

# How Rachel Reeves will find more than £50 billion a ye...

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I was interviewed yesterday by a journalist who wanted to know what I thought Rachel Reeves might do with regard to business taxation, and corporation tax in particular, when she becomes chancellor (assuming that happens). I admit my answer to that question was 'not a lot' given recent changes to corporation tax by the Tories that, given her comments to the media, Reeves seems unlikely to want to undo or change.

As a result we moved on to discuss how Reeves might manage the economy given that she appears to be unwilling to raise taxation. Nailed down in this way, I was forced to think about this issue afresh, and three very obvious ideas came to me.

Firstly, just as Rachel Reeves seems incredibly unwilling to change tax rates, I also think that she will be just as unwilling to increase personal and other

tax allowances from those levels to which the Tories are committed, which are supposedly fixed until 2028. We know that the impact of this decision, taken in 2021 before the onset of a bout of inflation, has now imposed a substantial cost on households and businesses in the UK and proportionately increased tax revenues despite the poor UK economy in recent years. Office fir Budget Responsibility (OBR) forecasts (such as they are) are based upon the assumption that these allowances will not change, and I am quite confident that Rachel Reeves has no intention of doing any such thing.

Secondly, I strongly suspect the Rachel Reeves believes that inflation will fall significantly over the next few years, probably to levels lower than that currently knowledged by the Bank of England, and even significantly below their 2% target. Given the way in which supposed interest charges on index linked bonds have been calculated by the ONS this means that there will be a substantial reduction in these charges over coming years, giving Reeves a potential budget for spending of maybe £30 to £40 billion a year.

Thirdly, because inflation will fall significantly, I strongly suspect that Labour will put pressure on the Bank of England to also significantly reduce interest rates. This demand

will be hard for the Bank to resist given the size of their likely House of Commons majority. If rates fall to maybe 2%, as would be appropriate at most, central bank reserve account interest will also fall dramatically, from in excess of £40 billion a year to less than £20 billion a year, providing a further boost to Rachel Reeves spending capacity.

That same reduction will also mean that the Bank of England will have no further reason to pursue quantitative tightening, because it will not be trying to maintain interest rates at above market levels. As a result, the cost of new borrowing government borrowing will also fall significantly, reducing pressure on Rachel Reeves.

Being precise about the combined impact of these issues not necessary, or even possible. What is appropriate to note is that most of these reductions in the cost of borrowing are not likely at present to be reflected in OBR estimates given the current mood music emanating from the Bank of England, which wants rates to remain high. The OBR has to reflect the Bank's view.

Now will the OBR be able to reflect these changes in the forecasts that they will issue in March.

However, matters may look very different by the time that Rachel Reeves comes to make her first budget statement in March 2025. By then she will, using the meaningless jargon adopted by neoliberal forecasters, have substantial 'fiscal headroom' within her budget as consequence of rapidly falling interest costs. It will be this reduction rather than sums raised by extra tax revenues that she will use as the foundation for Labour spending plans.

I could, of course, be entirely wrong about this, but Reeves must have some reasons for optimism with regard to spending, and these are the only ones that I can find.