

The work of the OBR following the EU referendum

In light of last week's referendum vote to leave the European Union – and given the remit set out for us by Parliament in primary and secondary legislation – we thought it would be helpful to set out the OBR's role in assessing the potential implications for the economy and public finances.

Pre-referendum

The legislation underpinning the OBR requires us to produce our forecasts and analysis on the basis of the current policy of the current government and precludes us from looking at alternative policy options. For this reason, when we published our last *Economic and fiscal outlook* in March we did not produce an assessment of the implications of leaving the EU, but simply summarised the relatively limited body of external analysis available at that time.

Our next medium-term forecast

The OBR publishes medium-term forecasts when requested to do so by the Chancellor, to accompany Budgets and Autumn Statements. The Chancellor said on Monday that we should produce our next assessment in the autumn, which would allow any decisions on the initial fiscal response to be taken when the new Prime Minister is in place. The precise date will be a matter for the Government, which under normal circumstances has to give us 10 weeks' notice.

In producing that forecast, we will of course be able to draw on the much larger volume of official and external analysis now available, and any further studies published in the meantime. Most attempts to date to assess the implications for the public finances have necessarily taken a top-down approach, based on views about the impact of near-term uncertainty, movements in the exchange rate and long-term changes in the trade regime on real GDP growth, plus the direct fiscal impact of eliminating or reducing our net financial contribution to the EU. Our forecast will also be affected by judgements on other more bottom-up issues, including the impact on the composition of nominal GDP (where different categories of income and spending are taxed at different rates), movements in asset prices, prospects for the labour market, the potential behaviour of different measures of inflation and the outlook for fiscally significant sectors such as financial services and oil and gas.

As noted above, we are required to base our forecasts on whatever is current government policy at the time. So in addition to incorporating any new tax and spending measures, we will need to take on board any information on the trade arrangements the Government wishes to pursue. This

would affect prospective trade volumes, migration flows and the size of any remaining financial contribution to the EU, all of which would have consequences for the public finances.

The *Fiscal sustainability report*

The OBR is required to publish a regular *Fiscal sustainability report*, which takes a forward look at the long-term prospects for the public finances and a backward look at the latest measures of the public sector's balance sheet. Like our medium-term forecasts, the forward looking projections have to be based on the current policy of the current government.

To avoid overlapping with the preparation of our medium-term forecasts, we commission the analysis underpinning these reports soon after the Budget so that we can publish shortly before the summer recess while Parliament is sitting. This year's *FSR* was due for publication on July 12.

In producing our long-term projections, we assume that the public finances evolve in line with our most recent medium-term forecast over the first five years and then project these forward over the subsequent 45 years. This allows us to assess the impact of prospective demographic changes and the evolving consequences of policies such as the provision of student loans.

Changes in the projections from year to year therefore reflect changes in the end-point of the medium term forecast (the position from which any long-term fiscal pressures have to be addressed) and changes in the extent to which the public finances are expected to improve or deteriorate thereafter (e.g. because of changes in the expected evolution of the population).

Given the timing and result of the referendum, and the current uncertainty around our future relationship with the EU, producing projections based on our March forecast would not necessarily be very informative. To produce meaningful long-term projections we would need to make a new medium-term forecast (which we will not be doing until the autumn) and new long-term assumptions in areas such as productivity growth and migration flows (which would be affected by the trade arrangements the government decides to pursue).

Under these circumstances, we have decided to cancel July's *FSR*. We hope to publish some of the material that would not be affected by the referendum result, for example the backward looking assessment of recent balance sheet developments, separately in due course. Depending on the timetable of future fiscal events and policy decisions, we will aim to produce illustrative long-term projections later this year or early next. This would fulfil our obligations under the Budget Responsibility and National Audit Act and Charter for Budget Responsibility. We would like to take this opportunity to express our gratitude to officials across a number of departments who have put valuable time and effort into the preparation of our long term projections.

Notes

1. The OBR is the UK's independent fiscal watchdog. We produce forecasts for the economy and the public finances, assess progress against the Government's fiscal targets, and report on long-term fiscal sustainability.
2. We will continue to publish our monthly commentary on the public finances on the same day as the ONS/HM Treasury statistical bulletin.
3. Questions should be sent to OBRpress@obr.gsi.gov.uk or contact Mark Dembowicz on 0207 271 2442.