

The Great Stagnation: Briefing 7

Austerity and Brexit

By Julian Jessop

2 September 2026



Summary

- This briefing examines two common explanations for the UK's poor economic performance over the last fifteen years: austerity and Brexit.
- Though critics of austerity often frame it in terms of 'savage cuts', the austerity programme of the Coalition and Conservative governments of the 2010s saw public spending remain roughly flat in real terms. Public spending as a share of GDP fell gradually from 45.5 per cent in 2010/11 to a pre-Covid low of 39.1 per cent in 2019/20.
- There are some sound critiques of austerity as implemented. Spending cuts in the early 2010s fell more heavily on capital expenditure than on day-to-day spending. Public sector net investment was roughly halved, from a peak of £75.2bn in 2008/09 (in 2025/26 prices) to a low of £37.3bn in 2013/14. That said, public investment remained a larger proportion of GDP than in the 1980s, 1990s and 2000s. Austerity does not seem to have harmed productivity in the public sector, which over the course of the 2010s saw relatively rapid growth.
- Furthermore, it is highly unlikely that the UK government could have continued to borrow at favourable rates without a plan for fiscal constraints. There is little reason to believe that any additional public money would have been spent wisely or could have significantly boosted productivity growth.
- The vote to leave the EU in 2016 and the protracted Brexit negotiations that followed undoubtedly ushered in a period of political instability and economic uncertainty which may have slowed growth in the short term. However, estimates of sustained losses of 4–8 per cent of GDP are likely to be exaggerated.
- When compared to other large European economies, the UK's real GDP per capita growth since 2016 has been towards the middle of the pack: slower than France and Italy but faster than Germany. The UK has underperformed in trade in goods, but outperformed expectations in trade in services, while investment has begun to catch up after a period of post-Brexit uncertainty.
- There is little hard evidence that either austerity or Brexit can explain Britain's weak economic performance in the post-2008 period. The reality is that the impact of neither shock was as large as is often assumed.

About the author

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About the publication

This briefing is a version of a chapter that appears in the IEA book, *The Great Stagnation: Why Britain Stopped Growing*, along with contributions from other authors. Each chapter presents and analyses a distinct explanation for the decline in British economic growth over the last two decades.

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Introduction

This briefing looks at two common explanations for the poor performance of the UK economy over many years. The first is the period of fiscal 'austerity' that began under

the Conservative-led Coalition government in 2010. The second is the impact of the vote to leave the European Union in 2016, culminating in Brexit.

This briefing will start with some different definitions of austerity and see how they measure up against the actual data. It will then review the ways in which austerity might have hindered, or helped, economic growth and productivity.

The second part of the briefing focuses on Brexit. The result of the 2016 referendum was itself an economic and financial shock, so it makes sense to start the clock from then. There were clearly some negative effects and upfront costs, but there have also been some positives with the potential for the benefits to grow over time.

One common theme is the difficulty of identifying the counterfactual. In other words, what would have happened if the UK government had taken a different fiscal stance after 2010, or if the UK public had voted to remain in the EU in 2016?

However, there is little hard evidence that either austerity or Brexit was a major factor contributing to the UK's poor economic performance. In part this is because neither shock was as large as many assume.

Defining austerity

Austerity seems to mean different things to different people, but it is generally seen as a 'bad thing'. One dictionary definition is 'a situation in which people's living standards are reduced because of economic difficulties.'

In public debates, the austerity of the 2010s is often characterised as 'savage cuts' in public spending which weakened the foundations of the economy and of society.

A more objective definition would be 'policies designed to reduce budget deficits through spending cuts, tax rises, or both'. In more technical terms, austerity is 'a discretionary tightening of fiscal policy with the aim of reducing the budget deficit'.

Viewed this way, austerity is simply a means to improve the health of the public finances, reducing the risks of a financial crisis and paving the way for more sustainable growth in future. It may also form part of a broader strategy to reduce the size of the state.

What do the numbers say?

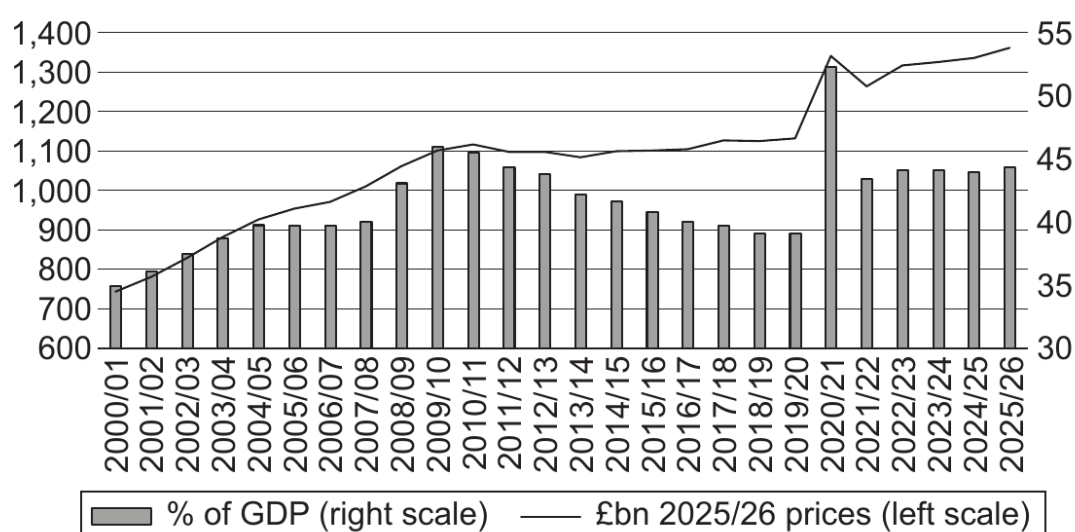
The Office for Budget Responsibility publishes a helpful databank which tracks the public finances over time (OBR 2026).

The first point to note is that public spending continued to increase every year throughout the 2010s, at least in cash terms. Total managed expenditure (TME) was

£743bn in 2010/11. By 2019/20, the last year before the Covid pandemic, it had risen to £885bn.

Of course, these numbers do not take account of the impact of inflation. However, even in real terms, total spending was little changed between 2010/11 and 2019/20, falling slightly in the first half of this period and then rising slightly in the second. This was still a large reduction relative to the plans inherited from the previous Labour government, but not in absolute terms.

Figure 1: UK total managed expenditure in real terms and as a percentage of GDP



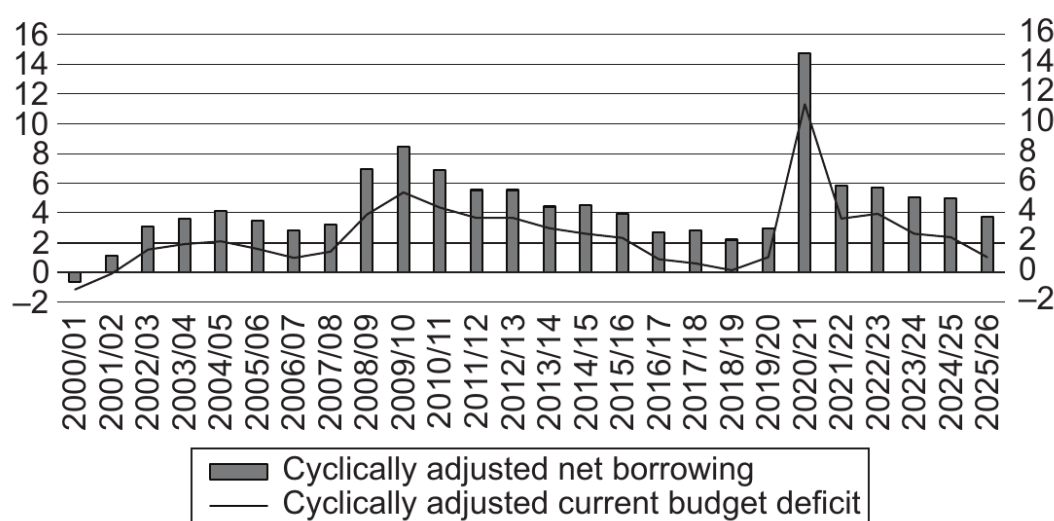
Source: Office for Budget Responsibility.

With spending held steady while the economy was growing, public spending as a share of GDP fell from 45.5 per cent in 2010/11 to a pre-Covid low of 39.1 per cent in 2019/20. However, this fall simply returned the ratio of spending to GDP to the levels seen before the Global Financial Crisis (GFC) of 2007/08.

On the revenue side, the tax burden was relatively stable throughout the 2010s. The upshot is that the annual budget deficit was brought down from 8.7 per cent of GDP in 2010/11 to 2.6 per cent of GDP in 2019/20 and this was mainly achieved via restraint on the spending side.

The data, at least in aggregate, therefore do not support the claim that austerity resulted in 'savage cuts' in public spending. It is more accurate to describe this in neutral terms as a period of gradual tightening in fiscal policy.

Figure 2: UK cyclically adjusted borrowing as a percentage of GDP



Source: Office for Budget Responsibility.

This is reflected in the steady decline in cyclically adjusted borrowing, which strips out the temporary effects of the economic cycle. In 2009/10, the cyclically adjusted deficit was 8.4 per cent of GDP, which was surely unsustainable. By 2018/19 this had been brought down to 2.2 per cent.

The cyclically adjusted current budget deficit was reduced from 5.4 per cent of GDP in 2009/10 to just 0.1 per cent in 2018/19. This meant that day-to-day spending was largely covered by tax revenues, which was a much sounder fiscal position.

Deficits versus debt

Some still argue that austerity ‘failed’ because the national debt continued to rise. This point can be quickly dismissed – because of some basic maths.

The persistent annual budget deficits (a flow) did mean that public sector net debt (a stock) rose from 70.6 per cent of GDP in 2010/11 to 79.6 per cent in 2018/19, and from £1,261bn to £1,776bn in cash terms. In the wake of Covid these numbers climbed to 93.7 per cent and £2,917bn respectively in 2025/26.

However, the stock of debt would only have fallen in cash terms if the government had run annual budget surpluses, which would not have been realistic. This might even have required more austerity, rather than less.

Moreover, the UK was not an outlier. The maths is the same everywhere.

Looking at the rest of the G7, there have been bigger increases in government debt (as a share of GDP) in the US, France, Italy and Japan. The only G7 economies where debt has not significantly increased since 2010 are Germany, where most now agree

that fiscal policy has been too tight, and Canada, where the 2008/09 recession was relatively shallow.

A price worth paying?

In short, the spending restraint of the early 2010s returned the public finances to much better health following the explosion of borrowing in the wake of the GFC. It is therefore hard to see how austerity could have contributed to the UK's much deeper and longer lasting problems.

Indeed, the official view at the time (supported by the IMF, among others) was that it was necessary to tighten fiscal policy to prevent an even worse outcome, even if this meant a weaker economic recovery in the short term. UK politicians and officials were particularly worried by the financial crisis then beginning to engulf Greece.

It was also argued that any economic drag from lower public spending would be at least partly offset by an increase in private spending, as the former helped to keep interest rates low and reduced the risks of 'crowding out'.

Could looser fiscal policy have boosted growth?

This more positive interpretation of austerity has still been widely challenged.

One counter-argument is that a combination of fiscal and monetary stimulus might have resulted in a stronger economic recovery, and that this could have turned the public finances around more quickly too.

In particular, the UK government (and others, including the IMF) may have underestimated the negative impact that fiscal tightening had on growth, especially when the economy was still weak, interest rates were already low and many other countries were cutting back as well (see Portes and Holland 2012; Wren-Lewis 2015).

In more technical terms, the fiscal multipliers that the OBR used to assess the impact of the tightening in policy announced in 2010 may have been too low (though the OBR itself has consistently disputed this).

Moreover, it is often argued the restraint in public spending fell particularly hard on capital budgets, delaying what may have been much-needed investment in infrastructure and public services and reducing the resilience of the UK economy to subsequent shocks (notably Covid).

According to this view, austerity was precisely the wrong approach. Instead, the government should have taken advantage of low interest rates to increase spending, both to provide an immediate boost to demand and to increase investment for the longer term.

Finally, some have argued that the international creditworthiness of the UK was never seriously in doubt. In part this is because, unlike Greece, the UK was not a member of the euro and therefore retained its independence on monetary policy and the ability to create money to service debts.

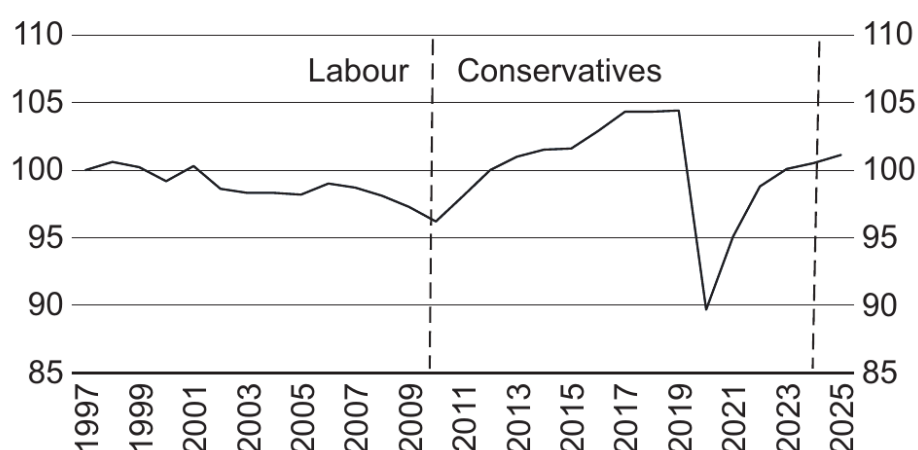
A defence of Austerity

There is a lot to unpack here, but there are three main reasons to reject these criticisms.

First, the degree of austerity is often overstated. As noted earlier, public spending was held broadly steady in real terms, rather than cut aggressively. Spending on healthcare in particular was protected and continued to grow in real terms between 2010 and 2019, albeit at a slower pace than under the previous Labour government.

The claim that the axe fell particularly hard on capital budgets may have more merit. Public sector net investment was roughly halved in real terms, from a peak of £75.2bn in 2008/09 (in 2025/26 prices) to a low of £37.3bn in 2013/14.

Figure 3: Total public sector service productivity (Index 1997 = 100)



Source: ONS.

Nonetheless, public sector net investment still averaged just under 2 per cent of GDP in the 2010s. This was higher than the averages in the 1980s, 1990s and 2000s, albeit flattered a little by the inclusion of student loans.

It might still be argued that spending failed to keep up with the increasing demands of a growing and ageing population. However, this was also a period of relatively rapid growth in total public sector service productivity, at least until Covid (ONS 2026).

Second, spending restraint was necessary. There was no guarantee that interest rates would have remained low if the government had chosen to increase borrowing rather than reduce it.

While the UK's position may not have been as parlous as that of Greece, investors would still have demanded higher interest rates to finance larger deficits. Indeed, doubts over the sustainability of the public finances are one reason why the UK government's cost of borrowing is relatively high now.

Third, there was no guarantee either that the government would have spent any additional money wisely.

An exception might be made here for spending on genuine 'public goods'. The 2010s saw large cuts in the budgets for environmental protections, defence and justice, which do now look short-sighted. But a major programme of public works in the 2010s could have been just as wasteful as HS2 is proving to be now.

Funding more borrowing via 'quantitative easing' (the purchase of government bonds by central banks using newly created money) might also have further blurred the lines between fiscal and monetary policy, as well as saddling future taxpayers with additional costs as the policy is unwound.

Conclusions on austerity

Bringing all this together, there is little evidence that the fiscal discipline of the early 2010s had a lasting negative impact on economic growth or productivity, including productivity in the public sector.

Instead, it succeeded in putting the public finances on a more sustainable path – at least until the Covid pandemic struck in 2020.

The economic impacts of Brexit

On 23 June 2016 the UK held a referendum on EU membership and voted to leave by a narrow majority of 52 per cent to 48 per cent. Although the referendum was technically 'advisory', the UK government had repeatedly said this was a 'once in a generation decision' and that it would 'implement what you decide'. The vote therefore began the process commonly known as 'Brexit'.

The referendum itself was about sovereignty. In this respect, Brexit has been a success because it has returned sovereignty to the UK. Multiple opinion polls show that a majority of the public still want decisions in key policy areas to be made by the UK government. The fact that politicians have not used that sovereignty well is not a failing of Brexit itself.

Nonetheless, this briefing is about the economic impact.

The decision to leave the EU was itself a shock. Most analysis of the economic impact of Brexit therefore starts the clock in 2016.

This period was characterised by heightened political and economic uncertainty. Article 50 was not triggered until March 2017, which formally began what was supposed to be a two-year exit process. However, negotiations between the UK and the EU dragged on, with Theresa May's government proving unable to secure parliamentary approval for her deal.

The 2019 general election eventually gave Boris Johnson a large majority to pass a revised agreement. The UK formally left the political structures of the EU on 31 January 2020. But even this was followed by a transition period where the UK remained part of the EU Single Market and Customs Union, which lasted until the end of that year.

This is important, because a lot of the initial disruption, especially to investment, can be traced to that prolonged period of uncertainty, which has now eased.

More positively, the UK left on relatively favourable terms. In particular, the Trade and Cooperation Agreement (TCA) provided zero-tariff, zero-quota trade in goods that meet rules of origin, alongside frameworks for services, digital trade, transport, energy, fisheries and social security coordination.

This is important, too. The upshot is that much less has actually changed than many people anticipated, feared or hoped, in the wake of the vote to leave.

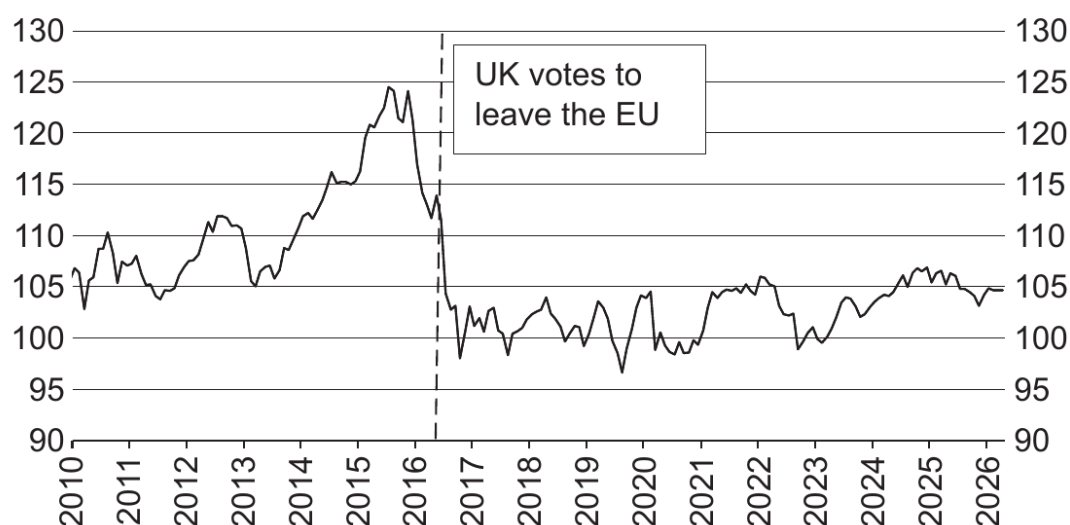
The immediate market reaction

The impact was seen first in the financial markets, where sterling and UK equity prices fell sharply in the wake of the referendum results. This was consistent with fears that Brexit would damage the UK economy in the long run and even that the uncertainty created by voting to leave would be enough to trigger an immediate recession. These fears had been fuelled by some gloomy analysis published in advance of the referendum by the UK government (HM Treasury 2016a,b).

Nonetheless, these market moves need to be seen in context. Sterling had already started to weaken in 2015 as a consensus emerged that the currency was overvalued. This was reflected in large current account deficits and below-target inflation, two problems which the fall in the pound at least helped to correct.

Moreover, in trade-weighted terms the fall in the pound between 2015 and 2016 did little more than reverse the rise since 2012. More than half the peak-to-trough fall in the value of the pound against the dollar over this period took place before the referendum result was known.

Figure 4: Sterling narrow effective exchange rate (2020 = 100)



Source: BIS.

Sterling has remained weak. But UK equity markets recovered quickly as the Bank of England cut interest rates, rather than raised them, and as the feared 'immediate recession' failed to materialise.

But beyond that initial shock, there is now a bewildering range of estimates for the harm that Brexit is assumed to have done to the UK economy, or the benefits of rejoining the EU. These studies can be divided into three types.

1. 'Crystal ball gazing'

Many studies were undertaken around the time of the referendum in 2016. These attempted to guess what the impact of Brexit might be using a wide range of models and assumptions, before the shape of any future agreement with the EU was even known.

The highest profile of these was the working assumption made by the OBR, which was that Brexit would reduce long-run productivity (specifically, GDP per head) by 4 per cent relative to remaining in the EU. However, this 4 per cent figure was simply a crude average of the results of 13 external studies. Even then, 9 of the 13 studies suggested the impact would be less than 4 per cent.

The OBR also assumed that both exports and imports would be around 15 per cent lower in the long run than if the UK had remained in the EU. This figure was also based on the average estimate of a number of external studies that looked at the impact of leaving the EU on the volume of UK–EU trade.

Crucially, the OBR's 15 per cent figure covered total trade in goods and services with the entire world, not just goods trade with the EU. A shock of this magnitude to the UK's global trade had always looked implausibly large, and it has indeed failed to

materialise. In particular, the UK's trade intensity (or 'openness') has continued to track that of similar countries, such as France.

2. 'Top down' (or doppelgänger) models

Several more recent studies have attempted to look back at the impact of Brexit by comparing the performance of the UK economy since 2016 to that of other countries and then attributing any divergence solely to Brexit.

The highest-profile example here is a paper published by the NBER last year, which suggested that GDP per head was 8 per cent lower than otherwise as a result of Brexit (Bloom et al. 2025).

The NBER paper used data for 33 advanced economies (the EU27, the US, Canada, Japan, Iceland, Norway and Switzerland) from 2006 to 2025, applying five different approaches. Four used data from all 33 economies, taking a simple unweighted average, a GDP weighted average, a gravity-weighted average (GDP divided by distance) and a trade-weighted average.

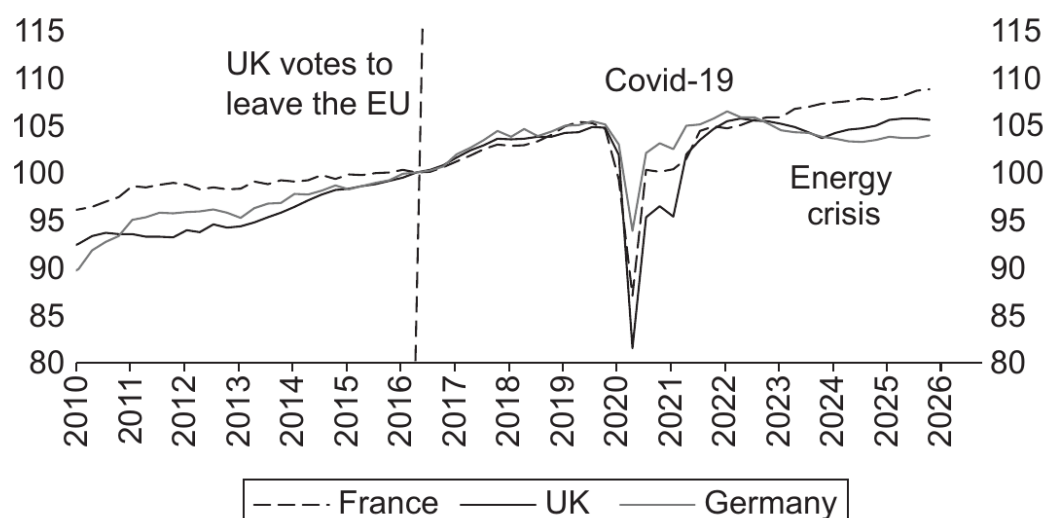
The fifth approach used a formal 'synthetic control model'. This is the most sophisticated version of a 'doppelgänger', where a computer algorithm is left to pick the weighted average of a subset of countries whose economic performance happened to match that of the UK most closely before 2016.

However, this approach simply cannot separate out the impact of Brexit from other reasons why some economies have grown more quickly (or slowly) than the UK since 2016.

These alternative explanations include the impact of the Covid pandemic and the energy crisis, and many others. For example, the US has benefited not just from relatively low energy but also from a large fiscal stimulus and the AI boom.

Care should be taken too when comparing the UK's economic performance since 2016 to that of countries hit hard by the euro area debt crisis of the early 2010s. The numbers for Italy, Spain and Greece in particular have been flattered by catch-up growth. The 8 per cent figure is implausibly large if you compare the actual performance of the UK economy to better matches such as France or Germany.

Figure 5: Real GDP per capita (Q2 2016 = 100)



Source: OECD.

3. Bottom-up studies

These studies have tried to calculate the impact of Brexit from the bottom up, using industry or sector level data. In principle, these studies might be better able to separate the impact of Brexit from other factors. But they are still flawed.

For example, the NBER paper also suggested that Brexit has reduced UK per capita GDP by 6 per cent (rather than 8 per cent) using an alternative approach based on micro-modelling. This drew on firm-level survey data from the Bank of England's Decision Maker Panel (DMP) survey. Any divergence in the performance of firms based on their pre-referendum exposure to the EU was then assumed to be due solely to Brexit.

The DMP is a relatively large survey, but the respondents are not necessarily representative of the UK economy as a whole. More importantly, divergences in the performance of individual firms depending on their exposure to the EU may also be picking up the relative weakness of major European economies over this period (especially Germany), or other factors such as the impact of the UK's relatively high energy costs on the competitiveness of goods which are mainly exported to the EU.

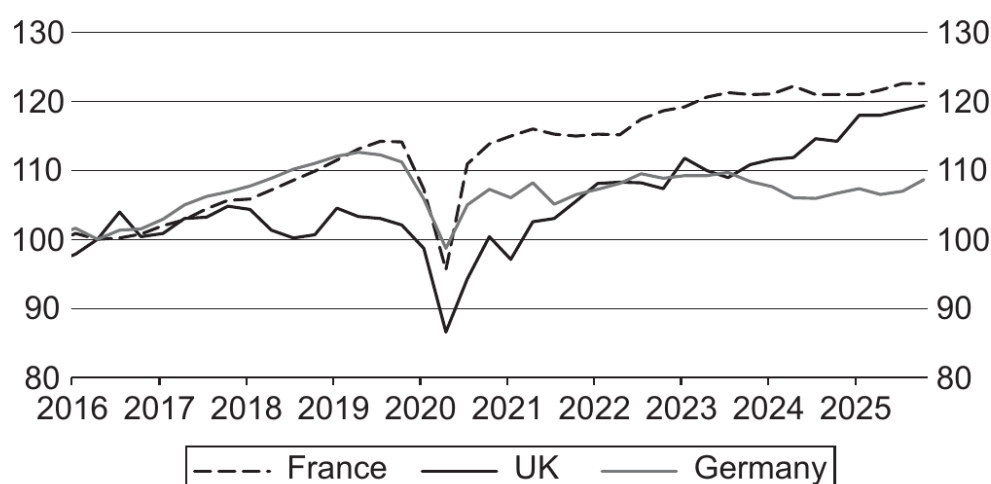
Finally, while the prospect of an increase in trade frictions with the EU will clearly have had some negative effects, these should prove to be (mostly) temporary as Brexit uncertainty fades and firms adjust to the new trading arrangements. Indeed, the DMP itself suggests that Brexit has dropped well down the list of concerns for most firms.

A better approach

Comparing the performance of just one country (the UK) to an average of many others is bound to gloss over all the alternative explanations for the differences. A more balanced view would look too at the performance of the UK economy compared to individual countries – especially those that might have been expected to perform similarly in the circumstances of the last ten years (not just in the ten before that).

Supporters of the doppelgänger approach, and especially the use of synthetic control models, argue that these techniques minimise the problem of ‘cherry-picking’ countries to fit a particular narrative. They are also widely used in other contexts.

Figure 6: Non-dwellings investment (Q2 2016 = 100)



Source: OECD.

But there is a trade-off here. There must be some role for judgement when it is obvious that other factors are at play. There may be a greater risk that leaning too much on computer models, or averages of as many as 33 very diverse economies, will stifle any intellectual curiosity.

Here then are some stylised facts.

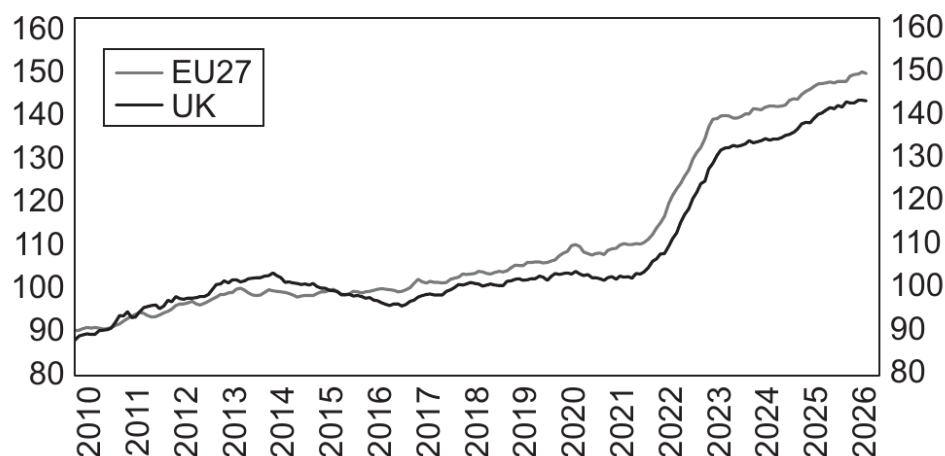
On investment, the UK lagged behind other comparable countries in the first few years after 2016, but then began to catch up again as Brexit uncertainty eased (although the stock of capital is still lower than it would otherwise have been).

On trade, the UK has underperformed on trade in goods with the EU, but also on trade in goods with the rest of the world beyond the EU. This suggests that the additional frictions in UK–EU trade have played a relatively small part.

Moreover, the UK has outperformed on trade in services, meaning that overall trade has held up much better than expected.

On inflation, any Brexit effect has been swamped by other factors. This is perhaps clearest if you look at food prices.

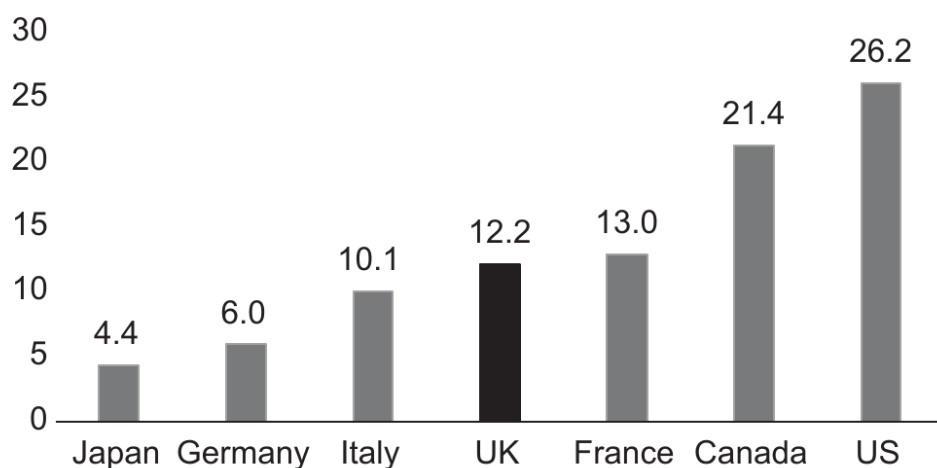
Figure 7: CPI food and non-alcoholic beverages (2015 = 100)



Source: ONS and Eurostat.

On total GDP, the UK economy has performed relatively well compared to other G7 economies in Europe. This largely reflects the initial surge in net immigration to the UK in the years after Brexit, confounding forecasts that migration would collapse.

Figure 8: Cumulative growth in real GDP (%) between Q2 2016 and Q4 2025



Source: OECD.

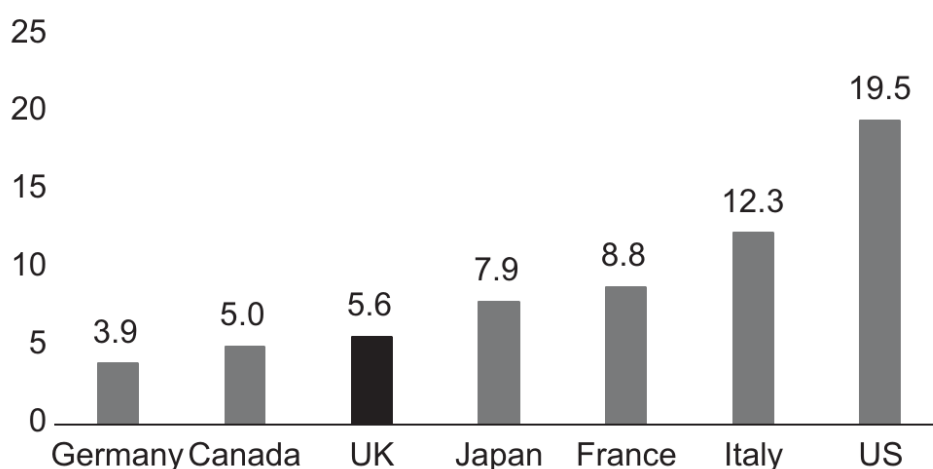
On per capita GDP, the UK has performed relatively poorly, but has still continued to track between France and Germany, while keeping pace with Canada. As noted earlier, Italy's faster growth since 2016 is partly just catch-up after the big hit from the euro debt crisis of the early 2010s. It has also been flattered by a huge fiscal stimulus.

Conclusions on Brexit

Many people want to believe that leaving the EU has been a disaster for the UK and are happy to blame Brexit for all the UK's problems. This involves exaggerating the costs while downplaying the benefits, both now and in the future.

It is more helpful to compare the performance of the UK to individual countries with similar characteristics, such as France, Germany and Canada.

Figure 9: Cumulative growth in real GDP per capita (%) between Q2 2016 and Q4 2025



Source: OECD.

This shows that Brexit has largely been a non-event in macroeconomic terms. Indeed, the real story is how little impact leaving the EU has had. This makes sense, because relatively little has actually changed.

The consensus also assumes that the costs of Brexit will only grow over time. In fact, there is already plenty of evidence that the headwinds are fading.

In particular, the initial uncertainty created by the vote to leave and the prolonged negotiations thereafter was a drag on business investment. But this drag is now lifting as Brexit uncertainty has eased.

Similarly, firms are adjusting to the new trading arrangements and have found alternatives to EU workers. The OBR's assumption that global exports and imports would be 15 per cent lower than otherwise simply has not materialised. Labour shortages have eased too.

There is no serious discussion of the potential benefits of Brexit. At most, the benefits of new trade deals are dismissed. But there is rarely even any acknowledgement of the scope for regulatory improvements – as already seen in sectors as diverse as financial services, life sciences, and animal welfare. And there is huge scope to do better in growth areas, such as AI.

Last but not least, the savings on budget contributions will also only get bigger as the EU expands.

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