Office for Budget Responsibility

July 2021 Fiscal risks report

The live event will begin at 11.00
Office for Budget Responsibility

July 2021 Fiscal risks report

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London
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Background on the Fiscal risks report

• OBR tasked with producing biennial *Fiscal risks report (FRR)* in 2015

• 2017 & 2019 FRRs took an ‘encyclopaedic’ approach to cataloguing 97 risks

• 2020 saw crystallisation of biggest fiscal risk in peacetime

• 2021 FRR shifts the focus to three potentially catastrophic risks
  • Coronavirus pandemic (Chapter 2)
  • Climate change (Chapter 3)
  • Cost of public debt (Chapter 4)
  • Update on 97 other risks (Chapter 5)

• Thanks OBR staff, HMT, Bank of England, Departments, & Think Tanks
Is the world becoming a riskier place?

Natural disasters

Source: The Emergency Events Database

Infectious disease outbreaks

Source: KF Smith et al. (2014)
Are governments more exposed to risks?

Public sector net debt

Source: ONS, OBR
Coronavirus economic impact

Change in real GDP in 2020 in advanced economies

Note: Based on IMF definition of advanced economies.
Source: IMF, ONS
Coronavirus fiscal rescue packages

Fiscal support by recipient for selected advanced economies

Source: IMF, OBR
Health system capacity in OECD countries

Indicators of health system capacity in OECD countries

- Health system capacity indicators such as acute care beds per 1,000, acute care bed vacancy rate, intensive care beds per 100,000, physicians per 1,000, nurses per 1,000, and CT scanners per 100,000.

Source: OECD, OBR
Coronavirus legacy spending pressures

Pandemic-related pressures on departmental resource spending

Source: OBR
Coronavirus economic legacy

Comparison of GDP forecasts

- Range of external forecasts
- OBR November 2020 upside scenario
- OBR November 2020 downside scenario
- Bank of England
- New independent forecasts
- Independent average
- OBR March 2021 forecast
- OBR March 2020 forecast
Global CO$_2$ emissions and temperatures

Global carbon dioxide emissions

Atmospheric concentrations of CO$_2$

UK contribution to global CO$_2$ emissions

UK share of global CO$_2$ emissions in 2016

CO$_2$ emissions relative to 1990

Source: Our World in Data
Contributions to cutting UK CO₂ emissions

Reduction in UK CO₂ emissions between 1990 and 2019

Source: BEIS
Whole economy cost of reaching net zero

Net cost of reaching net zero by sector

Source: CCC balanced net zero pathway
Fiscal costs of reaching net zero

Costs to the public sector of the transition to net zero

Source: CCC balanced net zero pathway, OBR
Fiscal opportunities on the way to net zero

Net revenue gains/losses from decarbonisation

Source: OBR
Net debt impact of reaching net zero

Early action scenario: difference in PSND from baseline

Source: OBR
Alternative fiscal scenarios toward net zero

Differences from baseline PSND under various scenarios

Source: OBR
Government debt and interest costs

Debt/GDP & Interest payments/GDP

Source: Bank of England, ONS, OBR
Accounting for lower interest rates

Contributions to the fall in global real interest rates

Composition of UK gilt investors

Holdings of UK government bonds

Source: DMO, ONS
Sensitivity to interest rate changes

Effective maturity of public sector liabilities

Rise in interest payments from a 1 ppt rise in interest rates

Source: Bank of England, Heriot-Watt/Faculty and Institute of Actuaries Gilt Database, ONS, OBR
Scenarios for the cost of public debt

Public sector net debt (% of GDP)

- Loss of investor confidence
- Higher interest rates
- Persistently higher inflation
- Temporary inflation shock
- Higher interest rates and growth
- Baseline

Source: ONS, OBR
Update on other fiscal risks

Changes to the 97 risks identified in the 2019 Fiscal risks report

Note: Darker shaded portions show the number of risks within each category that have been affected to some extent by the pandemic. Source: OBR
Lessons for dealing with catastrophic risks

• Catastrophic risks are real and may have become more frequent

• While it is difficult to predict when catastrophic risks will materialise, it is possible to anticipate their effects

• There are advantages in preventing or halting a process that involves rapidly escalating costs early

• When investing in risk prevention, governments have a tendency to ‘fight the last war’

• In the absence of perfect foresight, fiscal space may be the single most valuable risk management tool