1 Executive summary

Overview

1.1 The economy grew slightly more strongly than we expected in our last forecast during 2012 as a whole, but it also shrank a little more than we expected in the final quarter – mainly due to disrupted production in the North Sea. With the economy entering 2013 with somewhat less momentum than we expected in December, a weaker outlook for consumer spending, business investment and exports has prompted us to revise down our near-term growth forecasts to 0.6 per cent this year and 1.8 per cent in 2014.

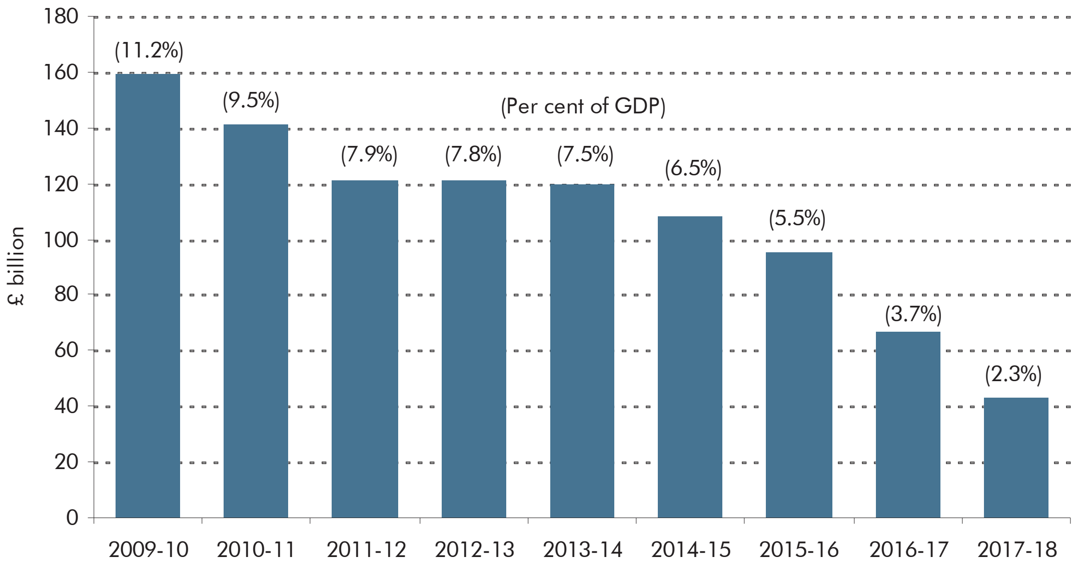
1.2 Our growth forecasts are unchanged thereafter, rising steadily to 2.8 per cent by 2017. The pace of recovery is constrained by slow growth in productivity and real incomes, continued problems in the financial system, the fiscal consolidation and the outlook for the global economy. We expect real GDP to be 0.6 per cent lower in 2017-18 than we thought in December, with nominal GDP 2.6 per cent lower as we have also revised down our forecast for whole economy inflation.

1.3 Chart 1.1 shows that public sector net borrowing (PSNB) – the gap between what the Government spends and raises in revenue – fell by a quarter between 2009-10 and 2011-12, thanks primarily to the tax increases and public spending cuts announced by this and the previous government. But, after adjusting for special factors, the decline in cash borrowing now appears to have stalled. We expect PSNB to be broadly flat this year and next, resuming its fall in 2014-15.

1.4 The headline measure of PSNB is forecast to come in at £86 billion this year, well down from its post-war peak of £159 billion in 2009-10. But excluding the Government's decisions to bring the Royal Mail's historic pension fund assets into the public sector, and to transfer the cash balances in the Bank of England's Asset Purchase Facility (APF) to the Exchequer, we forecast underlying deficits very close to £120 billion in 2011-12, 2012-13 and 2013-14.

1.5 We have raised our forecast for the underlying deficit this year by £1 billion since December. Tax receipts are around £5.1 billion lower (after adjusting for statistical reclassifications), mostly due to unexpectedly weak income tax and North Sea revenues. But the Government has chosen to offset most of the impact on the deficit by bearing down on spending by central government departments. We now expect departments to underspend the plans it set out last March by almost £11 billion this year, £3.4 billion more than we forecast in December. Our forecast for other spending is also £0.7 billion lower than in December.

Chart 1.1: Public sector net borrowing excluding the Royal Mail and Asset Purchase Facility transfers



Source: OBR

1.6 The underlying deficit is higher in cash terms throughout the forecast, with an upward revision of £11.8 billion by 2017-18. This reflects the weaker outlook for the economy and tax receipts. Relative to the size of the economy, receipts remain broadly flat through the forecast, as in December. Public spending falls by only 0.3 per cent of GDP between 2011-12 and 2013-14, compared to 0.8 per cent in December – downward revisions to nominal GDP push up given cash spending as a share of GDP. Thereafter public spending and the underlying deficit both fall at roughly the same rate as we expected in December.

1.7 The tax and spending measures in the Treasury's Budget policy decisions table have a relatively modest impact on the deficit, increasing or reducing it by no more than £3 billion (0.2 per cent of GDP) in any one year. The 'giveaways' and 'takeaways' net to zero when aggregated over the forecast. We have made no significant adjustments to our economic forecast to reflect these measures. The Treasury's table does not include the impact of its action to reduce spending by central government departments in 2012-13.

1.8 The Government's 'fiscal mandate' requires it to balance the cyclically-adjusted current budget (CACB) – the amount the Government borrows to finance non-investment spending, adjusted for the state of the economy – five years ahead. Our central forecast shows the CACB in surplus by 0.8 per cent of GDP in 2017-18, implying that the Government is more likely than not to meet the mandate. Thanks to the Budget measures, the CACB is also just in surplus in 2016-17.

1.9 Public sector net debt (PSND) is forecast to peak at 85.6 per cent of GDP in 2016-17, rather than 79.9 per cent a year earlier as in our December forecast. This means that the Government is once again not on course to achieve its 'supplementary target' of reducing PSND as a share of GDP in 2015-16. The cash value of PSND has been pushed higher by our upward revisions to PSNB and by assumptions about gilt issuance. Our downward revision to nominal GDP also means that a given cash debt now corresponds to a larger share of GDP.

1.10 There is huge uncertainty around all public finance projections, especially over this time horizon. We stress test the Government's chances of achieving its targets using sensitivity and scenario analysis. A key risk is that potential output turns out to be lower at the end of the forecast than we currently assume. More of the deficit would then be structural and would remain after the economy recovers.

Economic developments since our previous forecast

1.11 The latest data suggest that the UK economy shrank by 0.3 per cent in the final quarter of 2012. This was slightly larger than the 0.1 per cent fall we forecast in December, reflecting disrupted North Sea oil production. Output rose by 0.2 per cent in 2012 as a whole, against our December forecast of a 0.1 per cent fall. Surveys suggest little pick-up in underlying activity in recent months.

1.12 The labour market continues to surprise on the upside, despite the continued weakness of GDP growth. Employment rose to 29.7 million in the three months to December, against our December forecast that it would remain at 29.6 million. This increase was driven by a rise in full-time employees. Total hours worked per week rose by a further 2 million in the fourth quarter of 2012, to 947 million, compared to our forecast of a marginal fall of 1.4 million. The unemployment rate remains at 7.8 per cent, against our forecast of a slight increase to 7.9 per cent in the three months to December.

1.13 Earnings growth has been weaker than expected. Growth in average weekly earnings in the private sector in the fourth quarter of 2012 fell to 1.3 per cent, compared to 2.0 per cent in the third quarter and our December forecast for the fourth quarter of 2.0 per cent.

1.14 Our December forecast of 1.2 per cent GDP growth for 2013 was marginally above the average of outside forecasts at the time. Subsequently, the average forecast has fallen to 0.9 per cent. This partly reflects weaker-than-expected fourth quarter GDP, which suggests slightly less momentum going into 2013 than many forecasters envisaged at the time of our December forecast.

The economic outlook

1.15 We expect the economy to grow by 0.6 per cent this year and 1.8 per cent in 2014, down from 1.2 and 2.0 per cent respectively in our December forecast. These revisions reflect smaller contributions from net trade and consumption, as relatively weak UK export markets reduce the scope for export growth and sluggish disposable income growth weighs on household consumption. We also expect a smaller contribution from business investment, as upward revisions to the starting level lead us to expect less growth looking forward.

1.16 Business and consumer surveys, and other cyclical indicators, suggest that spare capacity in the economy was flat or shrank in the final quarter of 2012. This would imply that the weakness in output over this period was structural and that trend total factor productivity (TFP) had contracted. As in December we believe wider indicators are hard to square with severe renewed structural weakness. So we assume that the output gap was -2.7 per cent of potential in the fourth quarter, consistent with flat rather than negative trend TFP growth over 2012.

1.17 We have not changed our view on the outlook for potential growth since December. We expect it to pick up steadily, but still to remain below its long-term rate by the end of our forecast. This is consistent with the view that the financial system will remain impaired for some time to come and that the persistently negative output gap will itself weigh down on potential GDP.

1.18 There are some grounds for optimism as regards financial markets, with relative calm in the euro area and the Funding for Lending (FLS) scheme helping to improve bank funding conditions. But there is little evidence that this is yet increasing lending to the real economy. The situation in the euro area also remains a major risk to our forecast, with the underlying situation still fragile and the completion of long-term structural and institutional reforms a long way off.

1.19 Our view on medium-term growth prospects is unchanged from December. We expect the economy to grow by 2.3 per cent in 2015, 2.7 per cent in 2016 and 2.8 per cent in 2017. With GDP growing less quickly than potential GDP in the near term, the output gap widens to -3.8 per cent by the end of 2013.

1.20 Growth is not expected to return to above-trend rates until 2015, as credit conditions begin to normalise and real wages and productivity start to recover, supporting the growth of consumption. Even then, the output gap is assumed to narrow only at a relatively gradual rate thereafter, reflecting slow growth in productivity and real incomes, continued problems in financial markets, the fiscal consolidation, and the weak outlook for the global economy.

Table 1.1: Economic forecast overview

	Percentage change on a year earlier, unless otherwise stated						
	Outturn	Forecast[1]					
	2011	2012	2013	2014	2015	2016	2017
Output at constant market prices							
Gross domestic product (GDP)	0.9	0.2	0.6	1.8	2.3	2.7	2.8
GDP Level (2011 =100)	100.0	100.2	100.8	102.6	105.0	107.8	110.8
Output gap (per cent of potential output)	-2.7	-2.7	-3.6	-3.7	-3.4	-2.9	-2.3
Expenditure components of GDP at constant market prices							
Household consumption[2]	-1.0	1.0	0.5	1.2	1.7	2.4	2.8
Business investment	3.1	4.9	1.9	6.1	8.6	8.6	8.6
General government consumption	-0.1	2.6	0.4	-0.7	-0.4	-1.0	-1.8
General government investment	-26.2	2.7	2.6	5.0	1.8	-1.5	-1.2
Net trade[3]	1.2	-0.8	0.1	0.1	0.1	0.1	0.1
Inflation							
CPI	4.5	2.8	2.8	2.4	2.1	2.0	2.0
Labour market							
Employment (millions)	29.2	29.5	29.8	29.9	30.1	30.3	30.5
Average earnings[4]	2.3	2.1	1.4	2.7	3.6	4.0	4.0
ILO unemployment (% rate)	8.1	7.9	7.9	8.0	7.9	7.4	6.9
Claimant count (millions)	1.53	1.59	1.58	1.63	1.59	1.48	1.38
	Changes since December forecast						
Output at constant market prices							
Gross domestic product (GDP)	0.0	0.3	-0.6	-0.3	0.0	0.0	0.0
GDP Level (2011=100)[5]	0.0	0.3	-0.3	-0.6	-0.6	-0.6	-0.6
Output gap (per cent of potential output)	0.0	0.3	-0.1	-0.3	-0.3	-0.3	-0.4
Expenditure components of GDP at constant market prices							
Household consumption[2]	-0.1	0.4	-0.4	-0.3	-0.1	-0.1	-0.1
Business investment	0.2	1.1	-3.0	-2.1	-1.6	-1.5	-0.9
General government consumption	-0.3	0.2	1.1	0.7	0.8	1.1	1.3
General government investment	-5.9	11.9	5.1	0.1	4.8	1.1	-1.9
Net trade[3]	0.0	-0.1	-0.1	0.0	0.0	0.0	0.0
Inflation							
CPI	0.0	0.0	0.3	0.2	0.1	0.0	0.0
Labour market							
Employment (millions)	0.0	0.0	0.2	0.1	0.1	0.1	0.1
Average earnings[4]	0.1	-0.7	-0.8	0.0	-0.1	0.0	0.0
ILO unemployment (% rate)	0.0	0.0	-0.3	-0.2	-0.1	-0.2	-0.2
Claimant count (thousands)	0	-4	-78	-63	-41	-49	-53

[1] The forecast is consistent with the second estimate of GDP data for the fourth quarter of 2012, released by the Office for National Statistics on 27th February 2013.

[2] Includes households and non-profit institutions serving households.

[3] Contribution to GDP growth, percentage points.

[4] Wages and salaries divided by employees.

[5] Per cent change since December.

1.21 Over time we expect the recovery to be supported by contributions from private consumption, business investment and net trade:

- a weaker outlook for disposable income has led us to expect a smaller contribution from consumption to GDP growth than in December. Consumption growth is expected to slow this year, remain subdued in 2014, and then pick up from 2015 as disposable income growth recovers;
- business investment is forecast to make a relatively significant contribution to the recovery in growth in the medium term. But we have again revised down our forecast for business investment growth, as data revisions have increased the starting level and thus limited the scope for further growth;
- there is a small positive contribution from net trade over the forecast period, though weak recent export performance means that this contribution is slightly smaller in the near-term than we forecast in December; and
- government consumption reduces GDP growth from 2014, but less so than in December, reflecting further data revisions suggesting that real government consumption is holding up relative to nominal spending.

1.22 The labour market performed more strongly in the fourth quarter than we expected in December, with surveys pointing to continued employment growth into 2013. As a result we have revised up our employment forecast and lowered our unemployment forecast. We now expect unemployment to peak at 8.0 per cent of the labour force in 2014 before falling back to 6.9 per cent in 2017.

1.23 Total market sector employment is expected to rise by around 2.6 million between the start of 2011 and the start of 2018, more than offsetting a total reduction in general government employment of around 1.2 million.

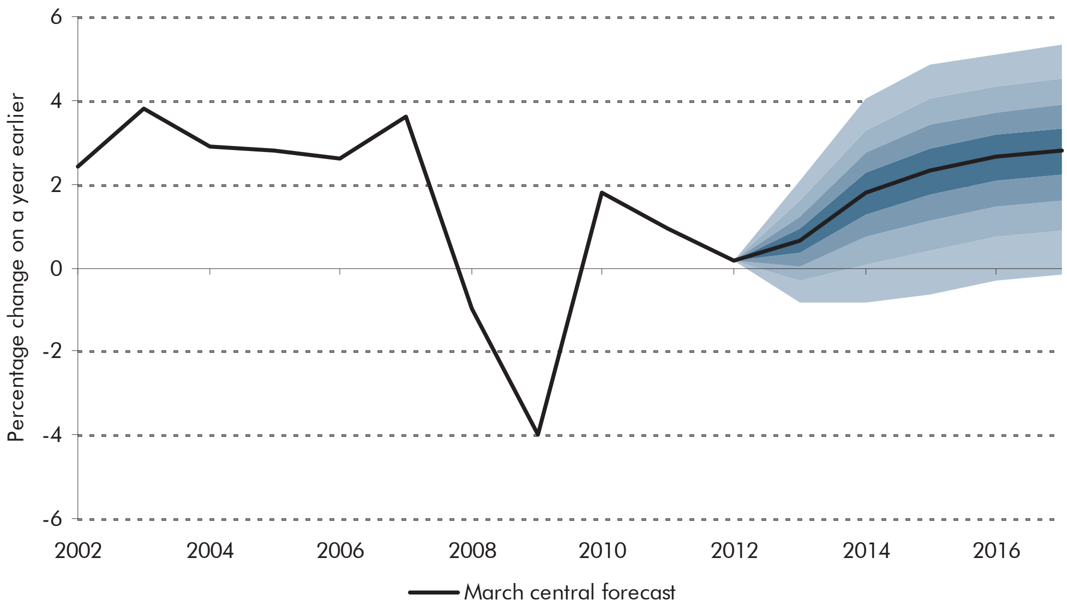
1.24 Higher employment and lower GDP growth mean that productivity growth is forecast to be weaker than in December. As a result we have also made a slight downward revision to our forecast for nominal wage growth since December. Our forecast for real wage growth is also weaker than in December. We now expect real wage growth to be negative in 2013 and only marginally positive in 2014 before picking up in 2015 and reaching 2 per cent in 2016.

1.25 We expect CPI inflation to be higher in 2013 than we forecast in December, due to recent outturn data and higher oil prices. We also assume that sterling's recent depreciation will put upward pressure on CPI inflation over the next few years by pushing up import prices. Overall, we expect CPI inflation to rise towards the middle of this year and then fall gradually over 2014 and 2015.

1.26 We have also lowered our forecast for the GDP deflator, due to recent data and a reassessment of the rate of growth in the price of government consumption. The level of nominal GDP in 2017-18 is 2.6 per cent lower than in our December forecast. Of this, 0.6 per cent is attributable to a lower level of real GDP, with the remainder reflecting a lower GDP deflator. Around two-thirds of the reduction in real GDP is assumed to be cyclical rather than structural and persistent.

1.27 There is considerable uncertainty around any economic forecast. Chart 1.2 presents our central growth forecast with a fan showing the probability of different outcomes based on the pattern of past official forecasting errors. The solid black line shows our median forecast, with successive pairs of lighter shaded areas around it representing 20 per cent probability bands. It suggests there is a roughly 30 per cent chance that the economy will shrink in 2013.

Chart 1.2: GDP fan chart



Source: ONS, OBR

The fiscal outlook

1.28 Public sector net borrowing (PSNB) is estimated to have fallen by about a quarter from its post-war peak of £158.9 billion (11.2 per cent of GDP) in 2009-10 to £121.0 billion (7.9 per cent of GDP) in 2011-12. We forecast that it will come in at £86.5 billion (5.6 per cent of GDP) this year, but this figure is flattered by Government policy decisions that have a temporary impact on the deficit.

1.29 Excluding the decisions to transfer the Royal Mail's historic pension assets to the public sector, and the surpluses in the Bank of England's Asset Purchase Facility

(APF) to the Exchequer, the underlying PSNB is expected to be little changed this year or next from the figure recorded in 2011-12. Specifically, we forecast an underlying deficit of £120.9 billion (7.8 per cent of GDP) in 2012-13, and £119.8 billion (7.5 per cent of GDP) in 2013-14.

1.30 Given the uncertainty surrounding all public finance forecasts – and the typical size of revisions to the outturn data – the small falls in PSNB in 2012-13 and 2013-14 are fiscally and statistically insignificant. Over the past 20 years the average in-year error for the official PSNB forecasts made at Budget time has been 0.3 per cent of GDP or about £5 billion in today's terms.

1.31 The underlying deficit is then expected to fall more sharply again from 2014-15, dropping from 6.5 per cent of GDP in that year to 2.3 per cent of GDP in 2017-18. We expect public spending to fall from 45.2 per cent of GDP next year to 40.5 per cent in 2017-18, despite an increase in debt interest spending of 0.7 per cent of GDP over the same period. Public sector receipts are expected to be broadly flat, falling from 38.4 per cent of GDP next year to 38.3 per cent in 2017-18.

Table 1.2: Fiscal forecast overview

	Per cent of GDP						
	Outturn	Forecast					
	2011-12	2012-13	2013-14	2014-15	2015-16	2016-17	2017-18
Public sector net borrowing	7.9	5.6	6.8	5.9	5.0	3.4	2.2
Cyclically-adjusted net borrowing	6.0	3.6	4.3	3.3	2.7	1.3	0.6
Surplus on current budget	-6.0	-6.0	-5.2	-4.3	-3.5	-1.9	-0.9
Fiscal mandate and supplementary target							
Cyclically-adjusted surplus on current budget	-4.2	-4.0	-2.8	-1.7	-1.2	0.1	0.8
Public sector net debt[1]	71.8	75.9	79.2	82.6	85.1	85.6	84.8
	Changes since December forecast						
Public sector net borrowing	0.0	0.4	0.6	0.7	0.9	0.7	0.6
Cyclically-adjusted net borrowing	0.0	0.6	0.6	0.4	0.6	0.5	0.3
Surplus on current budget	0.1	-0.3	-0.6	-0.6	-0.7	-0.5	-0.4
Cyclically-adjusted surplus on current budget	0.1	-0.5	-0.6	-0.4	-0.4	-0.3	-0.2
Public sector net debt[1]	5.5	1.2	2.3	3.7	5.1	6.4	7.5
Underlying public sector net borrowing							
PSNB excluding Royal Mail and APF transfers	7.9	7.8	7.5	6.5	5.5	3.7	2.3

[1] Debt at end March; GDP centred on end March.

1.32 Table 1.3 shows that our forecast for underlying PSNB in 2012-13 is £1.0 billion higher than the estimate we made in December. Adjusting for statistical reclassifications, tax receipts this year are around £5.1 billion weaker than in December, primarily reflecting unexpectedly weak income tax and North Sea receipts over the last couple of months. But the impact on the deficit has been largely offset by the Government taking action to reduce central government departmental expenditure in 2012-13, including by pushing some spending into 2013-14. We anticipate that central government departmental expenditure will be £11 billion lower this year than the Treasury planned last March and £3.4 billion lower than we anticipated in December. Our forecast implies very low expenditure in the remainder of 2012-13, compared to previous years. But the outturn data may take some time to reflect the recent decisions and their impact may be reflected in revisions to the data for previous months.

Table 1.3: Change in public sector net borrowing

	£ billion						
	Outturn	Forecast					
	2011-12	2012-13	2013-14	2014-15	2015-16	2016-17	2017-18
Public sector net borrowing excluding Royal Mail and APF transfers							
December forecast	121.4	119.9	112	99	81	56	31
March forecast	121.0	120.9	120	108	96	67	43
Change	*-0.4*	*1.0*	*8.3*	*9.9*	*14.3*	*11.4*	*11.8*
of which:							
Receipts forecast[1]	-3.1	5.1	8.9	8.6	11.9	13.5	14.1
Expenditure forecast[1]	2.7	-0.7	-0.3	-0.9	-0.5	-0.4	-1.0
Measures in the Treasury's policy decision table	0.0	0.0	-1.3	1.6	2.8	-1.7	-1.3
Changes to departmental underspends[2]	0.0	-3.4	1.0	0.5	0.0	0.0	0.0

[1]Excluding fiscally neutral switches including the reclassification of SLS transfers and changes in the proportion of tax credits treated as negative tax

[2]Including as a result of action taken by the Government to reduce and/or delay expenditure

1.33 Compared to our December forecast, underlying PSNB excluding the Royal Mail and APF transfers is considerably higher each year from 2013-14, with the difference reaching £12 billion in 2017-18. Table 1.3 shows that this is driven by the following factors:

- forecasting changes increase borrowing by £13 billion in 2017-18. This is primarily driven by lower expected receipts, due to our weaker economic forecast. In particular our forecast for income tax and NICs is £6 billion lower by 2017-18 due to a lower forecast for labour income growth and due to the weakness of these receipts seen in recent months. A number of forecasting changes have left medium-term expenditure broadly unchanged from December; and

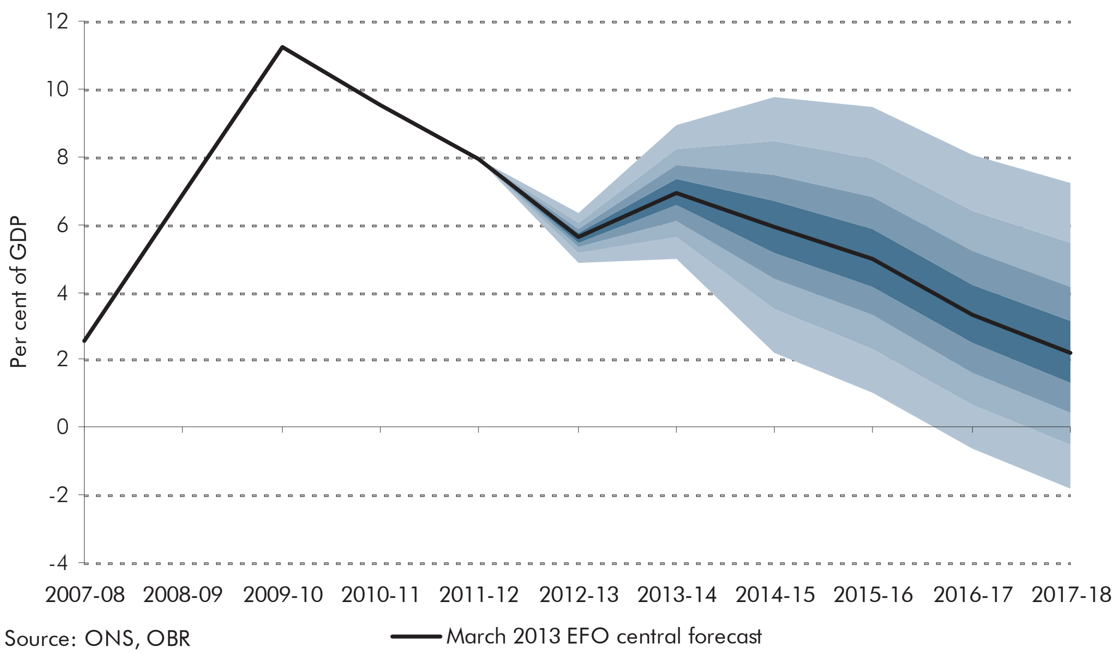
- policy measures on the Treasury's Budget policy decisions table are neutral over the forecast horizon, with a small fiscal tightening of £1.3 billion in 2017-18.

1.34 The current budget balance, which excludes borrowing to finance net investment spending, is forecast to move from a deficit of £93 billion or 6.0 per cent of GDP this year to a deficit of £16 billion or 0.9 per cent of GDP in 2017-18. Compared to our December forecast, the deterioration in the current budget is slightly less than the deterioration in PSNB, reflecting changes to investment spending.

1.35 The cyclically-adjusted current budget (CACB) moves from a deficit of 4.0 per cent of GDP in 2012-13 to a surplus of 0.8 per cent of GDP in 2017-18. The CACB in 2017-18 has deteriorated by 0.2 per cent of GDP compared to our December forecast. This is smaller than the 0.4 per cent of GDP deterioration in the unadjusted current budget balance, as most of the downward revision to the GDP forecast is deemed to be cyclical rather than structural.

1.36 All fiscal forecasts are subject to significant uncertainty. Chart 1.3 shows our median forecast for PSNB with successive pairs of shaded areas around it representing 20 per cent probability bands. As in Chart 1.2 above, the bands show the probability of different outcomes if the pattern of past official forecasting errors were to be a reasonable guide to future forecasting errors.

Chart 1.3: PSNB fan chart



Source: ONS, OBR

1.37 Public sector net debt (PSND) rises as a share of GDP each year up to and including 2016-17, peaking at 85.6 per cent of GDP, before falling to 84.8 per cent of GDP in 2017-18. PSND in 2017-18 is now expected to be around 7.5 per cent of GDP higher than we forecast in December. Table 1.4 breaks down this change as follows:

- the level of nominal GDP over the past year has been lower than we forecast in December, and we expect lower nominal GDP growth in the future. By reducing the denominator we use when calculating PSND as a share of GDP, this increases PSND by 2.2 per cent of GDP in 2017-18;
- our forecast for PSND in cash terms is also higher than in December, by 5.3 per cent of GDP in 2017-18. This is a consequence of:
  - higher net borrowing (excluding APF transfers) over the forecast period which leads to a rise in PSND of £56 billion by 2017-18;
  - a judgement that the Debt Management Office is likely to issue gilts at a lower premium relative to their nominal value than we assumed in December increases the forecast by £28 billion by 2017-18; and
  - other changes increase PSND by £15 billion in 2017-18. Budget measures increase net debt by £5 billion and the stock of Bradford & Bingley and Northern Rock (Asset Management) liabilities winds down more slowly in later years. These public sector bodies have now been included in 2011-12 outturns for the first time.

Table 1.4: Change in public sector net debt

	Per cent of GDP						
	Outturn	Forecast					
	2011-12	2012-13	2013-14	2014-15	2015-16	2016-17	2017-18
December forecast	66.4	74.7	76.8	79.0	79.9	79.2	77.3
March forecast	71.8	75.9	79.2	82.6	85.1	85.6	84.8
Change	**5.5**	**1.2**	**2.3**	**3.7**	**5.1**	**6.4**	**7.5**
of which:							
Change in nominal GDP[1]	0.4	1.0	1.3	1.5	1.8	2.0	2.2
Change in cash level of net debt	5.1	0.2	1.0	2.2	3.4	4.4	5.3
	£ billion						
December forecast	1025	1186	1270	1362	1442	1498	1534
March forecast	1104	1189	1286	1398	1502	1580	1637
Change in cash level of net debt	**78**	**3**	**17**	**36**	**60**	**82**	**103**
of which:							
Changes in net borrowing (ex. APF)	0	1	9	19	33	44	56
Auction price effects	0	2	5	12	17	23	28
Asset purchase facility	0	0	0	0	0	2	4
Financial transactions and other	79	1	3	6	10	13	15

[1] Non-seasonally-adjusted GDP centred end-March.

Performance against the fiscal targets

1.38 In the June 2010 Budget the Coalition Government set itself a medium-term fiscal mandate and a supplementary target, namely:

- to balance the cyclically-adjusted current budget (CACB) by the end of a rolling, five-year period, which is now 2017-18; and
- to see public sector net debt (PSND) falling as a share of GDP in 2015-16.

1.39 Our latest forecasts suggest that the Government has a greater than 50 per cent chance of meeting the fiscal mandate. In December we forecast that the CACB would be in surplus by 0.9 per cent of GDP in 2017-18. In the absence of the policy measures in the Budget, the expected surplus would have fallen to 0.5 per cent of GDP. The measures – which include a switch from current to capital spending that improves the current balance without affecting borrowing overall – take the expected surplus back up to 0.8 per cent of GDP.

1.40 The Budget policy measures also mean that we expect the CACB to be in surplus by 0.1 per cent of GDP in the previous mandate year, 2016-17. In the absence of the measures we would have forecast a deficit of 0.2 per cent of GDP, compared to the surplus of 0.4 per cent of GDP that we forecast in December.

1.41 PSND is forecast to rise to a peak of 85.6 per cent of GDP in 2016-17, rather than 79.9 per cent a year earlier as in December. Consequently, as in December, we do not believe that the Government is on course to hit the supplementary target – we expect PSND to rise by 2.4 per cent of GDP in the target year, up from an increase of 1 per cent of GDP in December.

1.42 In the absence of the Royal Mail and APF transfers, and the ONS decision last year to reclassify Bradford & Bingley and Northern Rock (Asset Management) as central government bodies, we would still have expected the Government to meet the mandate, but with 0.1 per cent of GDP less margin for error. We would also have expected the rise in PSND in 2015-16 to be 3.2 per cent of GDP rather than 2.4 per cent of GDP, thus breaching the supplementary target by a slightly wider margin.

1.43 There is considerable uncertainty around our central forecast, as there is around all fiscal forecasts. This reflects uncertainty both about the outlook for the economy and about the performance of revenues and spending for any given state of the economy. Given these uncertainties we probe the robustness of our central judgement in three ways:

- first, by looking at past forecast errors. If our central forecasts are as accurate as official forecasts were in the past, then there is a roughly 70 per cent probability that the CACB will be in balance or surplus in 2017-18 (as the mandate requires) and a roughly 50 per cent chance a year earlier;

- second, by looking at its sensitivity to varying key features of the economic forecast. The biggest risk to the achievement of the mandate is that we again need to revise down our estimates of future potential output, reducing the size of the output gap in the target year. If potential output was 1 per cent lower than in our central forecast in 2017-18, and the output gap therefore -1.1 per cent of potential rather than -2.1 per cent, then the Government would no longer be on course to balance the CACB in 2017-18. We would also expect the Government to miss the mandate if gilt yields increased by 150-200 basis points relative to our central forecast, assuming that this was not offset by higher interest and dividend receipts; and

- third, by looking at alternative economic scenarios. We examine the potential impact of a further 15 per cent depreciation of sterling, noting the that the impact on GDP could be positive or negative depending on the consequences for exports and inflation. In either event, given the particular parameters we choose, the Government would still be on course to meet the mandate, but to breach the supplementary target.