Aadya Bahl November 25th, 2025

# Budget 2025 – how to cure the UK's low productivity

*Productivity powers economic growth and shapes living standards. Yet the UK continues to falter on both counts. Low productivity and weak investment have become defining features of the economy, and this year's Budget will once again confront this challenge.* ***Aadya Bahl*** *explores how the 2025 Budget can shape future growth and help pull Britain out of its productivity slump.*

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The Budget is the UK government's key fiscal event of the year, setting out its tax and financial plans alongside new forecasts for the economy and public finances. These forecasts are produced by the Office for Budget Responsibility (OBR) and detail five-year projections based on the policy package set out in the Budget. In the weeks leading up to the announcement, the OBR undertakes several forecasting rounds, sent confidentially to the Chancellor to inform policy decisions.

Among the many inputs that feed into these projections, the outlook for productivity is perhaps the most consequential. Productivity determines the long-term path of economic growth, influencing wages, tax revenues and living standards across the country.

## A fragile productivity outlook

The OBR is widely expected to downgrade its productivity growth forecast in the upcoming Budget. In its most recent forecast, published alongside the Spring Statement in March 2025, it projected that output per hour worked – a standard measure of labour productivity – would increase by 0.2 per cent in 2025, 1.1 per cent in 2026 and 1.3 per cent in 2029. Outside the pandemic period, the UK has not experienced sustained productivity growth at this level for two decades.

Other independent assessments are more pessimistic. The Bank of England's latest report notes that GDP growth, business confidence and investment intentions remain subdued. It also finds that labour market tightness has eased, predominantly through reduced employment. At the same time, private sector wages have continued to rise while productivity has remained flat. If demand turns out to be weaker than firms anticipate, these higher labour costs may prompt them to reassess staffing levels.

> *Low productivity growth is more than a technical concern; it shapes the fiscal landscape and affects every household directly. When productivity stagnates, wages grow slowly, public services come under strain, and living standards weaken.*

The Institute for Fiscal Studies (IFS), for instance, anticipates medium-term productivity growth of around 0.8 per cent. But small changes in these assumptions have large fiscal consequences. Each 0.1 percentage point reduction in annual productivity growth could add roughly £7 billion to borrowing by 2029-30. So, if the OBR were to align its forecast more closely to the IFS outlook, projected borrowing could increase by around £14 billion.

This additional borrowing would exceed the headroom of £9.9 billion the Chancellor built into her rules for the next five years, leaving the government on course to breach its targets. If that were to happen, the Chancellor will need to make changes in the upcoming budget to restore this headroom.

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## Policy stability for growth

Weak business investment, skills shortages, and underinvestment in infrastructure have constrained growth and productivity in the UK for over a decade. The UK has one of the lowest rates of capital investment among advanced economies, and many firms remain hesitant to invest in their workforce.

A central reason for this hesitation is policy instability. A growing body of academic evidence shows that political and economic uncertainty depresses investment and productivity growth. Since 2010, the UK has cycled through four departmental structures for business policy, 11 secretaries of state for business, and seen repeated shifts in industrial strategy and corporation tax policy.

This churn has taken place alongside the economic shockwaves of Brexit, the pandemic, the energy crisis, and broader geopolitical tensions. These circumstances have created domestic policy uncertainty and discouraged firms from investing in productivity-enhancing activities such as training, research, and innovation.

Greater fiscal and policy stability could help reverse this. With a large parliamentary majority and no requirement to call an election for four years, the government should be well placed to offer that stability. Its education and skills reforms, industrial strategy, prioritisation of public investment, planning and pensions reforms all have the potential to support growth, but only if they are sustained and consistently implemented.

# The choices ahead

Low productivity growth has clear implications for fiscal policy. The government needs resources to invest in the foundations of growth: people, infrastructure and innovation. Yet with limited fiscal headroom, it faces difficult trade-offs.

> *Productivity stagnation is not driven by a single issue but by a web of interconnected problems in investment, skills, policy design, and policy coherence.*

One option would be to borrow more, but this would go against the government's own fiscal rules. The others would be cutting spending, which risks undermining public investment, or raising taxes. The upcoming Budget will need to confront these choices directly.

Productivity stagnation is not driven by a single issue but by a web of interconnected problems in investment, skills, policy design, and policy coherence. This Budget is an opportunity to move away from short-term fixes in taxation and toward a credible, stable, and long-term strategy for growth.

Many of the building blocks are in place, with the government advancing its growth mission through initiatives such as the industrial strategy, the employment rights bill and planning reforms. But only sustained policy effort, combined with a genuine commitment to stability, will enable the UK to reverse its productivity slump and improve living standards.

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## About the author

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Aadya Bahl is a Policy Officer at the Centre for Economic Performance at the London School of Economics. Her work aims to use data-driven and research-backed insights to inform policy decisions. Prior to joining CEP, she worked with Metro Dynamics across multiple projects aimed at driving inclusive growth across places, and the GM Chamber of Commerce on the Local Skills Improvement Plans. She has a Master's in Development Economics and Policy from the University of Manchester.

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