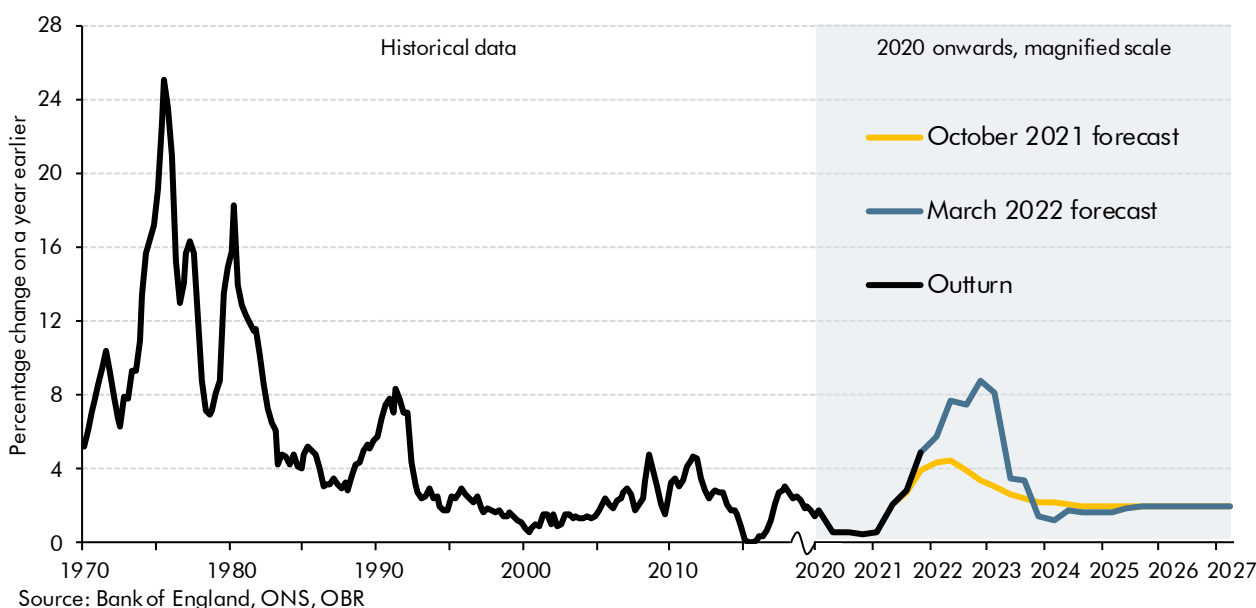


# 1 Executive summary

## Overview

- 1.1 Two years since the start of the pandemic, this *Economic and fiscal outlook (EFO)* is presented against the backdrop of another unfolding global shock. The Russian invasion of Ukraine is foremost a human tragedy and a reminder of the terrible costs of wars and the immense and immeasurable losses for those caught up in them. The conflict also has major repercussions for the global economy, whose recovery from the worst of the pandemic was already being buffeted by Omicron, supply bottlenecks, and rising inflation. A fortnight into the invasion, gas and oil prices peaked over 200 and 50 per cent above their end-2021 levels respectively. Prices have since fallen back but remain well above historical averages.
- 1.2 As a net energy importer with a high degree of dependence on gas and oil to meet its energy needs, higher global energy prices will weigh heavily on a UK economy that has only just recovered its pre-pandemic level. Petrol prices are already up a fifth since our October forecast and household energy bills are set to jump by 54 per cent in April. If wholesale energy prices remain as high as markets expect, energy bills are set to rise around another 40 per cent in October, pushing inflation to a 40-year high of 8.7 per cent in the fourth quarter of 2022 (Chart 1.1). Higher inflation will erode real incomes and consumption, cutting GDP growth this year from 6.0 per cent in our October forecast to 3.8 per cent. With inflation outpacing growth in nominal earnings and net taxes due to rise in April, real living standards are set to fall by 2.2 per cent in 2022-23 – their largest financial year fall on record – and not recover their pre-pandemic level until 2024-25.

Chart 1.1: CPI inflation



- 1.3 Despite these economic headwinds, the public finances have continued to recover from the pandemic more quickly than we expected. Tax receipts this year have been revised up by 4 per cent thanks to strong growth in tax paid by higher earners and by companies. And despite higher inflation pushing up debt interest costs, borrowing is set to more than halve from its post-World War II high of £322 billion (15.0 per cent of GDP) in 2020-21 to £128 billion (5.4 per cent of GDP) in 2021-22, £55 billion less than we forecast in October.
- 1.4 Borrowing in 2022-23 is then £16 billion *higher* than we forecast in October, at £99 billion (3.9 per cent of GDP). That reflects record-high debt interest costs of £83.0 billion, double our October forecast, and near-term rebates and tax cuts that inject £17.6 billion into the economy. The latter offset half the blow to household finances from higher energy and fuel bills and a third of the overall fall in living standards that households would otherwise have faced. Over half the £9 billion in energy costs support is recouped over the subsequent five years, while the 5p fuel duty cut is to be more-than-fully reversed next year. The ‘pay later’ phase of these measures comes when energy bills are set to fall back.
- 1.5 Before taking account of the policies in this Spring Statement, positive news since October has led us to revise up receipts by £37 billion in 2024-25 – the Government’s fiscal target year. Higher inflation and interest rates mean nearly two-thirds of that is consumed by higher spending (revised up £23 billion in 2024-25), leaving a net £14 billion (0.5 per cent of GDP) pre-measures borrowing windfall. Student loans reforms that reduce the share of loan balances expected to go unpaid free up a further £5 billion, leaving almost £20 billion of fiscal room for manoeuvre in the target year at this Spring Statement. Cuts to personal taxes costing £10 billion consume just over half of that, with the remainder reducing borrowing. In the process the Chancellor has undone just over a quarter of the overall value of the personal tax rises he announced last year and around a sixth of the overall net tax rises he has announced since becoming Chancellor.
- 1.6 Public sector net debt excluding the Bank of England falls by 1.0 per cent of GDP in 2024-25, a margin of £27.8 billion against the Government’s fiscal mandate, £10.3 billion greater than in our October *EFO*. And the current budget is in surplus by £31.6 billion (1.2 per cent of GDP), up £6.5 billion from October. History suggests these margins would be consistent with a 58 and 66 per cent chance of meeting each fiscal target respectively, broadly in line with the headroom previous Chancellors have given themselves.
- 1.7 But few of these fiscal targets were actually met in the past and there are numerous risks to the outlook at present. Higher energy prices and inflation as a result of a longer war in Ukraine or tougher international sanctions would reduce the Chancellor’s headroom by over £4 billion in our illustrative scenario. There could be pressure to: provide further support for households in the event of another large rise in the energy price cap in October; address the 5 per cent fall in the real value of welfare benefits in 2022-23; or cancel next year’s fuel duty super-indexation that would raise petrol prices 6 per cent overnight and be the first duty increase in 12 years. In the medium term, a sustained increase in global energy prices could lower potential output for a net energy importer like the UK, damaging fiscal prospects. And while successful vaccines have reduced pandemic-related uncertainties, the recent rise in hospitalisations demonstrate that Covid remains a risk.

## Economic outlook

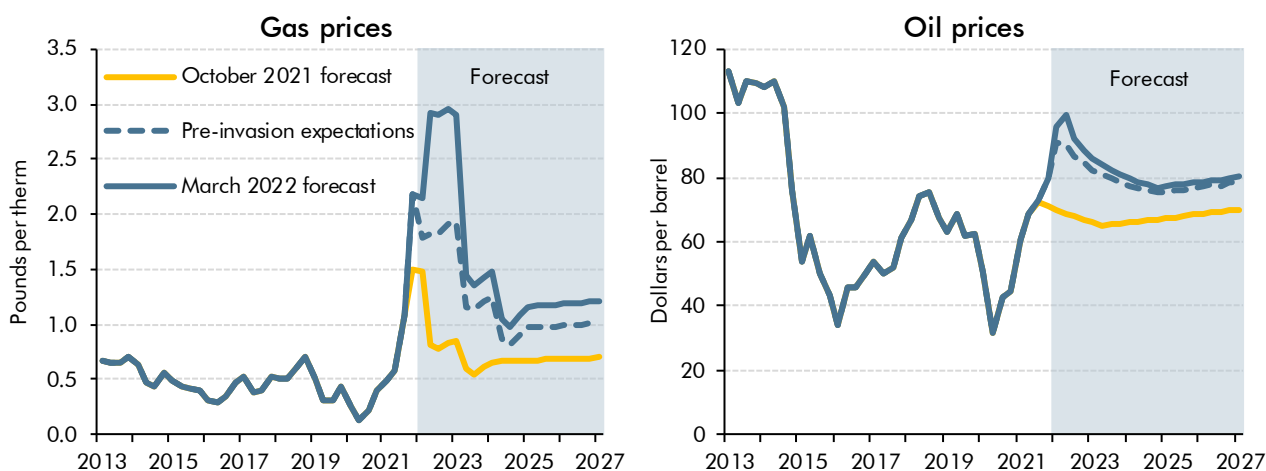
### Developments since October

- 1.8 The Russian invasion of Ukraine, and the international response, pushed already elevated gas and oil prices to their highest levels in more than a decade. Month-ahead gas prices jumped to around £5.40 a therm on 7 March and oil to a 14-year high of around \$130 a barrel on 8 March, following the announcement of US and UK curbs on Russian oil exports, before falling back. When we closed our forecast for commodity prices on 2 March, the monthly peaks in market expectations for future gas and oil prices averaged just over £3 a therm and \$103 per barrel, almost 100 and 45 per cent higher respectively than the peaks in our October forecast. Energy prices have remained volatile since, with gas and oil price expectations over the next six months respectively around 15 per cent below and 5 per cent above the levels assumed in our forecast when we finalised the *EFO* on 20 March.
- 1.9 This latest jump in global gas and oil prices hits a UK economy that has only just returned to pre-pandemic levels of activity and was already experiencing rising inflation from higher global goods and energy prices and a tightening labour market. Despite being buffeted by the Omicron variant, output regained its pre-pandemic level in January 2022, two years after the start of the pandemic and broadly in line with our October forecast. Buoyant labour demand has helped the unemployment rate to fall to 3.9 per cent in the three months to January, rather than rise above 5 per cent as we expected in October following the end of the furlough scheme. But total employment remains 450,000 below pre-pandemic levels due to a smaller population and weaker labour market participation, especially among older people. CPI inflation reached 5.5 per cent in January 2022, 1.2 percentage points above our October forecast. In response, the Bank of England has raised Bank Rate three times to a level of 0.75 per cent.

### Global outlook and energy prices

- 1.10 We have assumed that the Russian invasion reduces global GDP growth by 0.5 percentage points in 2022. This adds to downside news since October from Omicron and persistent supply bottlenecks, taking our forecast for global growth in 2022 down a full percentage point from 4.9 to 3.9 per cent. But these headwinds are assumed to be temporary, with gas and oil prices falling part of the way back next year and global GDP returning to our October forecast levels by the forecast horizon. But given the unfolding situation in Ukraine, there is unusually high uncertainty around this outlook in both directions.
- 1.11 The UK is a net energy importer, and despite having a relatively low energy intensity of output, we are highly reliant on gas and oil in our energy mix. Gas and oil together supplied 76 per cent of total UK energy consumption in 2019 compared to a European average of 57 per cent. And while we import little of it directly from Russia (6 per cent of our gas and 8 per cent of our oil), we pay global market prices for all of it and so, like all net importers of these commodities, face a deterioration in our terms of trade. Our forecast is based on the average gas and oil future prices over the first week of the Russian invasion between 24 February and 2 March, which imply prices fall back sharply from their current multi-year highs, but remain elevated (Chart 1.2).

Chart 1.2: Gas and oil prices

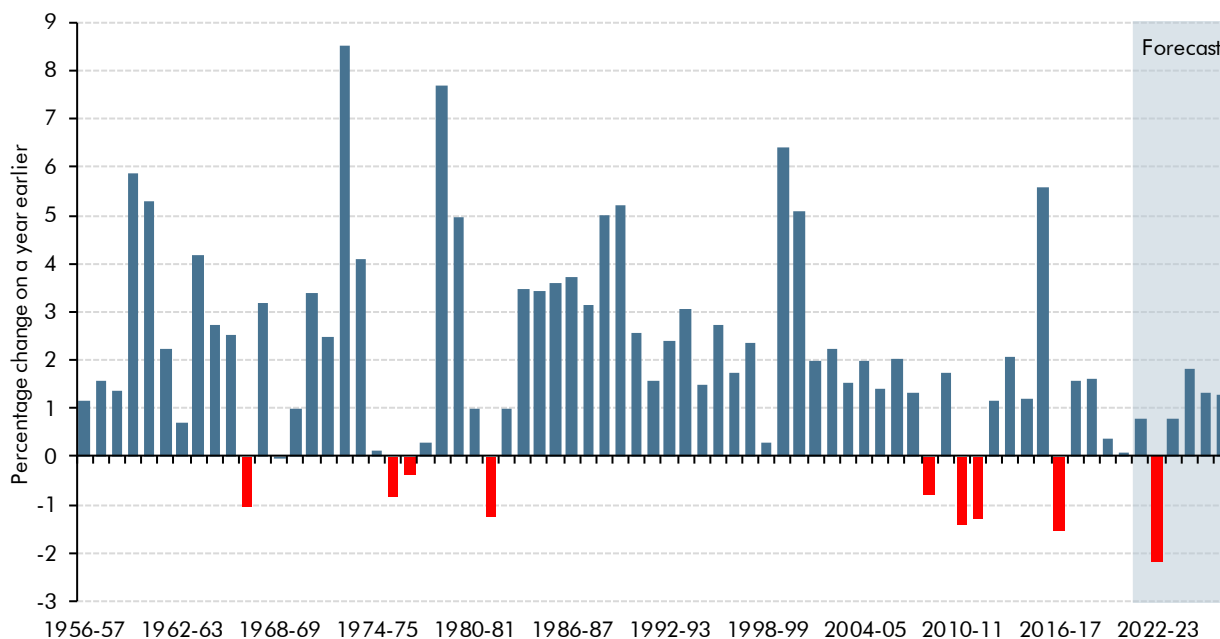


Note: We have based our March 2022 forecast on three years (rather than our usual two years) of the futures curve. We then hold gas and oil prices flat in real terms for the remainder of the forecast.  
Source: Datastream, OBR

## Short-term economic outlook

- 1.12 Higher global energy prices will feed through to higher domestic prices over the course of 2022, with CPI inflation now forecast to peak at close to 9 per cent in the fourth quarter of this year, 4.3 percentage points higher and two quarters later than the peak in our October forecast (Chart 1.1). This would be the highest level of consumer price inflation in around 40 years when the second oil shock pushed inflation into double digits in the late 1970s and early 1980s. Our forecast is conditioned on market expectations of further interest rate rises that take Bank Rate to a peak of 1.9 per cent by the third quarter of 2023, well above the path in our October forecast, which peaked at 0.75 per cent at the end of 2023.
- 1.13 Rising inflation outpaces nominal earnings growth which, combined with net tax increases starting in April, weigh heavily on living standards in the coming 12 months. Real household disposable incomes per person fall by 2.2 per cent in 2022-23, the largest fall in a single financial year since ONS records began in 1956-57. Government support for household bills announced in February boosts most households' incomes by £350 in 2022-23, offsetting around half the £700 rise in energy bills taking effect in April. This fraction is broadly maintained across 2022-23, with the temporary 5p cut in fuel duty and permanent increase in the National Insurance contributions (NICs) primary threshold announced in this Spring Statement partly offsetting the further £830 increase in the energy price cap that we expect in October. Taking account of both energy and non-energy pressures on household incomes, the policy measures announced since October offset a third of the overall fall in living standards that would otherwise have occurred in the coming 12 months.

Chart 1.3: Change in real household disposable income per person



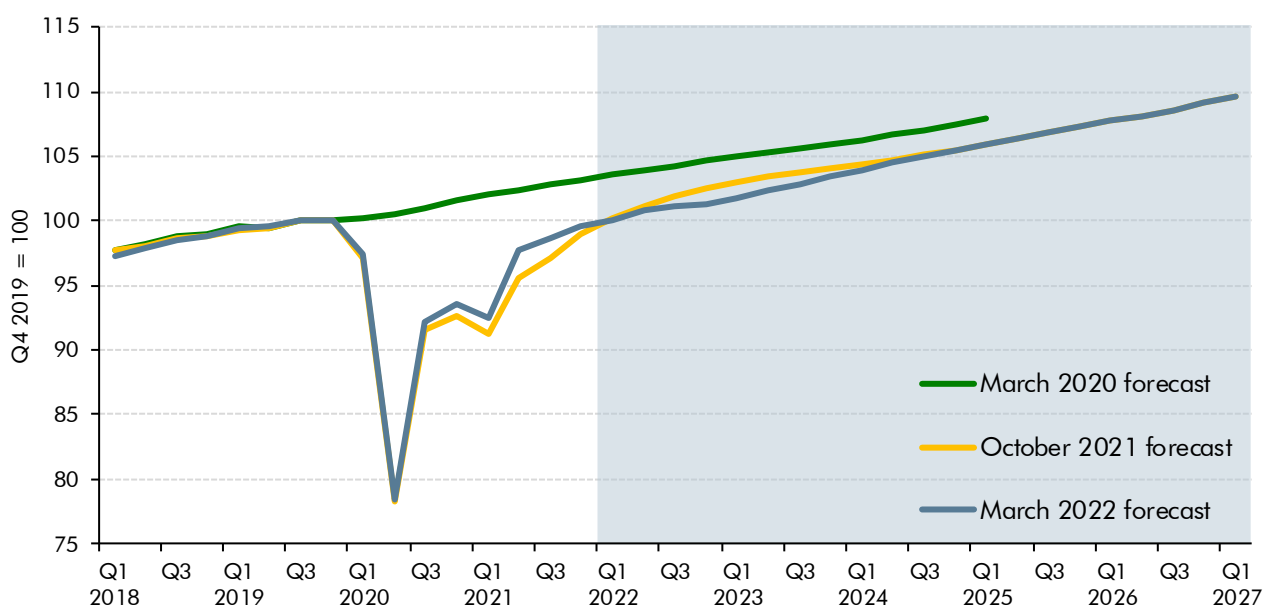
Source: ONS, OBR

1.14 This additional fiscal support boosts growth in 2022-23 by 0.3 percentage points, but the large fall in real disposable incomes weighs on household consumption and real GDP. We now expect real GDP growth of 3.8 per cent in 2022, down 2.2 percentage points from our October forecast. Consumption is given some support in the near term by greater drawdown of savings built up during the pandemic than we have previously assumed. And business investment is expected to grow by more than 10 per cent this year, boosted by the super-deduction on business investment, although we have halved our initial estimate of its peak impact. Net trade subtracts from growth again in 2022, but by less than we assumed in our October forecast, as weaker domestic demand lowers import growth.

## Medium-term economic prospects

1.15 Real GDP growth slows further to 1.8 per cent in 2023 as the rebound from pandemic-related restrictions fades, the cost of living squeeze continues, some fiscal support is withdrawn, and monetary policy tightens further. Growth then recovers in 2024 to 2.1 per cent as lower energy prices drag inflation below the 2 per cent target, supporting real incomes. Growth then settles around its potential rate of 1¾ per cent a year from 2025 onwards, while per-capita GDP growth averages just over 1½ per cent a year. The level of real GDP from 2025 is unchanged from our October forecast as we have maintained our assumption that the pandemic has led to economic scarring of 2 per cent of GDP (Chart 1.4). But we have revised up the contribution to scarring of lower labour supply (due to a smaller population and lower labour force participation) from 0.8 to 1.2 percentage points and made an offsetting downward revision to the hit to productivity (see Annex C).

Chart 1.4: Real GDP



Note: Outturn data are consistent with the first estimate of the fourth quarter of 2021.

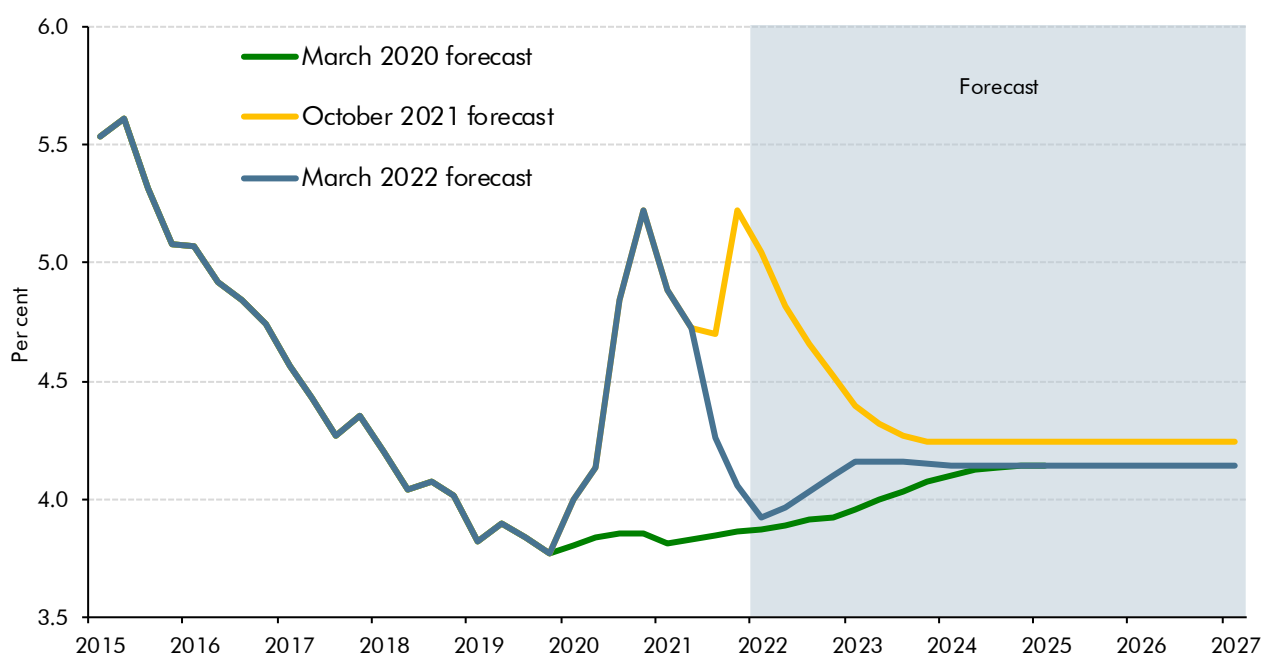
Source: ONS, OBR

- 1.16** The weak outlook for households' real incomes means that we expect lower consumption over the forecast period than in October – especially in the near term – although it is cushioned initially by a lower saving rate, which falls to a historically low rate of around 3 per cent. Business investment is expected to grow rapidly this year and to continue to outpace GDP growth. With little evidence to suggest that we revise our assumption about the negative effect of Brexit on UK trade flows, we continue to forecast little growth in export and import volumes and a fall in the trade intensity of the economy over the medium term.
- 1.17** CPI inflation slows to 4.0 per cent in 2023 as global energy and goods prices fall back but domestic inflationary pressures gather pace. Wholesale energy futures prices are consistent with a significant fall in the energy price cap in 2023 and the assumed easing of global supply bottlenecks should result in a normalisation in tradable goods prices. But the increase in nominal wage growth this year, driven by high inflation and a tight labour market, should flow through to the prices of non-tradable goods and services. Inflation then falls below target to 1.5 per cent in 2024 as energy prices fall further and the opening up of a small amount of excess supply lessens domestically generated inflation pressures. Inflation remains slightly below its 2 per cent target in 2025 before returning to 2 per cent in 2026 as falls in energy prices drop out of the annual calculation.
- 1.18** Nominal GDP was revised up materially in the 2021 Blue Book, so the level is around 2 per cent higher than our October forecast in the medium term. But cumulative growth across the forecast period – the metric that matters most for our fiscal forecasts as it closely drives tax receipts – has been revised only modestly. Nominal GDP growth averages 4.6 per cent a year between 2022 and 2026, down from 4.7 per cent a year in our October forecast.

## Labour market

1.19 Labour market developments since our last forecast have been mixed. Unemployment troughs in the first quarter of 2022 at 3.9 per cent, 1.1 percentage points lower (390,000 fewer people), than we expected in October. The combination of record-high vacancies, lower participation, and low redundancies indicates a tighter labour market than we expected in October, meaning unemployment rises only slightly over the forecast period (Chart 1.5). We expect it to settle at its sustainable rate of 4.1 per cent in the medium term, 0.1 percentage points lower than assumed in October. But positive news on unemployment has been offset by negative news on labour market participation. Employment is still down 450,000 on pre-pandemic levels. And we now expect there to be around 400,000 fewer people in the labour force at the forecast horizon than was assumed pre-pandemic. Of this, around 190,000 is due to a smaller population (largely the result of lower net inward migration), and 210,000 is accounted for by a higher inactivity rate among those of working age (largely the result of more early retirements and greater prevalence of long-term sickness).

Chart 1.5: Unemployment rate



Source: ONS, OBR

1.20 Nominal earnings rise by 5.3 per cent in 2022, 1.4 percentage points faster than forecast in October as a result of tight labour market conditions and high labour market churn in an environment of rising inflation. But wage growth is not expected to fully compensate for higher inflation, much of which is externally driven, meaning that real wages fall in both 2022 and 2023. Thereafter, earnings growth eases a little further, but inflation drops back more rapidly, resulting in a partial recovery in real wages in the final three years of the forecast. On a post-tax basis, real wages stagnate over much of the forecast period.

## Key risks to the economy forecast

1.21 In the first quarter of this century, the UK economy has been subjected to an extraordinary array of shocks. The financial crisis, Brexit and the pandemic are all expected to have long-term consequences for potential output, a key determinant of medium-term fiscal prospects. The uncertain course of the invasion of Ukraine and international sanctions brings with it the prospect that energy prices could rise further than markets (and therefore our forecasts) currently assume (as explored in a scenario in Chapter 4) driving inflation close to double digits and GDP 0.8 per cent lower in the near term. A more *sustained* increase in whole-economy input costs could do lasting damage to potential output in a net energy importing economy like the UK, compounding the long-term economic legacy of past shocks. With Covid cases once again on the rise in the UK and around the world, the emergence of a vaccine-escaping variant could lead to a further sharp contraction in GDP and an increase in long-run economic scarring (as explored in another Chapter 4 scenario).

Table 1.1: Overview of the economy forecast

	Percentage change on a year earlier, unless otherwise stated						
	Outturn		Forecast				
	2020	2021	2022	2023	2024	2025	2026
<b>Output at constant market prices</b>							
Gross domestic product (GDP)	-9.4	7.5	3.8	1.8	2.1	1.8	1.7
GDP per capita	-9.7	7.4	3.5	1.5	1.9	1.6	1.5
GDP levels (Q4 2019=100)	90.4	97.1	100.8	102.6	104.8	106.6	108.4
Nominal GDP	-4.6	7.7	6.7	5.0	4.0	3.7	3.7
Nominal GDP (£ billion)	2,153	2,318	2,474	2,597	2,701	2,801	2,904
Output gap	-0.4	1.3	0.7	-0.3	0.0	0.0	0.0
<b>Expenditure components of real GDP</b>							
Household consumption	-10.5	6.1	5.4	1.0	1.5	1.1	1.2
General government consumption	-5.4	14.5	2.6	1.2	1.4	1.6	2.0
Business investment	-11.4	-0.7	10.6	5.6	3.6	5.4	4.5
General government investment	2.7	11.9	-1.1	7.8	-2.0	1.1	1.7
Net trade <sup>1</sup>	0.8	-1.2	-0.6	-0.1	0.5	0.0	-0.1
<b>Inflation</b>							
CPI	0.9	2.6	7.4	4.0	1.5	1.9	2.0
<b>Labour market</b>							
Employment (million)	32.5	32.4	32.7	32.9	33.1	33.2	33.3
Average earnings	1.8	6.2	5.3	2.8	2.6	2.9	3.2
LFS unemployment (rate, per cent)	4.6	4.5	4.0	4.2	4.1	4.1	4.1
Productivity (output per hour)	1.3	1.2	-0.2	1.0	1.6	1.3	1.3

<sup>1</sup> Contribution to GDP growth.



## Fiscal outlook

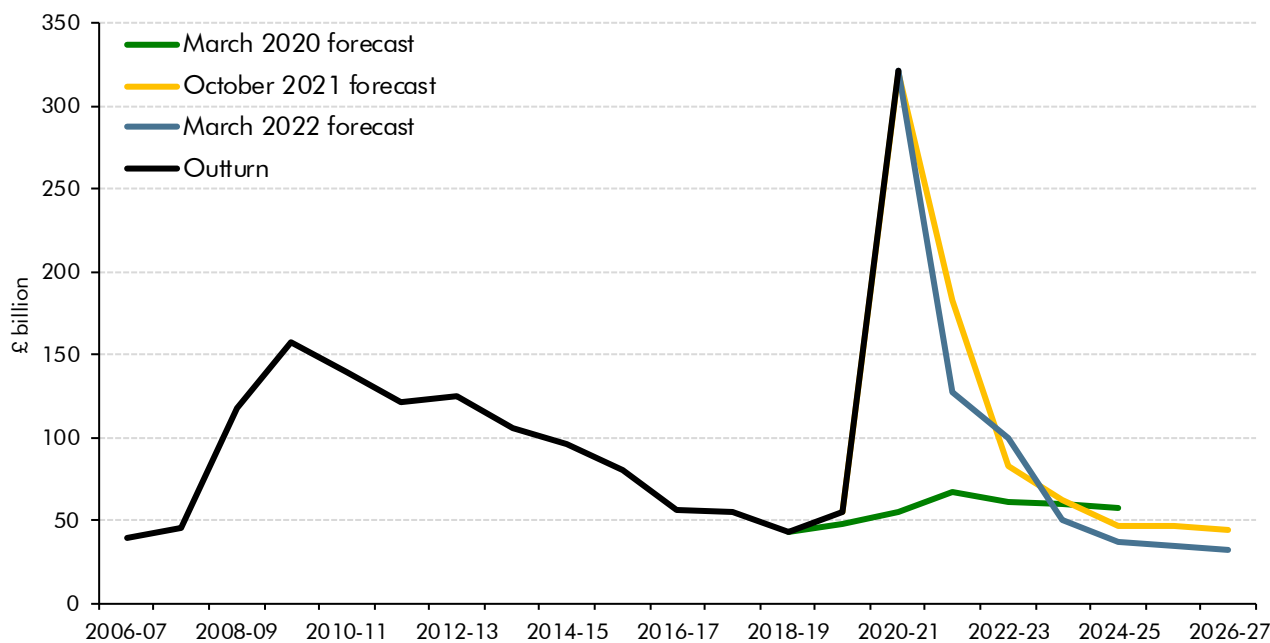
### Developments since October

1.22 Despite the challenging economic backdrop, borrowing in 2021-22 has been revised down sharply – by £55 billion relative to our October forecast to £128 billion (5.4 per cent of GDP). Tax receipts have been revised up £38 billion (4.4 per cent) this year thanks to strong growth in income tax (especially from those in higher tax brackets) and corporation tax (especially from the financial sector), as well as much higher self-assessment payments over the past two months. Growth in tax receipts has outstripped growth in nominal GDP, pointing to a more tax-rich composition of economic activity and a stronger medium-term revenue outlook. Departmental spending has come in lower than expected again (by £9.4 billion, or 1.9 per cent), as has local authority spending; only debt interest costs are materially higher, as the spike in RPI inflation has hit index-linked debt, adding £13.1 billion to debt interest spending since October. Overall, borrowing falls 60 per cent this year from the post-World War II record of £322 billion (15.0 per cent of GDP) it reached in 2020-21. This partly reflects the withdrawal of pandemic-related fiscal support, which we now estimate to have totalled £310 billion, of which just under half went to public services, a third went to households, and a fifth went to businesses.

### Fiscal prospects

1.23 Despite the large undershoot this year, borrowing in 2022-23 is £16.1 billion *higher* than we forecast in October at £99.1 billion (3.9 per cent of GDP). That reflects the spike in inflation – both directly via debt interest and indirectly via the policies put in place to help households cope with higher prices – outweighing the £30.1 billion pre-measures upward revision to receipts. Debt interest spending jumps to a nominal record high of £83.0 billion, double our October forecast and its highest level as a share of revenue since 1997-98. Policy support for household incomes in 2022-23 totals £17.6 billion, with £8.9 billion coming via support for households' energy bills (£6.0 billion of which is recouped over the subsequent five years), £2.4 billion via a one-year 5p cut in fuel duty, and £6.3 billion via raising the primary NICs threshold from £9,880 to £12,570. These costs are partly offset by student loans reforms that reduce the effective subsidy provided by the state for new loans from over half to just over a third in the long term, but for which the associated fiscal savings are recorded upfront, lowering borrowing by £11.2 billion.

Chart 1.6: Public sector net borrowing



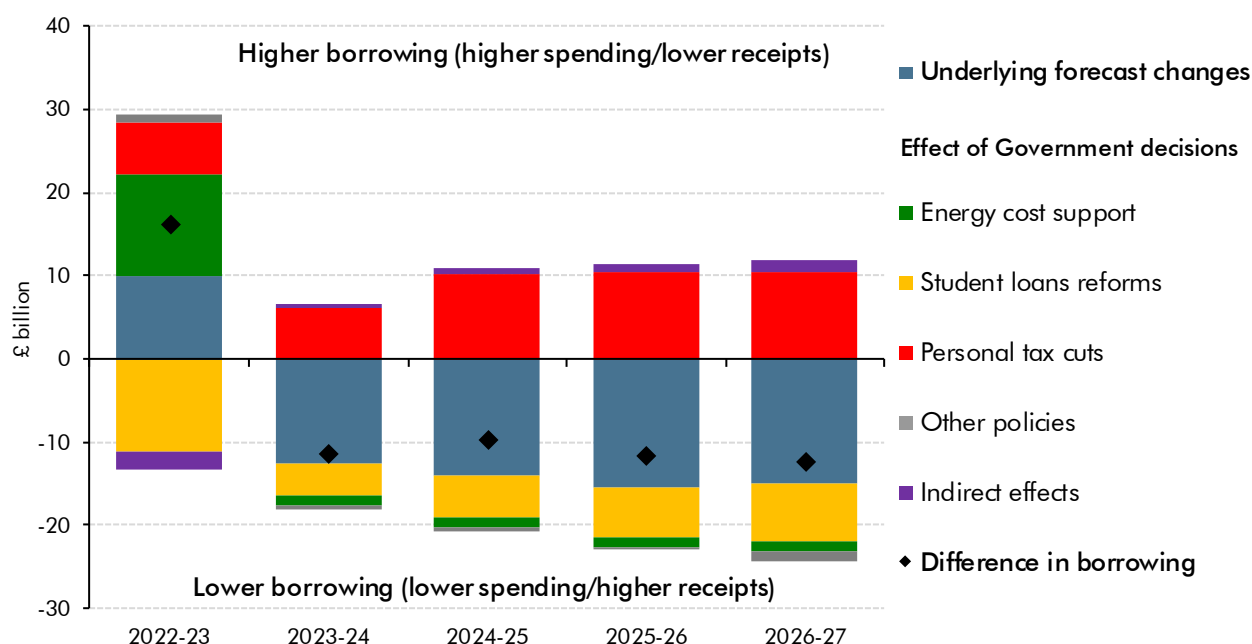
Source: ONS, OBR

1.24 Borrowing continues to fall in subsequent years, reaching a little over 1 per cent of GDP (£31.6 billion) in 2026-27. This would be the smallest budget deficit for 25 years and 0.8 per cent of GDP lower than our pre-pandemic March 2020 forecast for 2024-25 (the final year of that forecast). Between 2023-24 and 2026-27, borrowing is around ½ per cent of GDP (£11 billion) below our October forecast. Focusing on changes in the level of borrowing in the fiscal target year of 2024-25 since that forecast, Chart 1.7 shows:

- **Forecast changes** have given the Chancellor a fiscal windfall of almost £15 billion in 2024-25. This reflects a £37 billion boost to receipts (largely from more tax-rich economic activity than we assumed in October), which is only partially offset by a £23 billion upward revision to spending (primarily due to higher interest rates adding to debt interest spending and higher inflation adding to welfare spending).
- The Chancellor has also freed up £5 billion in terms of borrowing (although not in terms of debt) from the **student loans reforms**.<sup>1</sup>
- He has used around half of this additional £20 billion of fiscal room for manoeuvre to finance two **personal tax cuts** – raising the primary NICs threshold to align with the income tax personal allowance from July 2022 and cutting the basic rate of income tax from 20 to 19 per cent from April 2024 – which together cost £10 billion in 2024-25.
- After factoring in other modest policy-related effects, this leaves £10 billion to **reduce borrowing**.

<sup>1</sup> Student loans affect borrowing and debt in different ways. The reforms reduce the proportion of cash outlays that are recorded upfront in accrued borrowing much more than they affect the overall cash outlays that matter for debt. See Box A.1 in Annex A.

Chart 1.7: Changes in public sector net borrowing since our October forecast



Source: ONS, OBR

Table 1.2: Changes to public sector net borrowing

	£ billion						
	Outturn	Forecast					
		2020-21	2021-22	2022-23	2023-24	2024-25	2025-26
March 2020 forecast	54.8	66.6	61.5	60.2	57.9		
October 2021 forecast	319.9	183.0	83.0	61.6	46.3	46.4	44.0
March 2022 forecast	321.9	127.8	99.1	50.2	36.5	34.8	31.6
<b>Difference since March 2020</b>	<b>267.1</b>	<b>61.2</b>	<b>37.7</b>	<b>-10.0</b>	<b>-21.4</b>		
of which:							
Underlying differences <sup>1</sup>	97.1	13.5	31.7	20.4	27.1		
Direct effect of Government decisions <sup>2</sup>	220.6	75.4	18.9	-20.9	-43.5		
Indirect effect of Government decisions	-50.6	-27.7	-12.9	-9.4	-5.0		
<b>Difference since October 2021</b>	<b>2.0</b>	<b>-55.2</b>	<b>16.1</b>	<b>-11.4</b>	<b>-9.8</b>	<b>-11.5</b>	<b>-12.4</b>
of which:							
Underlying differences <sup>1</sup>		-50.9	10.0	-12.5	-14.1	-15.4	-15.0
Direct effect of Government decisions		-4.2	8.3	0.6	3.6	2.9	1.2
Indirect effect of Government decisions		0.0	-2.1	0.5	0.7	1.0	1.3

Note: This table uses the convention that a negative figure means a reduction in PSNB i.e. an increase in receipts or a reduction in spending will have a negative effect on PSNB.

<sup>1</sup> Includes classification changes.

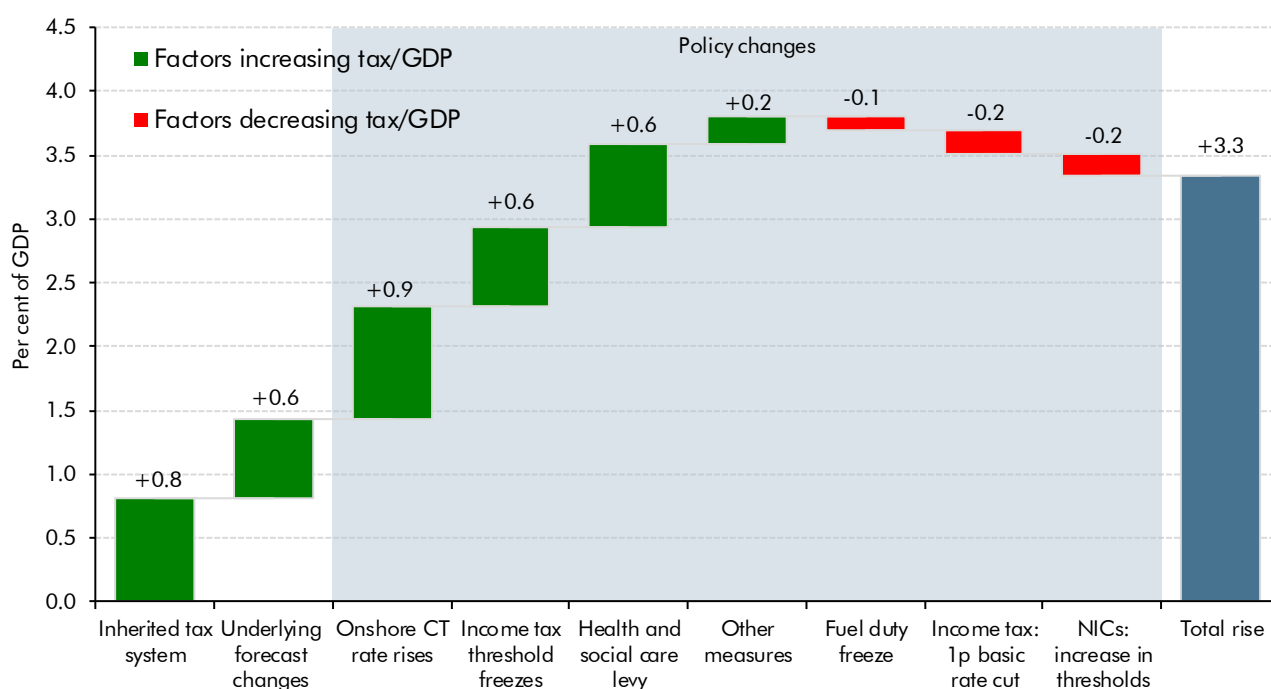
<sup>2</sup> The cost of policy decisions announced up to and including at October 2021 Budget and Spending Review has been adjusted to include significant updates to estimates via the usual recosting process.

**1.25** Net tax cuts announced in this Spring Statement offset around a sixth of the net tax rises introduced by this Chancellor since he took over the role in February 2020, and just over a quarter of the personal tax rises he announced last year (the freezing of the income tax personal allowance and higher-rate threshold and new health and social care levy). Those net tax rises, plus the more tax-rich composition of economic activity that has been factored into this forecast, raise the tax burden from the 33.0 per cent of GDP recorded in 2019-20

to 36.3 per cent of GDP in 2026-27 – its highest level since the late 1940s.<sup>2</sup> This 3.3 per cent of GDP increase in the tax burden in the space of seven years reflects (Chart 1.8):

- **Plans this Chancellor inherited** in March 2020 and **underlying forecast changes**, including higher effective tax rates observed this year and largely carried through to the rest of the period, which together raise the tax burden by 1.4 per cent of GDP.
- **Previously announced net tax rises** that add a further 2.2 per cent of GDP to the tax burden. These include the increase in the main rate of corporation tax to 25 per cent from April 2023, the income tax personal allowance and higher-rate threshold freezes, and the introduction of the new health and social care levy. These are partly offset by the cost of the customary annual fuel duty freezes.
- **Tax cuts announced in this Spring Statement** that lower the tax burden by 0.4 per cent of GDP. The personal tax cuts lower the tax take by £11 billion in 2026-27. Unlike previous freezes, the temporary 5p cut to fuel duty does not affect the tax burden in the medium term because it is slated to be reversed after 12 months, with RPI indexation on top implying an 8p increase next year – although the past decade of fuel duty freezes highlights a risk that that will not happen.

Chart 1.8: The rise in the tax-to-GDP ratio between 2019-20 and 2026-27



Note: This reflects the National Accounts measure of taxes.  
Source: OBR

<sup>2</sup> This refers to the National Accounts measure of taxes and National Insurance contributions.

- 1.26** Public spending is on a declining path as a share of GDP throughout the forecast period, though it settles at 41.1 per cent of GDP in 2026-27, 2.1 per cent of GDP higher than in 2019-20 and the highest sustained level since the late 1970s. Relative to our October forecast, it has been revised up sharply in 2022-23 (by £41 billion) and by material amounts thereafter (£17 billion a year on average). This largely reflects inflation-driven revisions to welfare spending (via the uprating of awards) and to debt interest spending, which is also affected by higher interest rates. Indeed, the effect of higher RPI inflation on debt interest explains all the addition to public spending in 2022-23, with debt interest hitting a record £83 billion in nominal terms (and a 36-year high of 3.3 per cent of GDP). Comparatively small net spending reductions in the Spring Statement offset an average of £5.4 billion a year of the upward revisions in our pre-measures forecast from 2023-24.
- 1.27** Lower cumulative borrowing across the forecast means that headline public sector net debt (including the Bank of England) peaks as a share of GDP in 2021-22, before falling to 83.1 per cent of GDP by 2026-27. Debt has been revised down from our October forecast in all years, by 2.7 per cent of GDP this year and by larger amounts thereafter, rising to 4.8 per cent of GDP in 2026-27 (left panel of Chart 1.9). Even so, the debt-to-GDP ratio in 2024-25 is 16 percentage points higher than in our pre-pandemic March 2020 forecast. But while debt has been revised down, the higher paths for RPI inflation in the near term and for interest rates throughout the forecast have raised the cost of servicing the debt (right panel). Indeed, the record-high accrued spending on index-linked debt next year takes the debt-interest-to-revenue ratio to a 25-year high of 7.6 per cent, and while it falls back to a historically low average of 3.4 per cent across the final three years of the forecast, that remains 0.7 percentage points higher than in our October forecast.

Chart 1.9: Public sector net debt and debt servicing costs

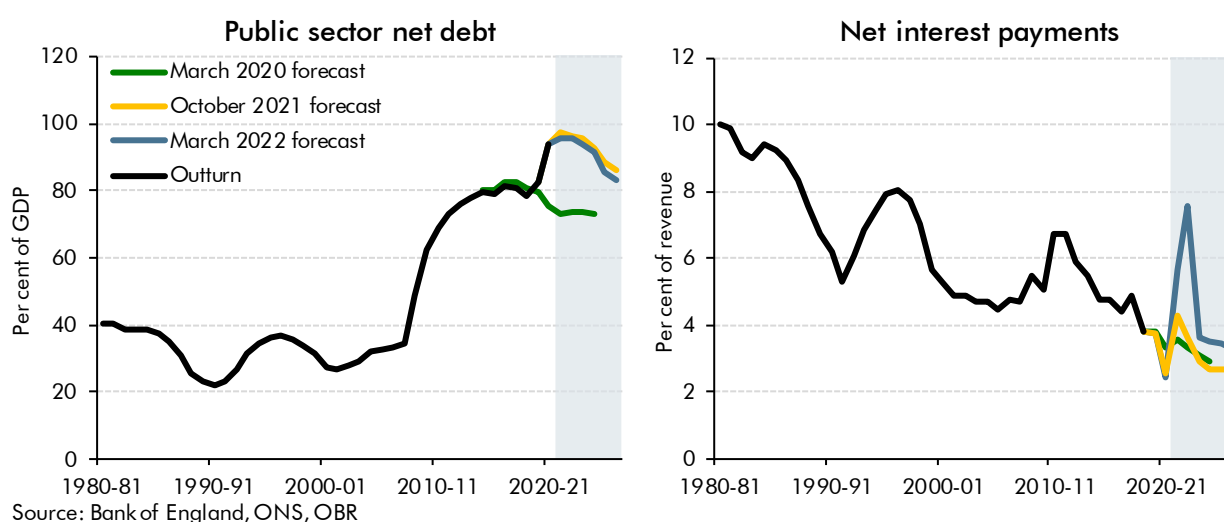


Table 1.3: Overview of the fiscal forecast

	Per cent of GDP, unless otherwise stated						
	Outturn	Forecast					
		2020-21	2021-22	2022-23	2023-24	2024-25	2025-26
<b>Revenue and spending</b>							
Public sector current receipts	37.0	38.0	39.3	40.1	40.0	40.0	40.1
Total managed expenditure	52.1	43.4	43.2	42.0	41.3	41.2	41.1
<b>Deficit: Current supplementary targets and previous fiscal mandate measures</b>							
Current budget deficit	11.7	3.8	1.7	-0.8	-1.2	-1.3	-1.4
Public sector net investment	3.4	1.6	2.2	2.7	2.5	2.5	2.5
Public sector net borrowing	15.0	5.4	3.9	1.9	1.3	1.2	1.1
Cyclically adjusted net borrowing	14.9	6.1	4.4	1.9	1.3	1.3	1.1
<b>Debt: Current fiscal mandate and previous supplementary target measure</b>							
Public sector net debt ex BoE	83.9	82.5	83.5	82.9	81.9	80.9	79.8
Public sector net debt	94.0	95.6	95.5	94.1	91.2	85.8	83.1
£ billion							
<b>Revenue and spending</b>							
Public sector current receipts	793.0	899.5	987.5	1,050	1,090	1,131	1,175
Total managed expenditure	1,115	1,027	1,087	1,100	1,127	1,166	1,206
<b>Deficit: Current supplementary targets and previous fiscal mandate measures</b>							
Current budget deficit	250.2	89.5	42.7	-21.9	-31.6	-36.2	-40.6
Public sector net investment	71.8	38.3	56.4	72.0	68.1	71.0	72.2
Public sector net borrowing	321.9	127.8	99.1	50.2	36.5	34.8	31.6
Cyclically adjusted net borrowing	318.6	143.7	109.9	48.6	35.6	35.3	31.7
<b>Debt: Current fiscal mandate and previous supplementary target measure</b>							
Public sector net debt ex BoE	1,905	2,011	2,145	2,218	2,274	2,329	2,382
Public sector net debt	2,134	2,330	2,453	2,516	2,533	2,469	2,480

## Performance against the Government's fiscal targets

1.28 In our central forecast, the Government's fiscal mandate and all three supplementary targets are met. The rolling three-year-ahead targets for falling debt and the current balance are also each met a year early in 2023-24. The improved fiscal outlook means the Government has a little more headroom against these targets than we predicted in October:

- The fiscal mandate to have **public sector net debt (excluding the Bank of England)** as a share of GDP falling by the third year of the rolling forecast period (currently 2024-25) is met by a margin of 1.0 per cent of GDP (£27.8 billion), a 0.4 per cent of GDP (£10.3 billion) improvement relative to our October forecast.
- The supplementary target to balance the **current budget** by the third year of the rolling forecast period is met by a margin of 1.2 per cent of GDP (£31.6 billion), a 0.2 per cent of GDP (£6.5 billion) improvement relative to October.
- The cap requiring **public sector net investment** not to exceed 3 per cent of GDP on average over the rolling five-year forecast period is met by a margin of 0.5 per cent of GDP (£13.8 billion), a 0.3 per cent of GDP (£6.5 billion) increase from October. This

reflects the accounting treatment of long-term fiscal savings from student loans reforms rather than any reductions in department capital spending plans.

- The ‘welfare cap’, which requires that a subset of **expenditure on welfare** is contained within a predetermined cap in 2024-25 set by the Treasury, is met by £5.3 billion, a £2.6 billion improvement relative to October. This might seem surprising when spending subject to the cap has been revised up by £3.2 billion in 2024-25 relative to our October forecast, but that is because the Treasury stipulates that an ‘inflation adjustment’ should in effect raise or lower the welfare cap to reflect the consequences of inflation surprises relative to forecast for the uprating of benefits subject to the cap.

Table 1.4: Performance against the Government’s fiscal targets

		Per cent of GDP		£ billion	
		Forecast	Margin	Forecast	Margin
<b>Year-on-year change in public sector net debt excluding the Bank of England in 2024-25</b>					
March 2020 forecast		-0.2	0.2		5.7
October 2021 forecast	Met	-0.6	0.6		17.5
March 2022 pre-measures forecast	Met	-1.3	1.3		34.9
March 2022 forecast	Met	-1.0	1.0		27.8
<b>Current budget surplus in 2024-25</b>					
March 2020 forecast		0.8	0.8	21.2	21.2
October 2021 forecast	Met	0.9	0.9	25.1	25.1
March 2022 pre-measures forecast	Met	1.5	1.5	41.3	41.3
March 2022 forecast	Met	1.2	1.2	31.6	31.6
<b>Public sector net investment average over the five-year forecast</b>					
March 2020 forecast		2.9	0.1		2.7
October 2021 forecast	Met	2.7	0.3		7.3
March 2022 pre-measures forecast	Met	2.7	0.3		8.8
March 2022 forecast	Met	2.5	0.5		13.8
<b>Welfare cap: specified welfare spending in 2024-25</b>					
October 2021 forecast	Met			138.3	2.8
March 2022 forecast	Met			137.4	5.3

1.29 These margins are consistent with a 58 and 66 per cent chance of meeting the debt falling and current balance targets, respectively. They are broadly in line with the headroom retained by previous Chancellors but could be wiped out by relatively small changes to the economic outlook, including a 1.3 percentage point shortfall in GDP growth in 2024-25 or a 1.3 percentage point increase in the effective interest rate in 2024-25.

1.30 More broadly, the modest improvement in headroom needs to be set against the elevated risks to the economic and fiscal outlook, with the Russian invasion of Ukraine the latest in a series of global shocks in the first quarter of this century. Greater disruption to energy markets from the war in Ukraine, widening of the conflict, or further tightening of international sanctions could mean energy prices and inflation remain higher for longer. Our energy markets downside scenario based on the highest market prices over the past three weeks – but with prices still dropping back sharply next year – reduces fiscal target headrooms by between £4 billion and £7 billion in 2024-25. And with infections rising at

home and abroad, our Covid downside scenario suggests the emergence of a vaccine-escaping Covid variant next winter could trigger another 3½ per cent fall in real output at its most severe point and with it demands for further fiscal support.

- 1.31 The more inflationary environment creates risks in specific policy areas. Despite the £9 billion in fiscal support for household energy bills delivered in the Spring Statement, pressure for more could build if the energy price cap in October does rise by the roughly 40 per cent assumed in our central forecast. Similarly, having frozen fuel duty in cash terms for the previous 12 years, the Government's plans for an RPI+5p super-indexation of fuel duty next year, which adds £3.6 billion to receipts but would raise petrol pump prices by 6 per cent overnight, are ambitious. In the welfare system, lags in CPI uprating of benefits means they fall by almost 5 per cent in real terms in 2022-23, reducing their real value by £12 billion, and take up to 18 months to catch up fully with higher inflation. Higher inflation has also eroded the real value of the departmental budgets set in cash terms in October's Spending Review by between £5 billion and £17 billion, while many departments are still coping with pandemic-related backlogs. And these policy and delivery pressures must all be managed in a context of heightened sensitivity of government borrowing costs to higher inflation and interest rates – as illustrated by the doubling of debt interest costs in 2022-23 from our October forecast, and the £9 billion a year upward revisions in interest cost thereafter.