

# Ten key facts about debt in the UK

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## Introduction

Since the global financial crisis of 2007-08, debt has been one of the main issues facing the UK economy, from the private sector debts which caused the crisis, to the impact the crisis has had on UK government debt.

We campaign to prevent debt burdens increasing poverty. In the UK, debt is a crucial factor lying behind determinants of poverty, from high personal debt burdens on low income households, to government policies which negatively impact on people in low incomes but which are introduced in the name of reducing the UK government's debt. As and when debt crises arise, as in 2007-08, their impact is to reduce incomes, and thereby potentially increase poverty.

Jubilee Debt Campaign has worked to end and prevent debt crises across the world, from Argentina to Zambia, Ghana to Greece. This briefing applies Jubilee Debt Campaign's experience of working to prevent and end debt crises in other countries to the analysis of the debt problems and opportunities facing the UK economy.

In all the debt crises we have worked on, whether in developing countries or richer countries such as Greece, the main risk has been debts owed outside the country. These debts are particularly dangerous because they lead to money flowing out of the country in interest and principal payments. Also, loans from abroad which have been helping to prop-up an economy can suddenly stop, either because of a change domestically, or more likely, a change in financial markets elsewhere in the world.

Throughout this briefing 'the UK' means all of the UK – public (the government) and private (individuals and companies) sectors resident in the UK. UK government is used when just the government is being referred to, UK private sector (which includes personal debts) when just the private sector. All the facts come from official sources, primarily the UK's Official for National Statistics, HM Treasury and Bank of England, and International Monetary Fund and World Bank.

The ten key facts we believe everyone should know before discussing debt issues in the UK are:

1. A quarter of UK government debt is owed to the UK government itself (Page 2)
2. Three-quarters of UK government debt is owed to people and institutions in the UK (Page 3)
3. Of G7 economies, only Germany has a lower government debt (as a proportion of GDP) than the UK (Page 4)
4. The UK government can currently borrow at the cheapest interest rates in its history (Page 5)
5. The UK government is paying virtually the lowest *amount* of interest on its debt in recorded history, as a proportion of GDP (Page 7)
6. UK government tax revenue (as a proportion of GDP) is the third lowest of G7 countries, and well behind other European countries (Page 7)

7. The debt of the UK's private sector is more than four times as big as that of the government (Page 10)
8. Unsecured personal debt in the UK is rising rapidly (Page 11)
9. The UK economy has the largest deficit with the rest of the world of any rich country (Page 12)
10. The UK's finance sector is the most exposed to a crisis of any G7 economy (Page 14)

## **1. A quarter of UK government debt is owed to the UK government itself**

The IMF say that the UK government's debt at the end of 2017 will be £1,795 billion, which is 89% of GDP.<sup>1</sup> Of the UK government's debt, almost one-quarter is owed to the UK government itself, via the Bank of England. The debt owed to the Bank of England, which is a "corporation wholly owned by the UK government"<sup>2</sup> comes from the quantitative easing policy. At the start of 2009, the Bank of England began creating money with which it bought UK government bonds. This was intended as a means to stimulate the economy to aid recovery from the financial crisis of 2007-2008. Since 2009, £435 billion has been created to buy UK government bonds,<sup>3</sup> most recently £60 billion since the June 2016 vote to leave the European Union.<sup>4</sup>

Almost no interest is paid by the government on the debts owed to the Bank of England. All interest payments above the Bank of England's base rate on these debts are returned by the Bank of England to the government.

Furthermore, the amount of debt owed to the Bank of England does not fall when the debts are repaid. When these debts are repaid<sup>5</sup>, the UK government pays the Bank of England. The Bank of England then uses this money to buy other government bonds on secondary debt markets, keeping the total amount of debt owed by the UK government to the Bank of England the same.<sup>6</sup>

By buying up assets, the impact of quantitative easing was to increase the value of those assets. Therefore, the most gains from the policy went to those who already owned assets, the rich. The Bank of England's own report has found that 40% of the value of quantitative easing has gone to the richest 5% of households.<sup>7</sup>

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<sup>1</sup> IMF World Economic Outlook database. Accessed on 30 October 2017.

<sup>2</sup> <http://www.bankofengland.co.uk/about/Pages/default.aspx>

<sup>3</sup> A 'bond' is a kind of way that governments and companies borrow. To take the example of a government, it borrows money in return for issuing a contract saying it will repay the money in full in a certain number of years (eg, 10) and interest every year until then (eg, 3%). This contract is known as a 'bond'. The bond is then tradable. Whoever initially lent the money usually sells the bond on. Such bonds are being bought and sold in their millions every day on financial markets. The current owner of a bond is called a 'bondholder'.

<sup>4</sup> <http://www.bankofengland.co.uk/markets/Pages/apf/default.aspx> In addition £10 billion has been created to buy corporate bonds.

<sup>5</sup> ie, when the bond matures

<sup>6</sup> For example, see <http://www.bankofengland.co.uk/markets/Documents/marketnotice151105.pdf>

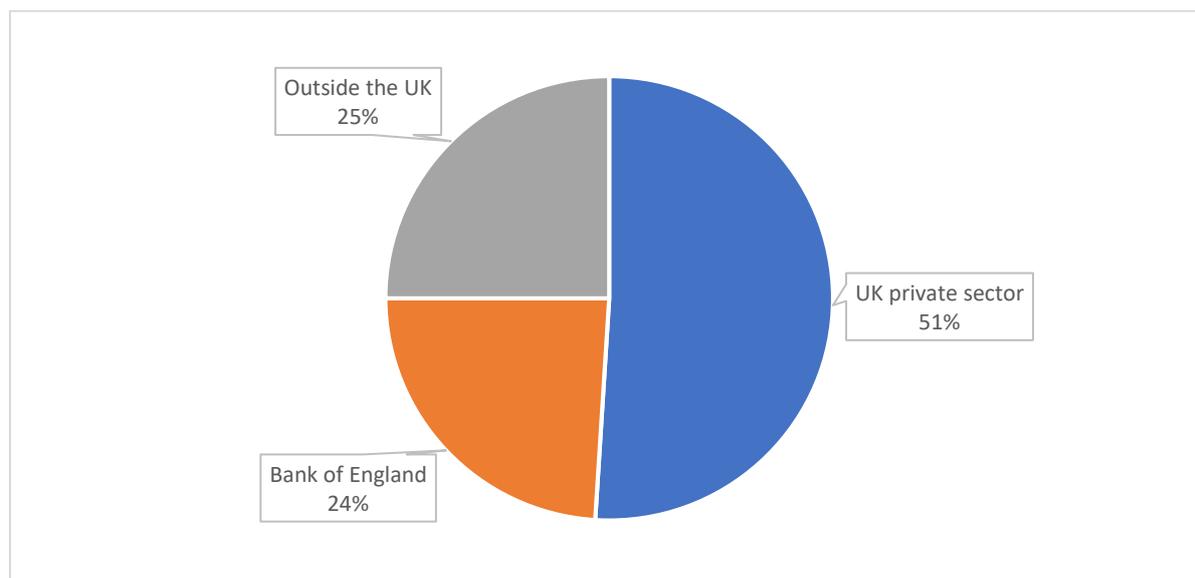
<sup>7</sup> <http://www.theguardian.com/business/2012/aug/23/britains-richest-gained-quantitative-easing-bank>

## 2. Three-quarters of UK government debt is owed to people and institutions in the UK

Government debt is sometimes referred to as “national debt” but this is extremely misleading. A large majority of UK government debt is owed to people and institutions in the UK, not by the UK government to other nations.

According to the UK Treasury, around 25% of the government’s debt is owed to people and institutions outside the UK.<sup>8</sup> Accounting for the 24% owed to the Bank of England, the remainder - 51% - is owed to the UK private sector, primarily pension funds and insurance funds (24%), but also UK households (13%), banks (8%) and other companies (6%).<sup>9</sup>

**Graph 1. Who UK government debt is owed to by sector, as of end-2016<sup>10</sup>**



Government debt owed externally is more risky as:

- External debt leads to flows of resources out of a country (whereas domestic debt is the movement of resources within a country)
- External lending is more likely to be volatile, influenced by changes elsewhere in the world

Two related but separate issues are the currency debt is owed in and the law it is owed under. Virtually all<sup>11</sup> UK government debt is owed in pounds, the creation of which are controlled by the UK

<sup>8</sup> The UK government says 27% of GILTs are owed to overseas investors [https://www.gov.uk/government/uploads/system/uploads/attachment\\_data/file/597297/debt\\_management\\_report\\_2017-18\\_web.pdf](https://www.gov.uk/government/uploads/system/uploads/attachment_data/file/597297/debt_management_report_2017-18_web.pdf) This does not include the 9% of debt owed through National Savings and Investments to UK citizens. Including this means 25% is owed to overseas investors.

<sup>9</sup> As above, calculated from [https://www.gov.uk/government/uploads/system/uploads/attachment\\_data/file/597297/debt\\_management\\_report\\_2017-18\\_web.pdf](https://www.gov.uk/government/uploads/system/uploads/attachment_data/file/597297/debt_management_report_2017-18_web.pdf)

<sup>10</sup> Except for the amount owed to the Bank of England, this is all calculated from [https://www.gov.uk/government/uploads/system/uploads/attachment\\_data/file/597297/debt\\_management\\_report\\_2017-18\\_web.pdf](https://www.gov.uk/government/uploads/system/uploads/attachment_data/file/597297/debt_management_report_2017-18_web.pdf) According to the Bank of England it owns £435 billion of UK government debt, which is 24% of £1,795 billion. <http://www.bankofengland.co.uk/markets/Pages/apf/default.aspx>

<sup>11</sup> The government has issued a small amount of debt owed in the Chinese renminbi, but this was part of its efforts to make London into a global centre for trading renminbi assets, rather than because it needed Chinese currency.

government. Unlike many other countries, which borrow in foreign currencies, because UK government debt is owed in the currency it controls, debt payments cannot suddenly increase if the pound devalues against other currencies.

All UK government debt is owed under English law. This means in the highly unlikely event that the government needed to restructure the debt, it could manage the process through UK legislation. This also means it would not be at risk of vulture funds preventing any debt reduction, as has been the case for other countries facing debt crises, for example Greece, Argentina, Liberia, Zambia and the Democratic Republic of Congo.

**Box. Domestic v. external debt: The cases of Japan and Greece**

Japan has the largest debt of any government as a proportion of national income: 239%.<sup>12</sup> However, most of this is either owed to the Japanese government itself or savers in Japan, which means it does not cause the country to have a financial imbalance with the rest of the world. Japanese government debt does not lead to significant financial flows out of the country, and does not require large loans from outside the country to keep paying it. Furthermore, the Japanese government can still borrow at very low interest rates. The Japanese government's external debt is just 28% of GDP<sup>13</sup> (and so 12% of the total debt). It can borrow at interest rates of 0% for ten years, or even -0.1% for five years.<sup>14</sup>

In contrast, Greece's government debt is very large, but less than Japan's – 181% of GDP.<sup>15</sup> However, almost all of this is owed outside Greece, primarily to EU institutions and the IMF. Greece's large government external debt is why it has had a debt crisis for the last seven years, and why it is unlikely the crisis will end unless there is large scale cancellation of the external debt.<sup>16</sup>

### 3. Of G7 economies, only Germany has a lower government debt than the UK

Despite growing significantly after the 2007/08 financial crisis (see point 6) by international and historical standards, UK government debt is still relatively low. The UK government has the second lowest debt of any country in the G7 proportionate to the overall size of the economy (see Graph 2. below). This remains the case if debt owed to a government's own central bank is excluded.<sup>17</sup>

Historically, the UK government's debt has been significantly higher. It increased above 100 per cent of GDP by the end of the First World War, going over 150% in the 1920s and 1930s. It reached a high of well over 200% of GDP at the end of the Second World War, and only fell below 100% in the 1960s. The fall in the size of the debt in the 1950s and 1960s was largely due to inflation and

<sup>12</sup> IMF. World Economic Outlook database.

<sup>13</sup> World Bank. Quarterly External Debt Statistics database SDDS

<sup>14</sup> <https://www.bloomberg.com/markets/rates-bonds/government-bonds/japan> A negative interest rate means the lender is effectively paying the Japanese government to lend to it. This is not done through paying the 'negative interest' every year, but instead through more lending more than will ultimately be repaid when the bond matures (and no interest in between).

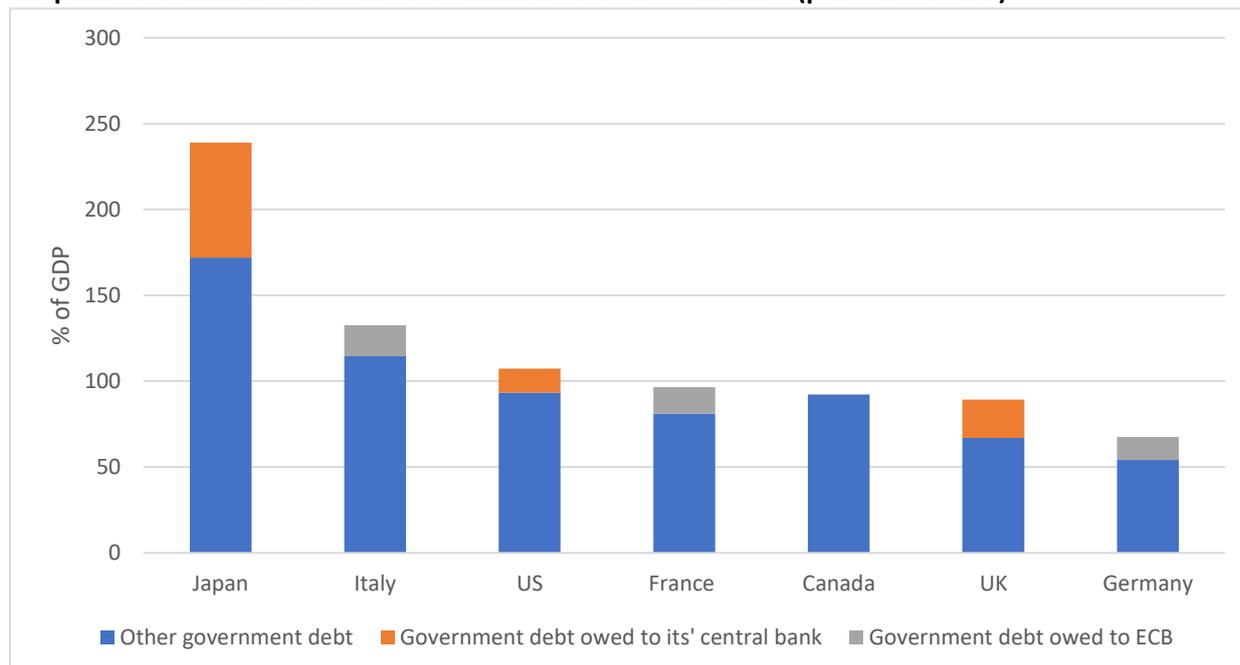
<sup>15</sup> IMF. World Economic Outlook database.

<sup>16</sup> For more on Greece see: Jubilee Debt Campaign. (2016). The Never-Ending Austerity Story: Why Greece's third 'bailout' changes nothing. <http://jubileedebt.org.uk/reports-briefings/briefing/the-never-ending-austerity-story-why-greeces-third-bailout-solves-nothing>

<sup>17</sup> As argued above, and by Lord Skidelsky, see <https://www.project-syndicate.org/commentary/rising-debt-unfounded-fears-by-robert-skidelsky-2016-01> Arguably debt owed to the ECB should not be counted as owed to the government's own central bank, as the ECB is not majority owned by any Eurozone government, and unlike in the UK, US and Japan, Greece has been made to repay the ECB just as if it were like any other creditor.

economic growth reducing the size of the debt as a % of GDP, rather than large government surpluses.

**Graph 2. Government debt owed at end-2016 for G7 economies (per cent of GDP)<sup>18</sup>**



However, measuring the size of government debt as a proportion of GDP is not very helpful, as this takes no account of the cost of the debt – the size of debt payments relative to income – or where those payments are going, ie, whether to people and institutions in the same country, or leaving the country. Instead, it is better to look at the costs of debt payments, and the size of debt owed outside a country.

#### 4. The UK government can currently borrow at the cheapest interest rates in its history

The interest rates the UK government can borrow at have been falling since 2007, and are at their lowest level ever.

Before the 2007-2008 financial crisis the UK government could borrow at an interest rate, fixed for ten years, of between 4% and 5%. From 2009 to 2011 this fell to 3% to 4%. In the second-half of 2011 the rate fell substantially, and then varied between 1.5% and 2.5% (see Graph 3. below). Since the June 2016 vote to leave the EU rates have fallen again, varying between 0.7% and 1.5% (and at the time of writing are 1.3%). According to the Financial Times, recent years have seen the lowest government borrowing costs in the UK's history.<sup>19</sup>

UK government debt is bought and held by a range of actors, including pensions funds, savers and speculators, and their desire to lend to the UK government is influenced by various factors. Lenders to the UK government are willing to accept a relatively low interest rate because UK government debt is one of the safest assets they can put their money into. Unlike most developing countries, the UK government controls the creation of the currency in which its debt is owed – sterling. This means

<sup>18</sup> Debt figures are from the IMF World Economic Outlook database. Debts owed to Central Banks are from the Bank of Japan, US Federal Reserve, Bank of England and European Central Bank.

<sup>19</sup> <https://www.ft.com/content/ef568030-a7a8-11e4-be63-00144feab7de>

it is extremely unlikely the UK government would default on such £ denominated debt. The risk of holding UK government debt is if inflation erodes its value.

**Graph 3. Interest rate paid on new UK government borrowing, fixed for 10 years<sup>20</sup>**



The fact that the UK government controls the creation of pounds sterling, and also that it has guaranteed tax revenue, mean that UK government debt is a very safe asset (alongside or just behind government debt of other countries who can also borrow in the currency they control, such as the US, Switzerland and Japan). At times of fragility and crisis, speculators are more likely to put their money into safe government debt.

UK government debt has been a safe haven during and since the financial crisis – a vital asset to store money through. For savers, particularly UK pension funds, it will continue to be a secure long-term asset, passed down through the generations as one generation cashes pension funds in and the next pays into them.<sup>21</sup>

The fact that most UK government debt is owed within the UK, all of it as pounds sterling, means that the government is at little risk of sudden increases in interest rates based on international financial flows. More likely is that economic shocks in the rest of the world will reduce UK government interest rates further as UK government debt continues to be a safe haven. When risks increase in other assets – from company shares to housing and real estate – savers and speculators take money out of those assets and put them in safe assets such as UK government debt. Whenever there are new events which reduce economic confidence – such as the vote to leave the EU – the interest rate on new UK government borrowing has fallen.

However, increasing UK government debt does have a distributional impact by transferring money from future taxpayers to the owners of the debt, which tends to be the rich. For example, 72% of pension fund wealth is owned by the wealthiest 20% of the population.<sup>22</sup> With UK government interest rates at low levels, this is not currently a large impact. Furthermore, interest rates are

<sup>20</sup> Figures from [www.uk.investing.com](http://www.uk.investing.com)

<sup>21</sup> It would be devastating for safe saving in the UK if UK government debt were substantially paid off.

<sup>22</sup> <https://www.nestpensions.org.uk/schemeweb/NestWeb/includes/public/docs/Cox-Private-pension-wealth,PDF.pdf>

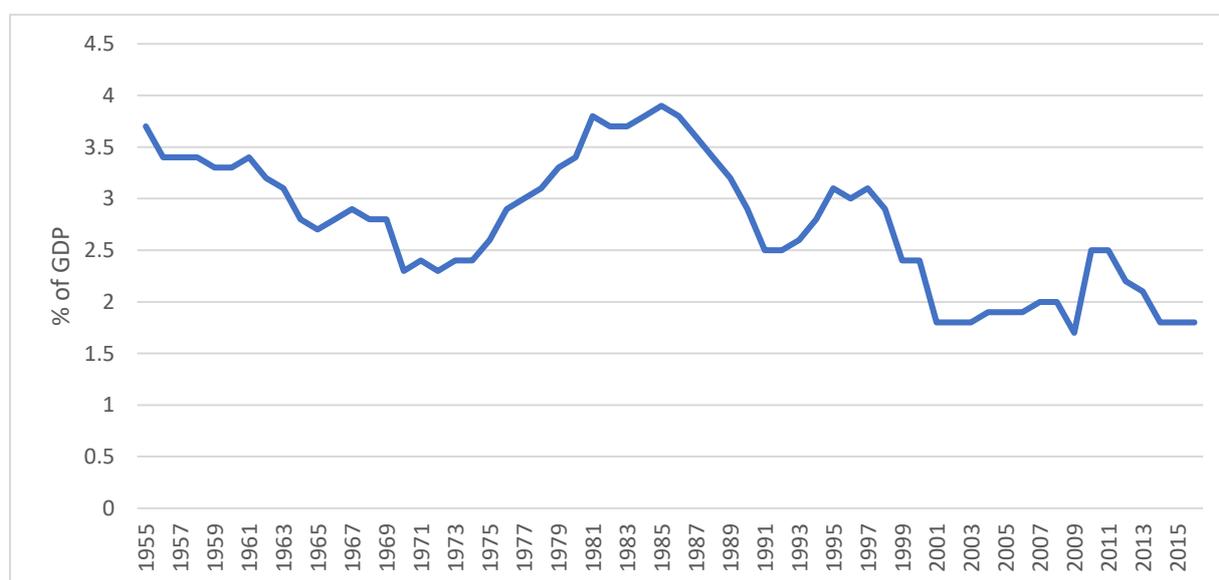
currently below inflation, so actually government debt acts to transfer money in real terms from savers to the government.

## 5. The UK government is paying virtually the lowest *amount* of interest on its debt in recorded history, as a percentage of GDP

The UK government is currently paying 1.8% of GDP in interest every year. This is the second joint lowest amount since records begin in 1955. The lowest was 2009 when it was 1.7% (see Graph 4. below). The other time interest payments were 1.8% of GDP was 2001-2003. This lower level of interest payments, despite the higher debt as a percentage of GDP is because:

- The interest rate paid on new government borrowing has fallen (see fact 4 above)
- A quarter of UK government debt is now owed to the Bank of England (see fact 1 above), on which the government only pays interest at the Bank of England base rate (now 0.5%) which is significantly lower than the interest owed under most of the debt contracts bought by the Bank of England

**Graph 4. Interest paid by the UK government as a percentage of GDP, 1955-2016<sup>23</sup>**



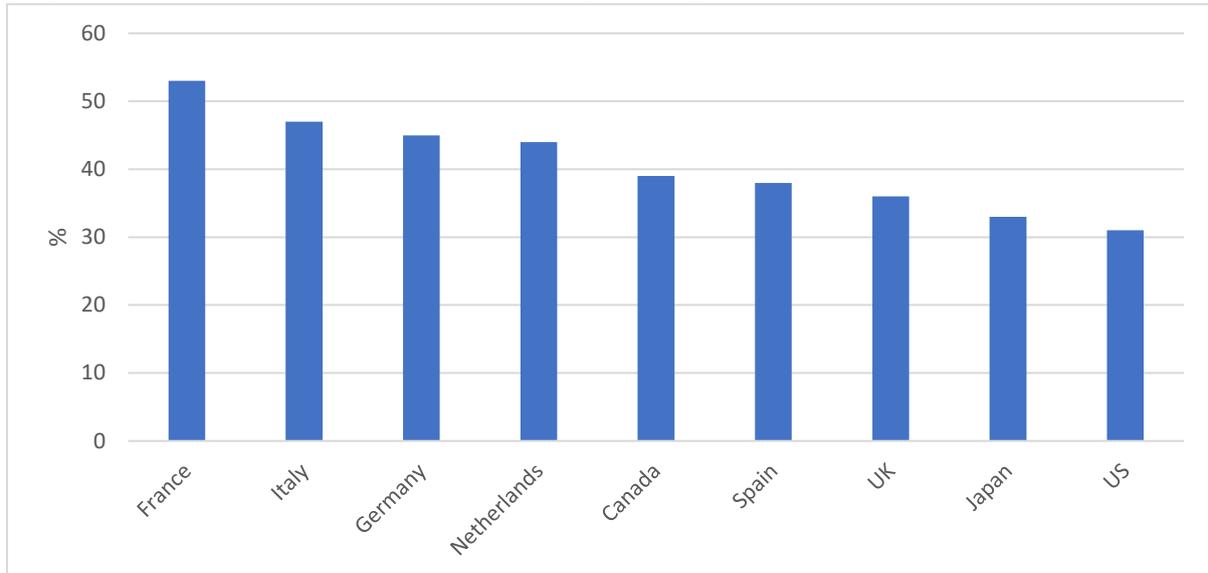
## 6. UK government tax revenue is the third lowest of G7 countries and well behind other European countries

The UK government continues to have one of the lowest tax revenue collection rates of major rich economies, as a percentage of GDP (see Graph 5. Below). On current government plans, tax revenue is projected to stay stagnant at 36% of GDP, at a time of increasing financial burdens from pensions and healthcare because of an aging population. The percentage of the population who are over 60 is projected by the Office for National Statistics to increase from 23.2% in 2015 to 26.1% by 2025.<sup>24</sup> Maintaining government revenue at the same level alongside an aging population will mean there is relatively less money available for public spending, including on pensions and healthcare.

<sup>23</sup> <http://researchbriefings.files.parliament.uk/documents/SN05745/SN05745.pdf> The figures used are those net of the Asset Purchase Facility, ie, accounting for the fact that most of the interest payments on debt owed to the Bank of England are returned to the UK government.

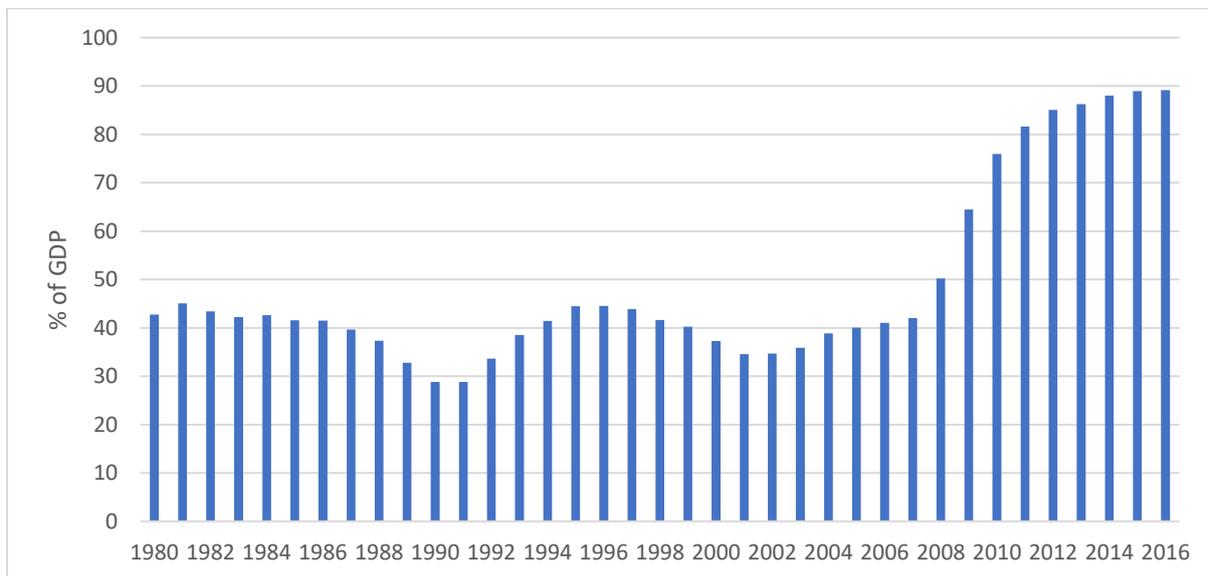
<sup>24</sup> <http://ons.gov.uk/ons/rel/npp/national-population-projections/2014-based-projections/stb-npp-2014-based-projections.html>

**Graph 5. Government tax revenue in 2016 as a percentage of GDP<sup>25</sup>.**



It was the fall in tax revenues because of the post-crisis contraction of the economy which created the large UK government deficit following the financial crisis of 2007-2008. Between the mid-1990s and 2007, UK government debt fell as a percentage of GDP, from 45% in 1996 to 42% by 2007 (see Graph 6. below). The debt then began to rise rapidly in 2008 after tax income collapsed. Between 2008 and 2009 government revenue fell by £58 billion (in 2014 £ terms), from £635 billion to £577 billion (by 9%).<sup>26</sup>

**Graph 6. UK government debt as a percentage of GDP, 1980 – 2016<sup>27</sup>**



Government debt inevitably increases during a sizeable financial crisis because of the collapse in government revenues. The government continuing to spend helps to protect more people from the impacts of the, hopefully temporary, recession, by keeping more demand in the economy and so fewer people lose jobs than would otherwise be the case. The deficit would then be expected to fall

<sup>25</sup> IMF World Economic Outlook Database. Accessed on 14/06/17

<sup>26</sup> Figures from IMF World Economic Outlook, amended to 2014 £.

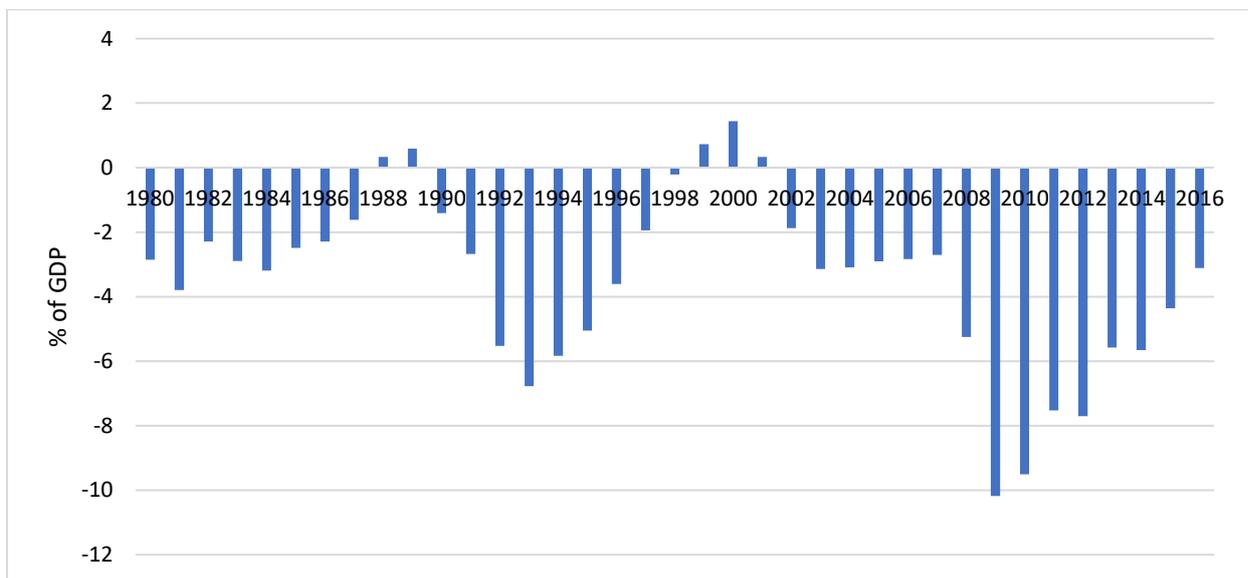
<sup>27</sup> IMF World Economic Outlook database. Accessed on 13/06/17.

as the economy recovers, and once the economy has recovered it becomes prudent to have a small surplus to help reduce government debt (alongside moderate inflation and growth which will also reduce the debt).

The size of the UK economy per person has only just returned to 2007 levels, which has led economist David Blanchflower to call it the slowest and worst economic recovery in the UK since the South Sea bubble in 1720.<sup>28</sup> Therefore, a government deficit would be expected, and be necessary, until the economy has grown substantially more.

In the 27 years from 1980 to 2016, the UK government has had a deficit in all but five years, when instead there were small surpluses (1988-89 and 1999-2001) (see Graph 7. below). Despite this, in the mid-1980s and mid-1990s the overall debt fell despite there being a deficit, because the rate of economic growth and inflation was higher than the deficit.

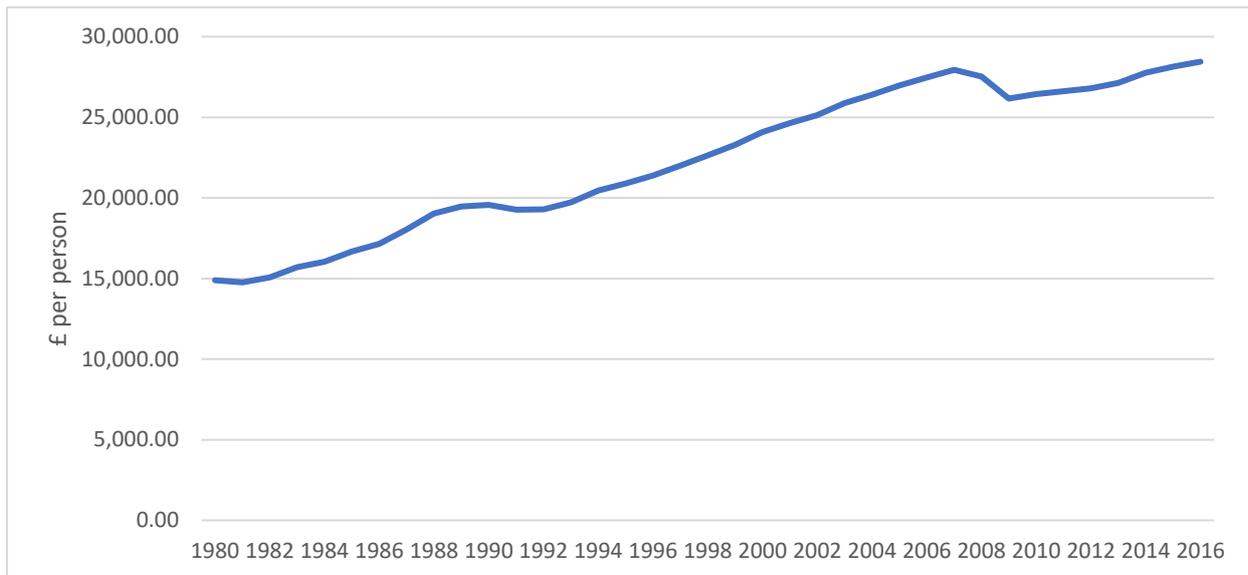
**Graph 7. UK government cash deficit, percentage of GDP, 1980-2016<sup>29</sup>**



<sup>28</sup> <http://www.independent.co.uk/voices/comment/britain-has-taken-longer-to-recover-from-recession-than-at-any-time-since-the-south-sea-bubble-9645218.html>

<sup>29</sup> IMF World Economic Outlook database. Accessed on 13/06/17.

**Graph 8. UK GDP per person, constant £, 1980 - 2016**



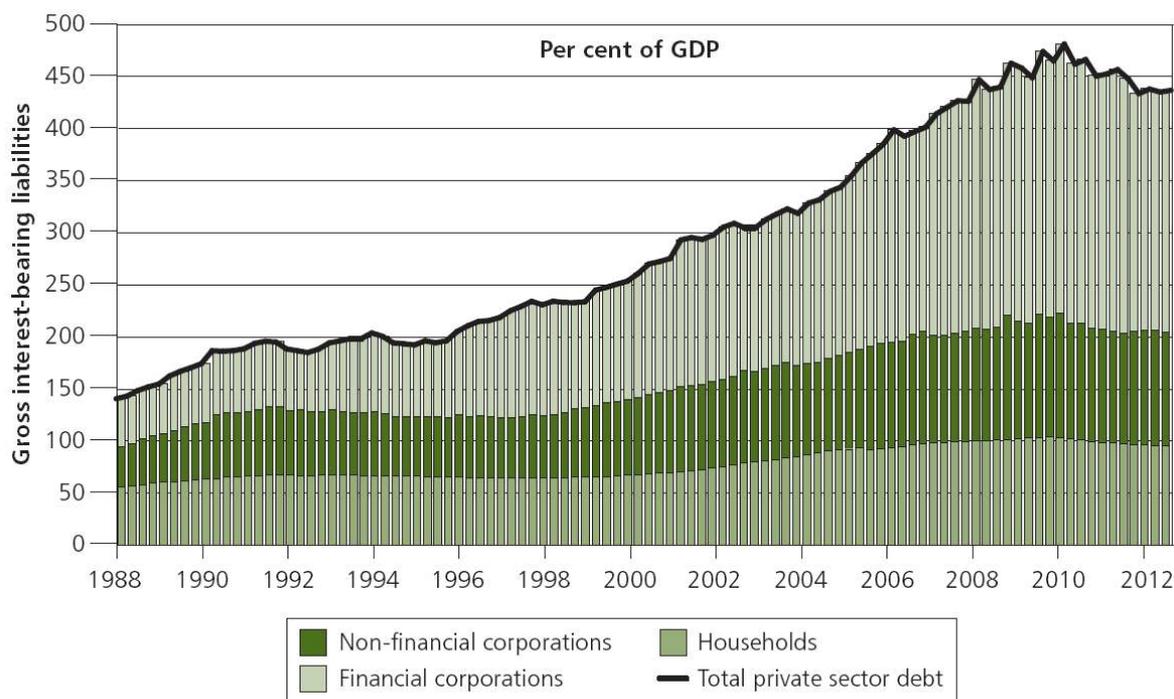
## **7. The debt of the UK's private sector is more than four times as big as that of the government**

The total debt of the UK's private sector debt, ie, companies and households, is estimated to be over 400% of GDP, more than four times the size of UK government debt. At the end of the 1980s private sector debt was 150% of GDP, but it then grew to over 450% of GDP by the financial crisis of 2008/2009 (see Graph 9. below).

These figures all come from the budget documents produced by the UK Treasury. However, these figures have not been included in the Budget since 2013. While there are up-to-date official figures on the debt of UK households and non-financial corporations, we cannot find such figures for financial corporations. According to the OECD, the debt of UK households and non-financial corporations was 231% of GDP in 2016. This is up slightly on the level in 2007 (224% of GDP) and 2013 (222% of GDP),<sup>30</sup> indicating that total UK private sector debt is likely to, if anything, have risen since the Treasury stopped publishing the data in 2013.

<sup>30</sup> <http://stats.oecd.org/index.aspx?queryid=34814>

**Graph 9. UK private sector debt 1988-2013, percentage of GDP<sup>31</sup>**



## 8. Unsecured personal debt in the UK is rising rapidly

Unsecured debt<sup>32</sup> is increasing rapidly (see Graph 10. below). Of personal debts, unsecured lending (also known as consumer credit) has been growing particularly rapidly. The annual growth rate was 8.2% in the year to September 2015,<sup>33</sup> 10.3% in the year to September 2016,<sup>34</sup> and 9.9 % in the year to September 2017.<sup>35</sup>

Total unsecured personal debt is now £204 billion,<sup>36</sup> which is £4,250 per adult in the UK. It has increased from £157 billion in mid-2013,<sup>37</sup> an increase of 30%.

<sup>31</sup> HM Treasury. (2013). Budget 2013 <https://www.gov.uk/government/publications/budget-2013-documents>

<sup>32</sup> Unsecured debt is any debt not guaranteed by an asset such as a house. It therefore excludes mortgages but includes personal loans, credit cards and pay-day loans.

<sup>33</sup> <http://www.bankofengland.co.uk/statistics/Pages/mc/2015/sep.aspx>

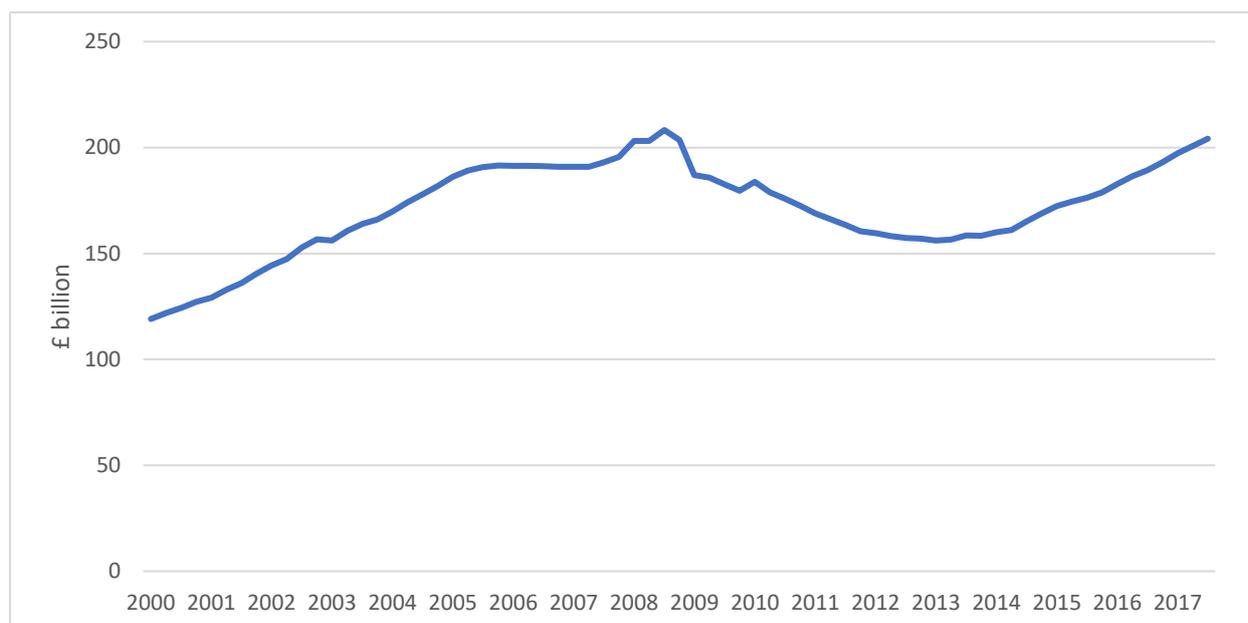
<sup>34</sup> <http://www.bankofengland.co.uk/statistics/Pages/mc/2016/sep.aspx>

<sup>35</sup> <http://www.bankofengland.co.uk/statistics/Pages/mc/2017/sep.aspx>

<sup>36</sup> <http://www.bankofengland.co.uk/statistics/Pages/mc/2017/sep.aspx>

<sup>37</sup> <http://www.bankofengland.co.uk/boeapps/iadb/FromShowColumns.asp?Travel=NlxSSx&SearchText=bl20>

**Graph 10. Unsecured personal in the UK, 2000-2017<sup>38</sup>**



## **9. The UK economy has the largest deficit with the rest of the world of any rich country**

The current account balance measures how much the UK (the public and private sector) is sending to the rest of the world each year through buying imports and making debt and profit payments, and how much it is earning through exports and receiving debt and profit payments.

If there is a current account deficit this means that the UK as a whole (private and public sectors) is borrowing from the rest of the world or selling things people in the UK own, to people outside the UK.<sup>39</sup> It is this borrowing or sale of assets which enable the UK to consume more from the rest of the world than it is earning from the rest of the world.

In 2016, the UK had a current account deficit of 4.4% of GDP. According to the IMF, this is the highest of any rich country (see Graph 11. below). Of other G7 countries, Canada had a deficit of 3.3% in 2016, the US 2.6% and France 1.1%. Italy had a surplus of 2.7%, Japan 3.9% and Germany 8.5%.<sup>40</sup>

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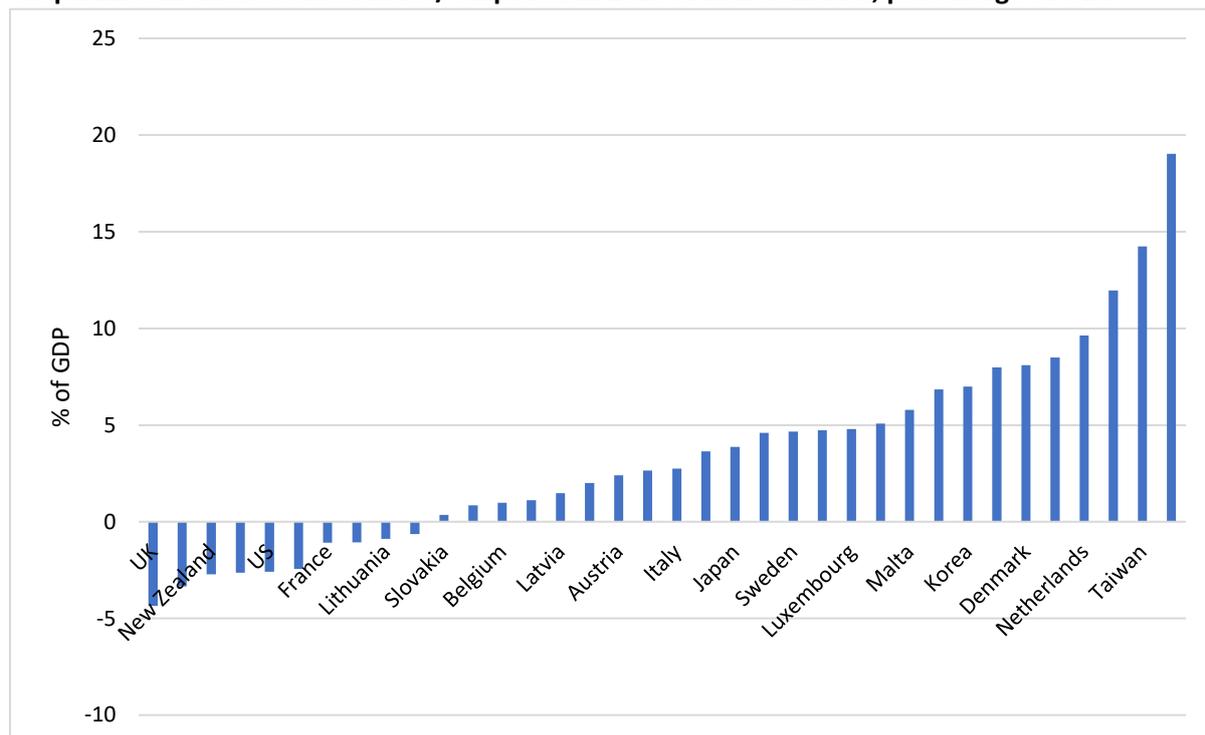
<sup>38</sup> Data from

<http://www.bankofengland.co.uk/boeapps/iadb/FromShowColumns.asp?Travel=NlxSSx&SearchText=b120>

<sup>39</sup> Most likely both of these things.

<sup>40</sup> IMF World Economic Outlook database.

**Graph 11. Current account deficits / surpluses in 2016 of rich countries, percentage of GDP<sup>41</sup>**



The impact of the whole UK economy spending more than it earns from the rest of the world is to increase debts owed outside the UK, or to sell-off UK assets to speculators from outside the UK, which then leads to interest and profits being sent out of the country in the future. Whilst a current account deficit allows the UK to consume more now, it is at the cost of reducing income in the future. Furthermore, if speculators suddenly reduce their willingness to lend to the UK economy, or buy UK assets, it can lead to a sudden drop in income in the UK, and so recession.

Governor of the Bank of England Mark Carney has said that the UK's large current account deficit means the country is dependent on "the kindness of strangers".<sup>42</sup> However, this is not quite right. Those outside the UK lending to the UK, or buying UK assets, are not doing so out of kindness, but in anticipation of receiving more back in return in the future.

The UK's current account deficit of 4.4% of GDP in 2016, was the joint highest on record, tied with 2013 and only beaten by 4.7% in 2014. Before 2013, the deficit had only gone over 4% once before, in 1989, during the boom just before the 1990s recession.<sup>43</sup> The Office for National Statistics<sup>44</sup> estimates the UK had an even higher deficit in 2016, 5.9% of GDP, the highest since records began.<sup>45</sup>

What is striking about the current record high deficits is that they have not even funded an economic boom.

<sup>41</sup> IMF World Economic Outlook database.

<sup>42</sup> <https://www.theguardian.com/business/2016/jan/26/mark-carney-fails-to-rule-out-eight-year-term-at-bank-of-england>

<sup>43</sup> ONS. Balance of payments time series dataset

<https://www.ons.gov.uk/economy/nationalaccounts/balanceofpayments/datasets/balanceofpayments>

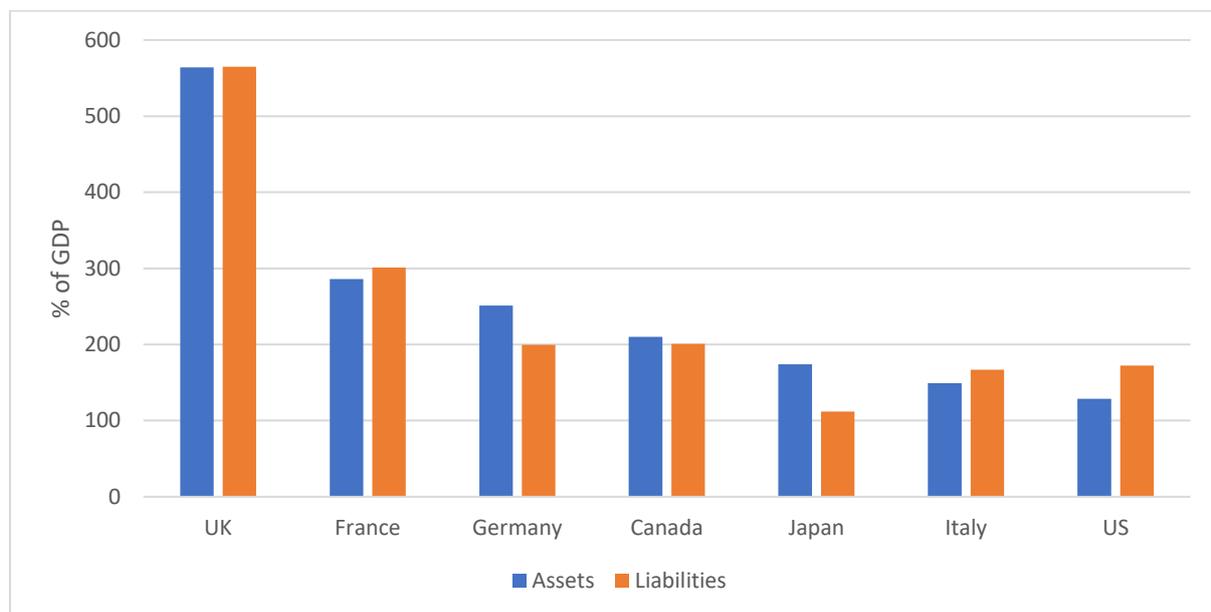
<sup>44</sup> We have focussed on the IMF figures as these are comparable between countries.

<sup>45</sup> <https://www.ons.gov.uk/economy/nationalaccounts/balanceofpayments/timeseries/aa6h/pb>

## 10. The UK's finance sector is the most exposed to a crisis of any G7 economy

The UK economy is the most exposed to global financial volatility of any major economy. In total, the UK economy (public and private sector) have the equivalent of 565% of GDP of financial liabilities to the rest of the world, and claim 564% of GDP as assets (most of these comes from the finance sector). This is significantly higher than the assets and liabilities of France, the next most exposed major economy, and more than double those of Germany (see Graph 12. below). Financial shocks, such as the fall in value of those assets, could rapidly and negatively affect the UK economy if they led to a fall in income for UK companies, even resulting in bankruptcy of major companies. In 2007-2008 it was the fall in value of such foreign held assets which led to the effective bankruptcy of UK banks.

**Graph 12. External assets and liabilities of G7 economies, end-2016, percentage of GDP<sup>46</sup>**



The ONS recently revised its estimate of assets and liabilities, which led to a change from a surplus of £470 billion (24% of GDP) to a deficit of £22 billion (1% of GDP).<sup>47</sup> This re-estimate led to headlines of “Britain’s missing £490 billion.” However, the real problem is not whether there is a small deficit or surplus, but the huge scale of the UK’s external assets and liabilities, such that re-estimates can lead to changes of the magnitude of £490 billion.

For example, if we imagine there was a 20% fall in the value of external assets held by all the G7 economies, this would leave the UK with net liabilities of 114% of GDP. France’s would be 72%, the US’s 69%, Italy 47% and Canada 32%. Germany and Japan would still have net assets of 2% and 27% respectively. This makes the UK uniquely vulnerable to financial changes elsewhere in the world.

<sup>46</sup> Assets and liabilities data from IMF database <http://data.imf.org/regular.aspx?key=60947518> GDP data from IMF World Economic Outlook database.

<sup>47</sup> <https://blog.ons.gov.uk/2017/10/23/has-500-billion-really-gone-missing/>