November 2016 *Economic and Fiscal Outlook* Briefing

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Good afternoon ladies and gentlemen.

My name is Robert Chote, Chairman of the OBR, and I would like to welcome you to this briefing on our latest *Economic and Fiscal Outlook*.

I am going to take you through some of the highlights and then we will be very happy to answer your questions. The slides and my speaking notes will be available on our website after we finish.

[SLIDE] Let me start with the usual background.

The EFO contains our latest five-year forecasts for the economy and the public finances and an assessment of the Government's progress against its current and proposed fiscal and welfare spending targets.

The views expressed are the responsibility of the independent Budget Responsibility Committee. But we have relied on the hard work of the OBR's staff and numerous officials in other departments and agencies.

As usual, the forecast went through a number of iterations to reflect new judgements, new data and proposed policy measures. We provided the Chancellor with our final pre-scorecard forecast on November 9th.

We have come under no pressure to change any of our conclusions and we have been provided with all the forecast information we requested. However, at each EFO we also ask the Treasury to detail any newly created contingent liabilities that might pose a risk to the forecast. On this occasion we asked specifically whether any had been created by assurances provided to Nissan. But the Treasury declined to say.

[SLIDE] Now let me turn to a brief overview of the report.

The economy has not slowed as sharply as some forecasters feared in the wake of the referendum vote to leave the European Union. But it *has* slowed. And the outlook is weaker than at the time of the Budget.

We expect the quarterly growth rate of GDP to continue slowing into next year, as uncertainty over the UK's future trade and migration regime delays business investment and as the fall in the pound squeezes real consumer spending by pushing up inflation. But growth remains positive – we have not assumed more aggressive job shedding or a jump in precautionary saving, both of which pose downside risks if the road to Brexit is bumpy. Our growth forecast next year is 1.4 per cent – down from 2.2 per cent in March, but slightly above the outside average.

We also assume that the cumulative growth potential of the economy is weaker than we thought in March over the forecast as a whole. This is largely because weaker business investment depresses trend productivity growth by slowing capital deepening.

Potential GDP growth is also depressed by a weaker outlook for net inward migration, which we would have increased in this forecast – but for the referendum vote – because of the continued strength of recent inflows. By the end of the forecast the economy is between 2 and 2½ per cent smaller than it would have been on our March forecast, with that extra inward migration, but about 10 per cent bigger than it is today.

The outlook for the public finances is also weaker than we expected in March. Borrowing was already overshooting our forecast ahead of the referendum, thanks mostly to weak income tax receipts and higher local authority spending. Looking forward, the income tax shortfall increases as the downward revision to our trend productivity forecast slows the growth of average earnings. Ignoring statistical classification changes, and before taking account of the Chancellor's Autumn Statement policy measures, we have revised up our deficit forecast by £18 billion in 2020-21. The main drivers are weaker income tax receipts, plus upward revisions to our forecasts for local authority spending and the cost of incapacity and disability benefits. This more than offsets lower debt interest costs and the strength of some other tax receipts.

Confronted by a near-term economic slowdown and a structural deterioration in the public finances, the Chancellor has opted neither for a big near-term fiscal stimulus nor for more austerity over the medium term. Instead he has proposed moving to a much looser fiscal target that would give him scope for around £56 billion more structural borrowing in 2020-21 than George Osborne was aiming for in March.

Our forecast revisions have used up about £20 billion of this extra room for manoeuvre and the Chancellor has chosen to give away almost another £10 billion, mostly in higher spending on investment. But this leaves around £27 billion to spare, in case the structural outlook for the public finances turns out to be worse than we think or if he wants to announce more giveaways. The mandate also allows him to borrow more if the temporary slowdown in the economy is more severe.

But if Mr Hammond does need (or decide) to use some of this margin, his overarching objective of balancing the budget as early as possible in the next Parliament will be even more difficult to achieve than it already is, given pressures from pension and other age-related spending.

[SLIDE] So now let me turn to the forecast in more detail and begin by explaining how we have tried to incorporate the impact of Brexit.

As you know, Parliament requires the OBR to produce its forecasts on the basis of current Government policy and not to look at alternatives. With the Brexit negotiations looming, this is far from straightforward.

Quite properly, we have been given no information about the Government's strategy or expectations for the negotiations that is not already in the public domain. And given the uncertainty surrounding the choices and trade-offs that the Government may have to make – and the consequences of different outcomes – we have not attempted to predict the precise end-point of the negotiations. Instead we have made a set of broad-brush judgements – consistent with a variety of outcomes – that we can revisit in future forecasts. Specifically we have assumed for now:

- First, that the UK leaves the EU in April 2019;

- Second, that negotiation of new trading arrangements inside and outside the EU will slow import and export growth for the next 10 years. As a result, import and export volumes are about 8 per cent lower by the end of the forecast than they otherwise would be;

- Third, that the UK will adopt a tighter migration regime and become less attractive as a destination. Our net inward migration assumption is unchanged since March, but we would have increased it by about 80,000 a year in the absence of the referendum, taking it closer to the recent outturn figures;

- Fourth, that any reduction in our expenditure transfers to the EU will be recycled into higher domestic public spending. This amounts to around £13 billion a year by 2020-21; and

- Fifth, that there will be no change to the structure or management of tax systems with common EU rules, such as VAT.

We have not made any specific assumption about 'passporting' for financial services, but we do assume that profits and salaries in the financial sector suffer slightly more than the rest of the economy.

So, on that basis, let me turn now to the outlook for economic growth.

[SLIDE] This chart shows the annual growth rates for real GDP that we forecast in March. [SLIDE] And here are the rates that we forecast today. There are significant downward revisions in 2017 and 2018, but little change thereafter. [SLIDE] Growth in per capita GDP is weaker than headline growth because the population increases over the forecast.

[SLIDE] The revisions are actually more complicated than this annual picture suggests, which becomes clearer [SLIDE] if you look at growth quarter-on-quarter. You can see here that we expect growth on this basis to continue slowing into next year, reaching a trough of about 0.2 per cent a quarter. It then bounces back before settling down at a slightly slower pace in the medium term than we assumed in March.

[SLIDE] Two main judgements underpin this profile.

First, we assume that growth slows in the near-term as uncertainty regarding the future trade regime – and perhaps the future of migration and other policies – leads firms to delay or cancel some investment. We have seen some evidence of that already, even before the referendum. Moving into next year, this is exacerbated by a squeeze on real consumer spending as the fall in the pound since the referendum pushes up import prices and CPI inflation. These two negative effects are partially offset by a near-term boost to GDP from stronger net trade volumes, as the weaker pound encourages exports and discourages imports and as weaker consumer and investment spending mean less demand for imports.

Second, we assume that potential growth in productivity – the amount of output that each worker can produce each hour – is weaker, thanks largely to weaker investment. This reduces the amount of growth the economy can sustain without pressure on inflation. The Treasury – in its pre-referendum analysis – also revised trend productivity growth down as a direct result of lower trade intensity. For now, like the National Institute, we have not. This link is not terribly well understood.

[SLIDE] We can see the impact of these two judgements together by looking at our forecasts for the actual level of GDP and the potential level that could be sustained without ongoing inflationary pressure.

This chart shows our forecasts for March and [SLIDE] this chart our forecasts today. You can see that the path of potential output to which the economy eventually returns is lower, but that in the near term we also fall further below that path than we thought we would in March.

This creates scope for a period of above-trend growth as that spare capacity is used up and the ‘output gap’ closes. It is that temporary period of above-trend growth that explains why we have not revised down the annual growth rate towards the end of our forecast even though the quarterly growth rate is weaker when it eventually settles down.

[SLIDE] The net result of this change to the growth profile is that we expect the level of activity in the economy to be about 1½ per cent lower at the end of the forecast than we thought in March. This chart shows how that revision is driven initially by lower investment and then by weaker real consumer spending, partly offset by the boost from net trade. [SLIDE] This shortfall rises to 2.3 per cent if we measure it against what our March forecast would have looked like if we had increased our net inward migration assumption to reflect recent higher inflows.

[SLIDE] This chart compares our forecast for the level of GDP with [SLIDE] the Bank of England's November *Inflation report* and the average of outside forecasts. We are slightly more optimistic than both as regards the growth rate, but in the Bank's case this is partially offset in level terms by their assumption that past GDP data will be revised up.

[SLIDE] As I mentioned a moment ago, one reason that we expect growth to slow is that we have revised up our inflation forecast, so that consumers can buy less with each pound in their pocket. This chart shows that we now expect CPI inflation to rise to a peak of around 2.6 per cent in the spring of 2018. Sterling is around 13 per cent weaker across the forecast than in March, thanks to its recent decline. We base our forecast on a rule of thumb that 80 per cent of the fall in the pound will feed into import prices and 20 per cent of that feeds through to consumer prices. Inflation is also pushed up by higher oil prices, but down by the near-term economic slowdown.

[SLIDE] With weaker productivity growth pulling down growth in average earnings – and the fall in the pound pushing up inflation – consumers will feel the squeeze. This chart shows our forecasts for average earnings growth and consumer price inflation in March, [SLIDE] and the same forecasts today. As you can see, growth in real wages stalls next year.

[SLIDE] When you think about movements in real wages, it is often helpful to think about the different perspectives of employers and employees. Employers care about the real product wage, the level of wages relative to the price of the output they sell. Employees care about the real consumption wage, the level of wages relative to the price of the things they buy. Both are lower than in March, but the real consumption wage more so. Employees end up about 3 per cent poorer on this measure than we expected in March – they will earn less because they are less productive and each pound they earn will go less far.

Turning to the external picture, the outlook for trade and the current account is affected by the fall in the pound, a weaker outlook for domestic demand and the slowdown in import and export growth likely as we move to new trade regimes with the EU and other countries.

[SLIDE] This chart shows our forecasts for import and export volumes in March [SLIDE] and today. You can see that both rise less quickly, as we move to new trade arrangements, but that the gap between them is smaller as the fall in sterling encourages exports and discourages imports, delivering a boost to GDP via the net trade contribution.

Look at the same comparison for values, rather than volumes, [SLIDE] [SLIDE] we find the opposite story. A fall in export prices relative to import prices outweighs the change in volumes – giving a wider gap between the two and a bigger trade deficit in value terms.

[SLIDE] So what does this mean for the current account, which last year recorded its biggest deficit as a share of GDP since the 18th century?

[SLIDE] This table shows that the deficit back in 2015 was much bigger than we expected: up from £80 to £100 billion – because the deficit on flows of investment income deteriorated again at the end of the year. [SLIDE] We expect the investment income deficit to be even worse relative to our March forecast this year, but then to narrow thanks in part to the fall in the pound, which boosts the value of our overseas earnings. [SLIDE] As we saw in the previous charts, the trade deficit is worse throughout the forecast in value terms. [SLIDE] On balance, by the end of the forecast, we expect a slightly lower current account deficit overall than in March.

[SLIDE] So now let us turn to the outlook for the public finances and begin by looking at what the changes to our economy forecast imply for the main economic determinants of our fiscal forecast.

As this table shows, weaker potential output growth implies weaker real GDP growth – we assume that the Bank of England keeps demand in the economy broadly in line with potential supply to keep inflation stable. Add in our revisions to whole economy inflation and that implies weaker nominal GDP growth. We can then split that out into different categories of income and spending. Weaker growth in wages and salaries, profits and consumer spending all imply weaker growth in tax revenues. Our forecast for business investment is much weaker than in March, but this is actually positive for tax revenues as it implies less use of capital allowances. But that is only a small offset.

[SLIDE] Turning to the public finances themselves, this chart shows our March forecast for public sector net borrowing – the headline budget deficit – and [SLIDE] our forecast today. As you can see, the budget balance is weaker every year than we forecast in March and we no longer return to surplus by the end of the Parliament. We now forecast a deficit of £68.2 billion this year, up from £55.5 billion. And we forecast a deficit of £20.7 billion in 2020-21, compared to a surplus of £11 billion.

[SLIDE] These numbers show the deterioration in the forecast each year, so [SLIDE] now let's break this down into its various components.

[SLIDE] The first contribution comes from classification decisions by the Office for National Statistics. This includes moving Welsh, Scottish and Northern Irish housing associations into the public sector, to join their English counterparts. More significantly, it includes moving the recording of corporation tax receipts from a cash basis (when they reach HMRC) to an accrual basis (closer to when the profits were made). This means that the measure announced by George Osborne to make large companies pay their CT bills sooner no longer generates a big one-off boost to recorded revenues in 2019-20 and 2020-21.

[SLIDE] The second contribution comes from the changes to our underlying pre-measures forecast. As we have heard, this is dominated by a downward revision to our income tax forecast, as weaker productivity growth implies weaker earnings growth.

[SLIDE] Finally we have the contribution of the policy measures that the Chancellor announced today. These amount to a consistent giveaway across the forecast, rising from £2.5 billion next year to £9.6 billion in 2020-21. We will look at these in more detail in a minute.

But returning to the underlying forecast changes, an obvious question is how much of this has to do with Brexit and how much with other factors. That is not straightforward to answer. We cannot be sure how far economic and fiscal developments in the run-up to the referendum were a consequence of the uncertainty it created and people's expectations of the results. And, looking forward, we can be no surer how things would have turned out in the absence of the referendum result than in the wake of it.

[SLIDE] Nonetheless, we have had a crack at answering this question and you can see the results here. The non-Brexit-related effects dominate this year and diminish over time. The Brexit-related effects are smaller this year and then increase over time. Let us look at the two in more detail, and you can read more in Annex B of the report.

[SLIDE] This table summarises what we think of as the predominantly non-Brexit changes in our forecast. [SLIDE] These are dominated at the outset by the shortfall in income tax and the unexpected strength of local authority spending that we saw last year and this year to date.

[SLIDE] This is increasingly offset by the improvement in the budget balance that we would have predicted if we had increased our net inward migration assumption, as that would have boosted tax revenue by more than it would have raised spending. [SLIDE] Smaller effects include the first upward revision to our North Sea revenue forecast since 2011 – thanks to higher dollar oil prices – and further upward revisions to the expected cost of incapacity and disability benefits.

[SLIDE] Turning to the Brexit-related effects, borrowing is pushed higher primarily by [SLIDE] lower trend productivity growth and lower net inward migration, both of which primarily reduce income tax. Together these cost more than £13 billion a year by 2020-21. [SLIDE] The effect of the temporary cyclical slowdown in the economy – as activity falls below potential but then returns back to it – increases to a peak of £8.6 billion in 2018-19 and then declines thereafter. [SLIDE] Higher inflation – specifically that part of it that reflects the weaker pound – pushes up the deficit via debt interest, public sector pension costs, welfare uprating and the cost of indexing tax allowances and thresholds, partly offset by higher excise duties. [SLIDE] These factors pushing up the deficit are partly offset by a fall in debt interest costs, via lower market and policy interest rates and the effect of the extra gilts bought by the Bank of England. Other factors also lower the deficit on balance.

[SLIDE] Taking the Brexit- and non-Brexit-related forecast changes together, our pre-measures forecast for the budget deficit has increased by 0.8 per cent of GDP cumulatively across the five-year horizon – with the Brexit-related changes accounting for about 0.6 of that. This is the third largest revision we have made in 14 forecasts, exceeded only by the upward revisions in November 2011 and December 2012.

In previous Budgets and Autumn statements, Chancellors have tended to respond to a deterioration in the medium-term outlook for the budget deficit by announcing spending cuts or tax increases to partially offset it. Mr Hammond is different. Confronted by a structural deterioration in the deficit of 0.9 per cent of GDP in 2020-21, he has chosen to increase borrowing by a further 0.4 per cent of GDP, as his proposed new fiscal mandate allows him to do.

[SLIDE] So let us look at his policy package in a bit more detail.

As I mentioned earlier, his ‘giveaway’ rises from £2.5 billion next year to £9.6 billion in 2020-21, dropping back in the last year of the forecast.

[SLIDE] The largest element is additional capital spending, which rises almost £6 billion by the end of the forecast – thanks to the Chancellor’s new National Productivity Investment Fund. The Government is actually planning an even bigger increase, but we assume from past experience that it won’t spend quite as quickly as it hopes. [SLIDE] Nonetheless, this would lift public sector net investment from 2.1 to 2.3 per cent of GDP, the highest since it spiked at the time of the financial crisis.

[SLIDE] The Chancellor has delivered a much smaller boost to day-to-day departmental spending. Back in March George Osborne promised to deliver £3.5 billion of unspecified efficiency savings in 2019-20. Mr Hammond will spend £1 billion of them on unspecified ‘priority areas’.

[SLIDE] As this chart shows, planned percentage changes in real capital and current departmental spending per head have changed significantly between the end of the Coalition, [SLIDE] the end of the Cameron Government, and [SLIDE] today. Current spending faces a 7 per cent cut, much reduced from the end of the Coalition, while capital spending sees a 37 per cent rise, much increased since the end of the Coalition. Of course the latter starts from a much smaller base.

[SLIDE] Returning to the policy package as a whole, the increase in current and capital spending is in contrast to a [SLIDE] small net tax increase. [SLIDE] The largest tax cut was also the most predictable – the freezing of fuel duty next April for the sixth year running. But in April 2018 it is going to go up in line with inflation – honest. The largest tax increase was for insurance premium tax. This is also becoming a habit. It will have been increased three times in 20 months, doubling overall.

[SLIDE] Welfare measures are a giveaway across the forecast. This largely reflects the Government's swift abandonment of the Personal Independence Payment cut announced back in the March Budget. But Mr Hammond has also decided to reduce the rate at which the new Universal Credit is withdrawn from people as their incomes rise. The rollout of Universal Credit has also been delayed once again, which costs money as the savings it will eventually make take longer to appear.

[SLIDE] To what extent does the policy package affect our forecast for the economy? The short answer is "not much". The fiscal loosening boosts GDP fractionally in 2017-18, while the net effect of the fuel duty freeze and the insurance premium tax increase marginally reduces inflation in the same year. Additional funds for building on public sector land should increase housebuilding by about 10,000 over the forecast, but measures affecting housing associations should cut it by 13,000. These figures are net effects on our forecast, so smaller than some of the numbers you may hear from the Government.

[SLIDE] Now let me turn to the Government's fiscal and welfare spending targets. Mr Hammond has inherited three targets from Mr Osborne, all of which he is on course to miss. And he has proposed three new targets, all of which he is on course to hit.

[SLIDE] The current fiscal mandate requires the Government to run a budget surplus in 2019-20 and thereafter, absent a bigger slowdown in the economy than we forecast today.

We forecast in March that Mr Osborne was on course to meet this target with £10 billion to spare. But the combination of the new approach to recording corporation tax revenues, his successor's fiscal giveaway and the revisions to our underlying forecast mean that we now expect the mandate to be missed by more than £20 billion. [SLIDE] But this is not a completely lost cause. Such are the uncertainties around the net borrowing forecast at that time horizon, there is still a 35 per cent chance of the target being hit on past forecast performance.

[SLIDE] Mr Hammond's proposed new fiscal mandate is much less demanding. It requires the structural budget deficit (in other words that part of government borrowing that is not a result of temporary weakness in the economy) to lie below 2 per cent of GDP by 2020-21. Last year the structural deficit stood at 3.8 per cent of GDP and so meeting the new mandate requires it to roughly halve over this Parliament.

We expect this target to be met with 1.2 per cent of GDP to spare, implying a 65 per cent chance of success on past forecast performance. On current policy, we expect the structural deficit to shrink by 3 per cent of GDP between 2015-16 and the mandate year. Two thirds of the improvement comes from lower spending, with cuts in welfare and day-to-day departmental spending more than offsetting the increase in capital as a share of GDP. One third comes from higher receipts, thanks largely to policy measures boosting National Insurance and self-assessment receipts, plus the introduction of the apprenticeship levy.

[SLIDE] So how much room for manoeuvre does the proposed fiscal mandate provide? Back in March George Osborne was aiming for a structural budget surplus of 0.5 per cent of GDP in 2020-21, but the new mandate allows Mr Hammond a deficit of 2 per cent of GDP. That 2.5 per cent of GDP difference is equivalent to around £56 billion.

[SLIDE] The change in our forecast absorbs 0.9 per cent of GDP and [SLIDE] the Chancellor has given away another 0.4 per cent with his Autumn Statement measures. [SLIDE] But that still leaves room for another 1.2 per cent of GDP of structural borrowing, equivalent to around £27 billion, just in case the outlook for the public finances is worse than we currently think or if the Chancellor wishes to pay for further giveaways. This is not an insignificant margin, but you can see from the scenarios that we set out in Chapter 5 that if productivity growth remains as weak as it has been in recent years then that would be sufficient to wipe it out.

The outlook for productivity growth remains the biggest and most important uncertainty around our fiscal projections, just as it has been in each of our previous forecasts. For all the attention it will receive now, Brexit has not supplanted this uncertainty. It has simply added to it.

[SLIDE] In addition to the new fiscal mandate, the Chancellor's draft *Charter* has also set out a new overarching objective for fiscal policy, namely to balance the budget as early as possible in the next Parliament. That will be quite a challenge, especially if he needs or decides to borrow more during this Parliament. For one thing, he is not currently planning a significant structural fiscal tightening beyond 2019-20.

Our latest long-term Fiscal sustainability report also suggests that there will be pressure to increase age-related spending by about 0.8 per cent of GDP between 2020-21 and 2025-26. This is largely because the population is getting older, but it is also because increases in the state pension age will not restrain pension spending during the next Parliament in the way that they do in this one. The number of people receiving the state pension is set to fall by 2.6 per cent during this Parliament, but to rise by 9.1 per cent during the next.

[SLIDE] Now let me turn from the Government's borrowing targets to its debt targets. The current 'supplementary target' requires debt to fall as a share of GDP each year to 2019-20 (and implicitly beyond). Mr Hammond's proposed replacement requires it only to fall in 2020-21.

[SLIDE] This chart shows our forecasts for public sector net debt in March and today. In March we thought it had peaked in 2015-16 at 83.7 per cent of GDP. Now we expect it to peak at 90.2 per cent of GDP in 2017-18. You can see from the chart that changes to our nominal GDP forecast have made relatively little difference. [SLIDE] The rise in the debt ratio since March reflects upward revisions to our cash debt forecasts, which are in excess of £200 billion by the end of the forecast.

[SLIDE] The upward revisions to our underlying forecast for the budget deficit increase net debt by £100 billion by 2020-21, while the Chancellor's net giveaway adds another £26 billion. [SLIDE] But the biggest increase – especially over the next two years – reflects the way in which the Bank of England's monetary policy package in August is recorded in the figures. The public sector is in effect borrowing money so that the Bank can buy gilts and corporate bonds and support bank lending through the Term Funding Scheme. But the figures do not fully net off the value of the assets that the Bank is buying, because the statisticians deem the corporate bonds and TFS loans to be illiquid.

[SLIDE] For this reason, the Treasury has asked us to forecast two new balance sheet measures in this EFO, one that excludes the Bank of England and one that includes a broader range of assets. Both rise less sharply than net debt on our provisional projections.

[SLIDE] Net debt is also being pushed slightly higher by a fall in the expected proceeds from financial asset sales. Lower share prices for Lloyds and RBS alone would have reduced expected proceeds by £6 billion by the end of the forecast. More importantly, the Government has put further sales of RBS shares on hold for the time being. This adds another £16 billion to net debt by 2020-21.

But, as always, it is important to remember that when the Government sells an asset for roughly what it is worth, this does not affect the underlying health of the public finances even if it reduces net debt. Indeed, it would not reduce public sector net financial liabilities – or PSNFL – the new broad-based balance sheet measure.

[SLIDE] The Government's third and final target is the welfare cap, which sets a cash limit on benefit and tax credit spending, excluding the state pension and payments linked to the ups and downs of the economy.

The current welfare cap was set in July 2015 at the level of our forecast at the time, with a 2 per cent margin to accommodate forecast revisions, but not policy giveaways. The cap was already being breached just four months later – thanks to disappointing savings from incapacity and disability benefit reforms, plus the cost of abandoning the cuts to tax credits announced in the July 2015 Budget.

[SLIDE] The expected breach is even bigger now, thanks to further upward revisions to the cost of incapacity and disability benefits, the abandonment of the March 2016 cut in Personal Independence Payment entitlements, and the decisions in this Autumn Statement to cut the taper rate and once again delay the roll-out of Universal Credit. By 2020-21 we expect welfare spending to be £8 billion above the cap and still almost £6 billion above it when you include the 2 per cent margin.

[SLIDE] The new proposed cap is higher, includes more margin for error and will be assessed only once a Parliament rather than every year.

The new cap is, in effect, 3 per cent above our current forecast in the target year of 2021-22 at almost £130 billion. Back in July 2015 George Osborne reduced his cap by about £12 billion, locking in the welfare cuts that he announced in that Budget. A few of those cuts have been abandoned, several of the Government's welfare reforms are saving less money than it hoped, and Mr Hammond has decided to taper Universal Credit less sharply. To accommodate this – and to allow space for future forecast and policy changes – Mr Hammond has in effect reversed the tightening of the cap that was announced by Mr Osborne.

[SLIDE] Finally, on that transformative note, let me conclude.

The outlook for the economy and the public finances is weaker than we thought in March. Having taken account as best we can of the possible implications of Brexit, our forecasts for GDP growth are somewhat more optimistic than those of the Bank of England, the external average and the Treasury's pre-referendum analysis. But there is even more uncertainty around them than usual, as well as obvious downside risks.

Weaker growth means weaker revenues and higher government borrowing, compounded by a deficit overshoot already this year.

Confronted by a near-term economic slowdown and a structural deterioration in the public finances, the Chancellor has opted neither for a big near-term fiscal stimulus nor for a ratcheting up of austerity over the medium term. He has announced a significant loosening of the Government's main fiscal target, sufficient to absorb our forecast revisions and pay for higher spending on public investment, while leaving half left over to absorb future bad news or further giveaways.

That room for manoeuvre may be necessary. Our forecast continues to rely on an improvement in the weak performance of productivity growth that we have seen in recent years and in many countries. And the fiscal costs of an ageing population are becoming increasingly apparent.