

## *Economic and fiscal outlook - March 2013*

### Weaker receipts halt fall in deficit

***Tax receipts are expected to be weaker over the next few years than we expected in December. As a result, public sector net borrowing will be broadly stable at around £120 billion last year, this year and next, after adjusting for recent policy decisions with a temporary effect on the headline deficit.***

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 GDP growth forecasts to 0.6 per cent this year and 1.8 per cent in 2014.

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.

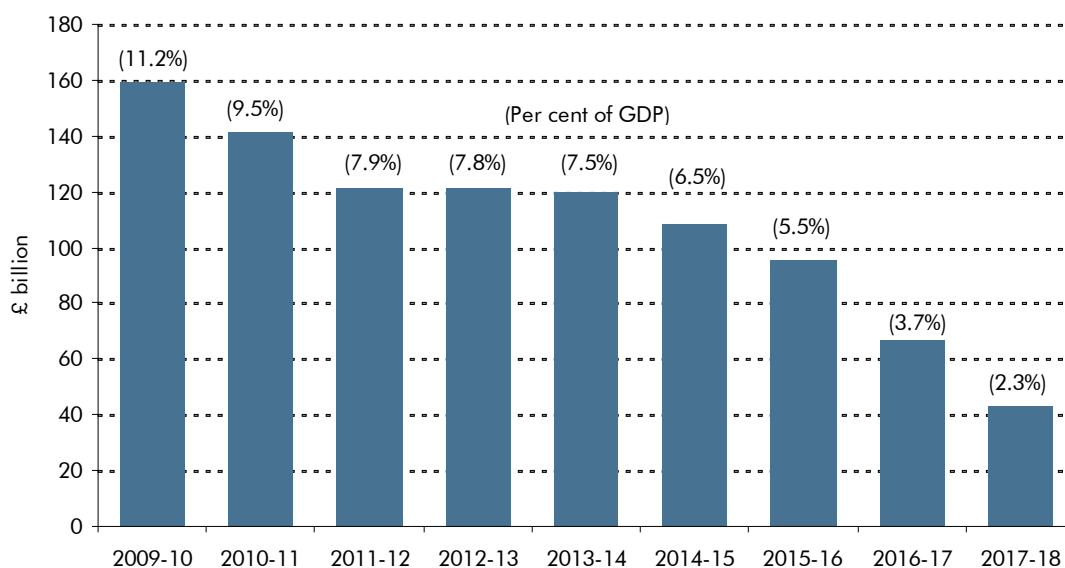
Chart A shows that public sector net borrowing (PSNB) – the gap between what the Government spends and raises in revenue – fell by a quarter between 2009-10 and 2011-12, thanks primarily to the tax increases and public spending cuts announced by this and the previous government. But, after adjusting 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.

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.

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



Source: OBR

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.

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.

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.

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.

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.

## Notes

1. The Office for Budget Responsibility is the UK's independent fiscal watchdog – responsible for producing forecasts for the economy and the public finances, judging progress towards the Government's fiscal targets, and reporting on long-term fiscal sustainability.
2. All of the documents published by the OBR today are available on our website at: [www.budgetresponsibility.independent.gov.uk](http://www.budgetresponsibility.independent.gov.uk)
3. The OBR has also announced today that the next *Fiscal sustainability report* will be published on 17 July 2013.
4. Where possible the OBR will release supplementary information on the *Economic and fiscal outlook* at 9.30am on 26 March, in response to requests received by noon on 22 March. We will release a list of the information to be published at 9.30am on 25 March. Subsequently, we will continue with our standard policy of releasing supplementary information monthly on the day of the HMT/ONS *Public Sector Finances* release.
5. Questions about the *Economic and fiscal outlook* should be sent to [OBRpress@obr.gsi.gov.uk](mailto:OBRpress@obr.gsi.gov.uk).

Table A: Overview of OBR March 2013 economy forecast

	Percentage change on a year earlier, unless otherwise stated						
	Outturn		Forecast <sup>1</sup>				
	2011	2012	2013	2014	2015	2016	2017
<b>Output at constant market prices</b>							
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
<b>Expenditure components of GDP at constant market prices</b>							
Household consumption <sup>2</sup>	-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 <sup>3</sup>	1.2	-0.8	0.1	0.1	0.1	0.1	0.1
<b>Inflation</b>							
CPI	4.5	2.8	2.8	2.4	2.1	2.0	2.0
<b>Labour market</b>							
Employment (millions)	29.2	29.5	29.8	29.9	30.1	30.3	30.5
Average earnings <sup>4</sup>	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
<b>Changes since December forecast</b>							
<b>Output at constant market prices</b>							
Gross domestic product (GDP)	0.0	0.3	-0.6	-0.3	0.0	0.0	0.0
GDP Level (2011=100) <sup>5</sup>	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
<b>Expenditure components of GDP at constant market prices</b>							
Household consumption <sup>2</sup>	-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 <sup>3</sup>	0.0	-0.1	-0.1	0.0	0.0	0.0	0.0
<b>Inflation</b>							
CPI	0.0	0.0	0.3	0.2	0.1	0.0	0.0
<b>Labour market</b>							
Employment (millions)	0.0	0.0	0.2	0.1	0.1	0.1	0.1
Average earnings <sup>4</sup>	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

<sup>1</sup> 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.

<sup>2</sup> Includes households and non-profit institutions serving households.

<sup>3</sup> Contribution to GDP growth, percentage points.

<sup>4</sup> Wages and salaries divided by employees.

<sup>5</sup> Per cent change since December.

**Table B: Overview of OBR March 2013 fiscal forecast**

	Per cent of GDP						
	Outturn	Forecast					
		2011-12	2012-13	2013-14	2014-15	2015-16	2016-17
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
<b>Fiscal mandate and supplementary target</b>							
Cyclically-adjusted surplus on current budget	-4.2	-4.0	-2.8	-1.7	-1.2	0.1	0.8
Public sector net debt <sup>1</sup>	71.8	75.9	79.2	82.6	85.1	85.6	84.8
<b>Changes since December forecast</b>							
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 <sup>1</sup>	5.5	1.2	2.3	3.7	5.1	6.4	7.5
<b>Underlying public sector net borrowing</b>							
PSNB excluding Royal Mail and APF transfers	7.9	7.8	7.5	6.5	5.5	3.7	2.3

<sup>1</sup> Debt at end March; GDP centred on end March.

**Table C: Public sector net borrowing: change since previous forecast**

	£ billion						
	Outturn	Forecast					
		2011-12	2012-13	2013-14	2014-15	2015-16	2016-17
<b>Public sector net borrowing excluding Royal Mail and APF transfers</b>							
December forecast	121.4	119.9	112	99	81	56	31
March forecast	121.0	120.9	120	108	96	67	43
<i>Change</i>	-0.4	1.0	8.3	9.9	14.3	11.4	11.8
<i>of which:</i>							
Receipts forecast <sup>1</sup>	-3.1	5.1	8.9	8.6	11.9	13.5	14.1
Expenditure forecast <sup>1</sup>	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 <sup>2</sup>	0.0	-3.4	1.0	0.5	0.0	0.0	0.0

<sup>1</sup>Excluding fiscally neutral switches including the reclassification of SLS transfers and changes in the proportion of tax credits treated as negative tax.

<sup>2</sup>Including as a result of action taken by the Government to reduce and/or delay expenditure.