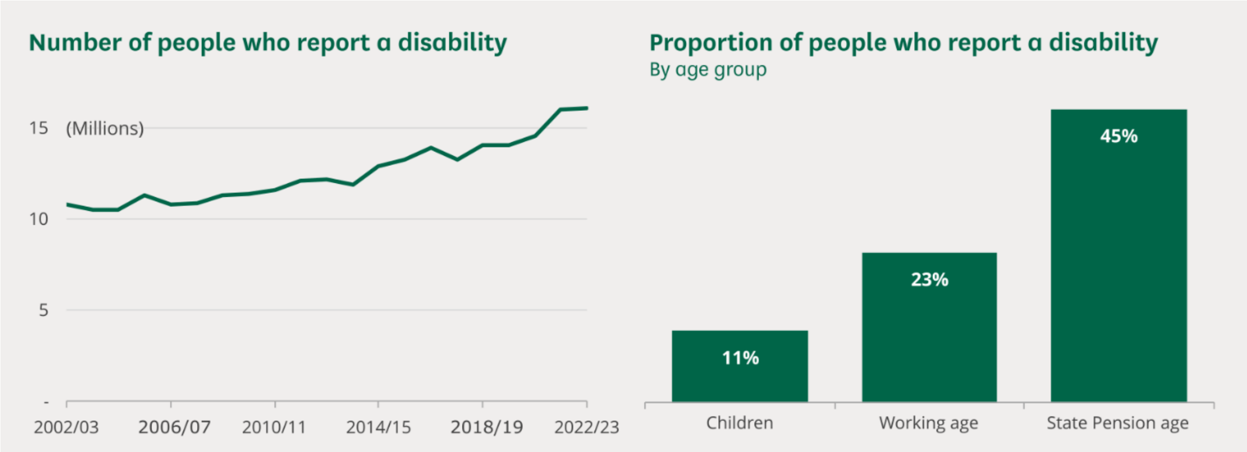

Source: https://commonslibrary.parliament.uk/research-briefings/cbp-9602/

The Autumn Budget 2025

Since I wrote this note, another report published by the National Institute of Economic and Social Research came out stating that the government needs to fill a £41.2bn black hole[23] – or in other words £50bn if you included some headroom. How can this hole be fixed? I doubt that the current government will make sufficient changes to net zero or migration policies. By lowering the voting age to 16 years, the government perhaps gave the strongest indication of what is ahead: The change of the triple lock. The triple lock means that the state pension will rise by the highest of either inflation, average earnings or 2.5%[24]. This legislation was introduced in 2010 after the Global Financial Crisis caused real yields to go negative and followed a period of low interest rates, low inflation and low average earnings increases. Today, the world looks very different, and the OBR estimates that the triple lock could cost the government £15.5bn per year by 2029-30[25]. I expect Labour to abolish the triple lock. However, to raise anything beyond this estimated £15.5bn could become tricky. All the proposals that Tax Justice UK is making (table below) would, in my opinion, backfire in a big way, as wealthy individuals would leave the country… A 5% rise in the corporate tax rate to 30% could raise

[23] https://niesr.ac.uk/publications/uk-economic-outlook-chancellors-trilemma?type=uk-economic-outlook
[24] https://www.moneyhelper.org.uk/en/blog/retirement/state-pension-triple-lock
[25] https://obr.uk/docs/dlm_uploads/Fiscal-risks-and-sustainability-report-July-2025.pdf p.7

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an additional £19.4bn (if one considers £97bn corporate tax revenue at 25% in 2023), which appears most likely in my opinion, but carries some risks of large corporations moving their HQ to the US.

How to raise £60bn		
#	Policy	£bn a year
1	Apply a 2% tax on assets over £10 million	24
2	Reform the Capital Gains Tax system through increasing rates and closing loopholes	12
3	Close the carried interest loophole so private equity bosses pay their fair share	0.51
4	Properly tax income from wealth, by applying National Insurance to investment income	10.2
5	Introduce a 4% tax on share buybacks	0.1-2
6	Make the oil and gas windfall tax permanent and introduce an excess profits approach	?
7	End and redirect fossil fuel subsidies for oil and gas companies	2.2
8	Tax private jets more	1.2
9	Properly fund and resource HMRC to tackle tax abuse and end unfair reliefs	6.5
10	Stop rich multinational corporations evading tax by mandating they declare profits wherever they operate	15

Source: https://taxjustice.uk/blog/how-to-raise-60-billion-for-public-services-our-ten-tax-reforms/

Concluding remarks

In order to end on a positive note and to put some of this gloom aside, if interest rates were to go below the 3.8% forecast and inflation does end up at 2%, the outlook on government finances could look a lot better. I do think this is still a possible outcome, and with less aggressive net zero timelines and a crackdown on crime and illegal/low skilled migration, the UK could thrive like few other countries can.

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