

March 2016 Economic and Fiscal Outlook Briefing

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Good afternoon ladies and gentlemen.

My name is Robert Chote, Chairman of the OBR, and I would like to welcome you to this briefing on our latest *Economic and Fiscal Outlook*.

I am going to take you through some of the highlights and then we will be very happy to answer your questions. The slides and my speaking notes will be available on our website after we finish.

[SLIDE] Let me start with the usual background.

The EFO contains our latest five-year forecasts for the economy and the public finances and an assessment of the Government's progress against its fiscal and welfare spending targets.

The views expressed are the responsibility of the Budget Responsibility Committee. But we have relied on the hard work of the OBR's staff and on the help of numerous officials in other departments and agencies.

As usual, the forecast went through a number of iterations to reflect new judgements, new data and proposed policy measures. We provided the Chancellor with the first draft of our fiscal forecasts on February 11th and a final pre-scorecard forecast on March 4th. We then met with him to discuss the forecast and the measures on the 7th. We have come under no pressure to change any of our conclusions.

[SLIDE] Let me start with a brief overview.

In the short time since our November forecast, economic developments have disappointed relative to expectations and the outlook for the economy and the public finances looks materially weaker.

The most significant change we have made in this forecast is to revise down potential productivity growth. (Combined with revisions to past outturn data and a weaker outlook for whole economy inflation, this means that the cash size of the economy is about 3 per cent smaller at the end of the forecast than we predicted in November.) Weaker potential output growth in turn means weaker growth in spending and incomes and a significant loss of tax revenue. Together with higher expected spending on disability benefits, this means that our underlying forecast for public sector net borrowing is around £11 billion a year worse on average over the next five years than in November, despite big savings on debt interest spending from lower market interest rates.

If the Chancellor had done nothing in his Budget today, the £10 billion surplus he was aiming for in 2019-20 in November would have become a £3 billion deficit. But the measures he has announced today almost exactly reverse this deterioration and get him back to a £10 billion surplus. He has achieved the bulk of this in five main ways:

- First, he has cut his planned limit on day-to-day departmental spending in 2019-20 by around £2 billion. This, together with almost £2 billion of new spending commitments announced in the Budget, will be funded by a £650 million cut in overseas aid and £3.5 billion of as-yet unidentified departmental cuts to be delivered by an 'efficiency review' that will report in 2018;
- Second, he has decided not to compensate public sector employers for an increase in the pension contributions they have to make. This reduces borrowing by £2 billion;
- Third, he has moved £1.6 billion of planned departmental capital spending out of 2019-20 and into the previous two years, which the Treasury describes as "accelerating investment plans";
- Fourth, he has delayed by two years the decision he announced in July to make large companies pay corporation tax three months earlier than they do now. The Treasury says it is doing this "to give businesses more time to prepare". It also shifts £6 billion of tax receipts into 2019-20 and £3.6 billion into 2020-21, out of the previous two years. But it has no impact on receipts thereafter;

- Fifth, as Iain Duncan Smith announced last week, the Government has tightened the eligibility criteria for disability benefits, after earlier reforms delivered only around 25 per cent of the savings it was looking for. This will reduce borrowing by £1.3 billion.

By restoring budget surpluses in 2019-20 and 2020-21, the Chancellor's measures keep him on course to achieve his 'fiscal mandate'. But he is now on course to breach his supplementary target to have debt falling as a share of GDP this year and beyond. We have actually revised our cash forecasts for net debt lower this year, but much weaker recent growth in nominal GDP than we had expected means that the debt-to-GDP ratio now rises this year before falling.

As in November, forecast welfare spending is higher than the cap the Chancellor set in July. Disability benefit spending is higher throughout the forecast, despite the announcement of tighter eligibility criteria.

Finally, for those of you who feel we haven't heard quite enough about Brexit recently, I am afraid we have to disappoint you. Parliament has told us to prepare our forecasts only on the basis of current Government policy, and current Government policy is to stay in. But we do note in the report that while other forecasters differ on the potential long-term impact of leaving the EU, there is a greater consensus that in the near term a vote to leave would usher in a potentially damaging period of uncertainty while our new relationship with the EU is negotiated.

So now let me talk about our economy forecast in a little more detail.

[SLIDE] This chart shows the rates of growth for real GDP – the volume of goods and services produced in the economy – and nominal GDP – the cash value of those goods and services – that we forecast at the time of the Autumn Statement in November.

[SLIDE] This chart shows that we are more pessimistic today.

We have revised real GDP growth down from an average of 2.4 per cent a year to 2.1 per cent. And we have revised nominal GDP growth down from an average of 4.3 per cent a year to 3.9 per cent.

So why the gloom?

[SLIDE] The main reason is that the data published by the ONS since November have been materially weaker than we and others expected.

The latest figures show economic growth losing momentum through 2015, despite the boost from lower oil prices. They also show weaker whole economy inflation. As a result nominal GDP rose by just 0.4 per cent in the second half of the year, compared to our forecast of 1.8 per cent. The main contributing factor was a widening trade deficit, although private investment was also weaker than expected.

With the economy growing only modestly – but employment and hours continuing to grow strongly – productivity fell sharply in the fourth quarter. [SLIDE] Rather than rising by 0.2 per cent as we had forecast, [SLIDE] output per hour fell by 1.2 per cent and thereby wiped out almost all the apparently promising improvement earlier in the year.

[SLIDE] Annual growth in average earnings – which should track productivity growth over the long-term – has also weakened, dropping from 3 per cent in September to less than 2 per cent in the final quarter.

Financial markets have also weakened. At the time we took the averages for this forecast, equity prices were almost 8 per cent lower than in November, sterling was more than 5 per cent lower, oil prices were 30 per cent lower and bond yields were on average 33 basis points lower across the US, Germany and Japan. World trade growth has also been weaker than expected, pointing to less robust demand for UK exports.

[SLIDE] Consistent with weaker medium-term growth, interest rate swap prices suggested that the Bank of England was not expected to raise interest rates until 2019 and that a cut in rates is more likely in the near term. [SLIDE] The Bank and the OECD have also revised down their own growth forecasts significantly since those they produced in November.

[SLIDE] Confronted by this background, the most significant change we have made to our forecast has been to revise down our estimates of trend or potential productivity growth – the amount of output the economy could produce sustainably per hour worked.

The pick-up in actual productivity growth we saw in mid-2015 looked consistent with our long-held assumption that trend productivity growth would pick up relatively soon to its pre-crisis average rate of 2.2 per cent a year as the financial system continued to mend. But that pick-up now appears to have been another false dawn.

[SLIDE] With the period of much weaker productivity growth since the financial crisis lengthening further, we have placed slightly more weight on that as a guide to the medium term outlook. [SLIDE] And we therefore assume that trend productivity will pick up to 2.0 per cent a year instead. This remains one of the most important and least certain judgements that any medium term forecaster has to make.

[SLIDE] A weaker outlook for trend productivity means a weaker outlook for potential output. This chart shows the estimated level of potential output – in other words the level that could be sustained in the long-term while keeping inflation stable – compared to actual output in 2007. As you can see, by November we had already revised this much lower than the Treasury's estimate in the pre-crisis Budget of 2008.

[SLIDE] In this forecast we revise it slightly lower still. [SLIDE] But it remains broadly in line with the estimates of the OECD and the IMF and well within the range of other outside forecasts. It is this loss of potential output relative to pre-crisis expectations that explains why we have had a large structural budget deficit and the need for significant fiscal consolidation.

[SLIDE] The UK is not alone in having to face up to a weakening in the outlook for trend productivity and potential output. This chart compares our current forecast for cumulative growth in trend productivity between 2010 and 2020 with an extrapolation of the forecast we made back in 2010. As you can see we have revised it down from 22 to 14½ per cent, a drop of 7½ percentage points. This is big, [SLIDE] but not quite as big as the 9 point downward revision from 24½ to 15½ per cent made by the Congressional Budget Office for the United States.

[SLIDE] Repeat the exercise for potential output and you can see that the CBO has had to make a much larger downward revision for the US than we have for the UK – 11 points versus 4 points. This is largely because we estimate that the trend rate of participation in the labour market will

be flat over the decade in the UK, despite an ageing population, while in the US it looks likely to fall significantly.

So what impact does our downward revision to potential output have on the economic variables that matter for our public finances forecast?

[SLIDE] As this table shows, weaker potential output growth – together with a small cut in our estimate of spare capacity in the economy – implies weaker real GDP growth, as we assume that the Bank of England keeps demand in the economy broadly in line with potential supply to keep inflation stable. Add in a weaker outlook for whole economy inflation and that implies weaker nominal GDP growth. We can then split that out into different categories of income and spending. Weaker growth in wages and salaries, profits and consumer spending all imply weaker growth in tax revenues. Our forecast for business investment is also weaker, but this is actually positive for tax revenues as it implies less use of capital allowances. But that is only a very small offset.

So how does this feed in to our forecast for the public finances?

[SLIDE] This chart will show how our forecasts for public sector net borrowing have changed since November, before taking today's Budget policy measures into account. There are five main factors pushing borrowing higher:

- [SLIDE] First, the downward revision to nominal GDP – and to the components of income and spending that make it up. This reduces tax revenues by about £7 billion next year rising to almost £14 billion in 2020-21. The effect of weaker average earnings growth on income tax and national insurance contributions accounts for about £8.5 billion of that.
- [SLIDE] Second, lower equity prices reduce receipts by £0.8 billion next year, rising to £2.3 billion. This largely shows in up in capital gains tax, inheritance tax, stamp duty and corporation tax;
- [SLIDE] Third, our forecasts for spending covered by the welfare cap are £0.6 billion higher next year, rising to £2.5 billion. Disability benefits are the biggest contributor, followed by carers' allowance and incapacity benefits;

- [SLIDE] Fourth, we have revised spending by local authorities, housing associations and other public corporations higher by around £1 billion a year. This is largely as a consequence of the latest outturn data, and;
- [SLIDE] Fifth, lower interest rates reduce receipts by £0.3 billion next year, rising to £1.1 billion, mostly because we get a lower return on our foreign exchange reserves.

[SLIDE] Other smaller forecasting changes increase the deficit in most years, but reduce it slightly in 2017-18.

[SLIDE] These upward pressures on borrowing are partially offset by another big cut in debt interest spending, which rises from almost £4 billion next year to more than £5 billion in 2020-21. This reflects lower market expectations of Bank rate and gilt yields, plus a downward revision to our forecast of RPI inflation. This is the third time in four forecasts that lower market interest rates have significantly pushed down prospective debt interest spending. Rate expectations have risen a little since we closed our forecast and there is clearly a risk that at some point this could go into reverse. But we have been saying that for ages.

The net effect of all this is to increase our underlying forecast for the budget deficit by almost £7 billion next year, rising to almost £17 billion in 2020-21. That is an increase of £56 billion in aggregate over the five years, which sounds enormous but is only half a per cent of GDP.

[SLIDE] Compare this with the even smaller *downward* revision to our forecasts of a quarter of a per cent of GDP – £27 billion cumulatively – that we made in November and you can see that the sofa has swallowed roughly two pounds this time for every one that it yielded last time.

In both this forecast and the November forecast, the Exchequer has benefited from lower debt interest costs, but suffered from lower equity prices, higher welfare costs and the impact of lower interest rates on receipts. In November the outlook for other receipts improved modestly – thanks in part to modelling improvements that remain in place. But in this forecast the outlook for receipts has deteriorated significantly, thanks almost entirely to the weaker outlook for the economy.

[SLIDE] We can put these underlying forecast revisions into context by comparing them to those that we have made in previous forecasts. As you can see, the revision of 0.5 per cent of GDP this time is in line with the average absolute size of the 13 revisions we have made since 2010, while the much-remarked revision in November was much smaller – only the ninth largest. As you can see, our revisions have gone in both directions, with nine pushing the deficit higher and four pulling it lower.

Hence my warning at the Scottish Parliament in January that: “What the sofa gives, the sofa can easily take away. And the sums lost or gained can often be much larger than they were in November”.

So how does this change in our pre-measures forecast affect the overall profile of public sector net borrowing, first in isolation and then combined with the impact of the policy measures in the Budget?

[SLIDE] This chart shows the forecasts that we made for public sector net borrowing back in November. We predicted that the deficit would fall from £73.5 billion this year to £4.6 billion in 2018-19. The budget balance would then move to a £10.1 billion surplus in 2019-20, rising to £14.7 billion in 2020-21. [SLIDE] This line shows the impact of the latest pre-measures forecast, in the event that the Chancellor did nothing in the Budget. On this basis the deficit would be slightly smaller this year than in November at £72.2 billion, but would then shrink more slowly. The budget balance would still be in deficit by £3.2 billion in 2019-20 and by £2.0 billion in 2020-21, breaching the fiscal mandate.

So what is the impact of the Budget measures announced today? [SLIDE]

They amount to a net giveaway averaging £6 billion a year in 2017-18 and 2018-19, followed by a net takeaway averaging just over £13 billion a year in 2019-20 and 2020-21. So the deficit would shrink even more slowly over the middle years of the Parliament than in our pre-measures forecast, but more quickly thereafter. This would put the Chancellor back on course for a £10.4 billion surplus in 2019-20, rising more modestly than in November to £11 billion in 2020-21.

[SLIDE] So let’s look in more detail at the package that brings this about. This chart will show the impact of different elements on the budget

balance, with those above the line increasing borrowing or reducing the surplus and those below the line lowering borrowing or increasing the surplus.

[SLIDE] The first thing to note is that the Chancellor has increased his plans for departmental current and capital spending in 2017-18 and 2018-19 and then reduced them in 2019-20 and – especially – in 2020-21.

As you can see here [SLIDE] the real cut in day-to-day departmental spending is shallower over the next three years than in November. The Government has re-opened the Spending Review it concluded just four months ago and has announced new spending in areas such as education, flood defence, City deals and grants to local authorities to compensate them for making permanent the doubling of small business rates relief, which it had previously been extending year by year.

These additional spending commitments still amount to around £2 billion in 2019-20. But in that year – the first to which the fiscal mandate applies – the Government says it will make £3.5 billion of as-yet undefined savings from an ‘efficiency review’ that will report in 2018.

Together with a £650 million cut in overseas aid (reflecting the fact that the commitment to spend 0.7 per cent of gross national income is cheaper when the economy is smaller), this would be sufficient to push real day-to-day spending below the level set out in the Autumn Statement. The Government then plans to keep spending at that same real level in 2020-21 rather than increasing it as it said in November.

[SLIDE] The story with departmental capital spending is slightly different. There are some new commitments, for example investment to reduce congestion on the M62. But the Government has also said that it will bring forward around £1.6 billion of capital spending already planned for 2019-20 – such as road maintenance and parts of the affordable housing and starter homes programme – into 2017-18 and 2018-19. Again this contributes to the swing from giveaway to takeaway over the forecast.

[SLIDE] The next element of the package is cuts to welfare, mostly disability benefits, which build gradually to £1.4 billion in 2019-20 and 2020-21. This largely reflects the decision last week to reduce the points

awarded for using some aids and appliances when applying for the personal independence payment or PIP. We estimate that this will reduce the number of people receiving daily living payments by 290,000 in 2020-21, with an additional 80,000 people moving from enhanced to standard awards. This also means that fewer people will be entitled to carer's allowance and employment and support allowance.

[SLIDE] Other spending cuts also mount steadily through the forecast, reaching £3.0 billion by 2020-21. These include the reduction in net public sector pension spending that results from using a lower discount rate when contribution rates are next set.

[SLIDE] Turning to tax, the biggest single measure is the decision to delay by two years the July Budget measure that requires large companies to pay their corporation tax bills three months earlier. The Treasury says this is "to give businesses more time to prepare". The original measure produced a one-off boost to receipts in 2017-18 and 2018-19 as companies in effect pay an extra quarterly instalment of corporation tax in one of those two years. This now shifts £10 billion to 2019-20 and 2020-21, the years to which the fiscal mandate applies. Of course, if corporation tax receipts were recorded in the official public finances data on an accrued basis – when the profits being taxed were generated – rather than on a cash basis – when the tax is paid – moving receipts between years like this would not be possible.

[SLIDE] The other tax measures are smaller in aggregate, but with large giveaways and takeaways offsetting each other. Excluding the large companies measure, there is a net tax cut of £2.8 billion in 2020-21. This includes tax cuts worth £10.7 billion, including income tax, the Lifetime ISA, corporation tax, capital gains tax and another freeze in fuel duty. These are partly offset by £7.9 billion of tax increases, including the soft drinks industry levy (which we assume will be passed on in full to the industry's customers), higher insurance premium tax, various increases in business tax and the usual anti-avoidance and evasion measures.

[SLIDE] Overall, the pattern is clear. A tax and spend giveaway through to 2018-19, followed by the promise of a takeaway in 2019-20 and 2020-21 – the years for which the Government has a surplus target.

You might think that this pattern looks familiar. And you would be right.

[SLIDE] Look how the three fiscal events to date under the current Government stack up in aggregate: first the July Budget, [SLIDE] then the Autumn Statement and [SLIDE] now this Budget. St Augustine would be proud: near-term giveaways followed by long-term takeaways.

[SLIDE] And this in turn has shifted the profile of the fiscal consolidation, if you measure a fiscal tightening or loosening as the change in the structural budget balance from one year to the next. The Coalition bequeathed a profile that had a very large tightening in 2016-17, the year after the election. This reflected the abolition of the NICs contracting out rebate in that year, plus the decision to squeeze public services in that year when ONS methodological changes pushed up annually managed expenditure, but the Coalition chose to squeeze departments rather than raise total spending. [SLIDE] The July Budget and [SLIDE] the Autumn Statement smoothed out this lump in the fiscal carpet only for it [SLIDE] now to reappear with a vengeance in 2019-20, with a prospective fiscal tightening of 1.5 per cent of GDP, which would be the largest in any year since 2010-11.

[SLIDE] Pulling back from the medium term outlook for a moment, let me say a little about the current fiscal year: 2015-16. I mentioned a moment ago that we have revised the deficit down this year, from £73.5 to £72.2 billion. This implies a drop of £19.7 billion since last year, whereas the first 10 months of the year have seen a decline of only £10.6 billion. Not surprisingly, most outside analysts have pencilled in a higher number.

The outlook for the budget deficit remains uncertain, even at this late stage of the fiscal year. But we do believe that the last two months will show a faster decline, with some of it showing up in revisions to earlier months' data and not all of it necessarily appearing by the time the ONS publishes its first estimate for the full fiscal year next month.

For example:

- We expect stronger growth in income tax and National Insurance Contributions, based on administrative data for February. There are some offsetting policy effects here too. Take-up of the Government's marriage tax allowance has been far lower than

expected, because of IT problems that have thwarted many people's attempts to claim it, plus lack of awareness and perhaps a reluctance to attract the attention of HMRC among other potential recipients. But take up of the Government's voluntary NICs scheme has also been much lower than expected, which goes in the opposite direction and reduces revenue;

- We expect stronger year-on-year growth in stamp duty land tax receipts, reflecting the timing of the 2014 reform;
- We expect VAT to be stronger in the next two months, reflecting recent administrative data;
- We expect lower borrowing by housing associations, reflecting a lower-than-expected estimate of their borrowing last year, and;
- We expect lower spending on EU contributions, largely because the Commission did not ask for as much as it could have done in the payment we make this month. This is a timing effect that will mean that more of calendar year 2016's contributions are paid in the 2016-17 fiscal year.

So how have the Budget measures fed back into our forecast for the economy that I showed you a few moments ago? [SLIDE]

- The move from giveaway to takeaway in the shape of the overall package nudges GDP growth slightly higher in 2017-18 and then slightly lower in the subsequent two years;
- The business tax measures announced in the Budget would not have a significant impact on investment in aggregate, although one (more significant) measure was dropped late in the process after we had closed the economy forecast. So the level of business investment is about half a per cent higher at the end of the forecast than the final policy package would suggest;
- The decision to levy National Insurance contributions on some termination payments nudges wages and salaries down very slightly by the end of the forecast;

- The ability to use the Lifetime ISA to fund first-time home purchases pushes house prices a little higher, and finally;
- The soft drinks industry levy pushes inflation up by about a quarter of a percentage point in 2018-19, as we assume that firms pass it on to their customers in higher prices. This measure raises about £500 million a year in the last three years of the scorecard, but this blip in inflation has a one-off cost of £1 billion to the Government by pushing up accrued interest on index linked gilts. So there is a bit of a transfer from drinkers to linkers.

[SLIDE] So now let me sum up what all this means for the Government's fiscal and welfare spending targets.

As we have mentioned in passing already, the Government now has two fiscal targets:

- The 'fiscal mandate' requires it to run a surplus on public sector net borrowing by the end of 2019-20 and in each subsequent year, while;
- The 'supplementary target' requires public sector net debt to fall as a percentage of GDP in each year to 2019-20 (after which it would continue to do so if the mandate was met).

These targets apply unless we judge the economy to be suffering a significant 'negative shock' on a definition set down by the Government.

[SLIDE] As discussed, our central forecast shows the fiscal mandate being met with about £10 billion to spare in both 2019-20 and 2020-21. This chart shows that on the basis of past forecasting errors, that is a relatively small margin for error. If this forecast is as accurate as past ones, the Government has a roughly 55 per cent chance of meeting the mandate.

[SLIDE] In the report, we also show how sensitive this judgement is to different assumptions regarding net inward migration. Our central forecast is based on the ONS's principal population projection, which assumes that net inward migration falls to around 185,000 in 2021. That

is close to the average of the past 20 years, much lower than over the past five years, but higher than the Government would like.

Our scenarios show the impact of the ONS's high and low migration population projections, which have net inward migration falling to 265,000 and 105,000 respectively by 2021. Higher inward migration is generally positive for the public finances over this horizon, because inward migrants are more likely to be of working age than the native population. But the impact is smaller than you might expect, because rises in employment are less tax rich than increases in average earnings – as the bigger revisions to our pre-measures forecast have shown.

We estimate that the high migration variant would increase the budget surplus by about £4½ billion by 2019-20, while the low migration variant would reduce it by the same amount. This is not to suggest that we recommend any particular level of migration or that the Government could not offset different outcomes with tax and benefit changes.

[SLIDE] Turning to the debt target, this chart shows that in November we expected public sector net debt to peak at 83.1 per cent of GDP in 2014-15 and to fall each year thereafter. In this forecast we have revised the cash level of net debt down over the next three years, in part because a weaker pound has pushed up the sterling value of our foreign exchange reserves. (This is an artefact of the way in which net debt is defined by the ONS and Eurostat. In reality the sterling value of the reserves is hedged against big currency movements). But in the later years of the forecast this effect is more than offset by higher borrowing.

[SLIDE] The cash profile of net debt is also affected by the path of asset sales. As you can see here, by moving from the November plans [SLIDE] to those in place at this Budget, the profile of asset sales receipts from next year onwards is now more front loaded – with an additional £20 billion of sales due next year, up from £11 billion in November. This is largely thanks to the announcement that UKAR will begin a major sale of Bradford & Bingley mortgages.

If changes in the cash level of net debt were all we had to worry about, the picture would look like this [SLIDE] and the supplementary target would still be met. But we also need to revisit the bottom half of the debt-to-GDP ratio, because we have revised down nominal GDP growth

significantly, especially in the near term. When you do this, [SLIDE] debt actually rises as a share of GDP between 2014-15 and 2015-16 – before falling thereafter – so that the supplementary target is breached.

[SLIDE] The Government also remains in breach of its welfare cap, which sets a ceiling on social security and tax credit spending (other than on state pensions and those benefits linked most closely to the economic cycle). [SLIDE] The Government set the cap in line with our forecast for this spending in July – locking in the effect of all the cuts announced in the Summer Budget. It also set a 2 per cent margin that can be used to accommodate forecast changes but not policy giveaways.

[SLIDE] By the time of our November forecast, spending within the cap was higher in each year of the forecast, largely reflecting slow progress on disability benefit reform and the Government's decision to reverse the main tax credit cuts that it announced in July.

[SLIDE] In this forecast, we have revised cap spending higher again, primarily because of new evidence on the transition from disability living allowance to the new personal independence payment. Our November forecasts were largely based on DWP's analysis of 900 existing DLA cases. But we now have evidence from 7,000 actual reassessment cases. This suggests that more people are successfully claiming PIP than the earlier sample suggested and that more of the successful claims are being awarded the enhanced daily living and mobility payments.

[SLIDE] As you can see from this chart, that has prompted another big upward revision to our disability benefits forecast that is only partially offset by the tightening of eligibility criteria announced last week. The Government wanted the transition from DLA to PIP to cut the cost of disability benefits by 20 per cent. Current evidence suggests that the saving would be more like 5 per cent in the absence of the changes announced last week.

The history of optimism bias in estimates of the impact of welfare reform is a real cause for concern, especially with the much larger transition to universal credit only now getting under way.

[SLIDE] The net effect of the underlying forecast changes and the Budget policy measures is to leave welfare cap spending above both the

headline cap and the forecast margin in each year of the forecast, so our judgement remains that the welfare cap is being breached.

[SLIDE] Finally, let me conclude. This has been an eventful Budget by any standards. We have made significant changes to our underlying fiscal forecast, although no larger than the average size of the revisions we have made in our 13 forecasts to date. Meanwhile, the Chancellor has announced a substantial package of 77 scorecard measures, the largest number any of us can remember.

The big picture is that a weaker outlook for the economy and further disappointment on the progress of disability benefit reform has increased the underlying budget deficit by about half a per cent of GDP on average, despite big savings on debt interest spending.

In response the Chancellor has announced a string of high profile tax cuts and new spending commitments. By the end of the forecast, most but not all of the tax cuts should be covered by other tax increases – although many of these are anti-avoidance and anti-evasion measures for which the revenue gains are relatively uncertain. The new spending commitments are set out in considerable detail – from cathedral repairs to cultural investment and from City Deals to smart motorways. The cuts in spending to finance them are less well specified, including a £3.5 billion efficiency review that will not report until 2018.

Even if all this was delivered, the Government would be looking to end the Parliament with a budget surplus noticeably smaller than the £10 billion he aimed for in July and November. But he remains on track thanks to further measures that shuffle spending out of the fiscal mandate year and shuffle receipts into it. On that basis, we judge that the Chancellor is on course to achieve the letter of the mandate with the same room to spare that he had in November.